PennState

Audited Financial Statements

The Pennsylvania State University

Fiscal Year Ended June 30, 2017

T H E   P E N N S Y L V A N I A   S T A T E   U N I V E R S I T Y

UNIVERSITY OFFICERS

as of October 20, 2017

ERIC J. BARRON
President

STEPHEN S. DUNHAM
Vice President and General Counsel

DAVID J. GRAY
Senior Vice President for
Finance and Business/Treasurer

A. CRAIG HILLEMEIER
Dean, Penn State College of Medicine;
Chief Executive Officer, Penn State Health; and
Senior Vice President for Health Affairs,
Penn State University

NICHOLAS P. JONES
Executive Vice President
and Provost

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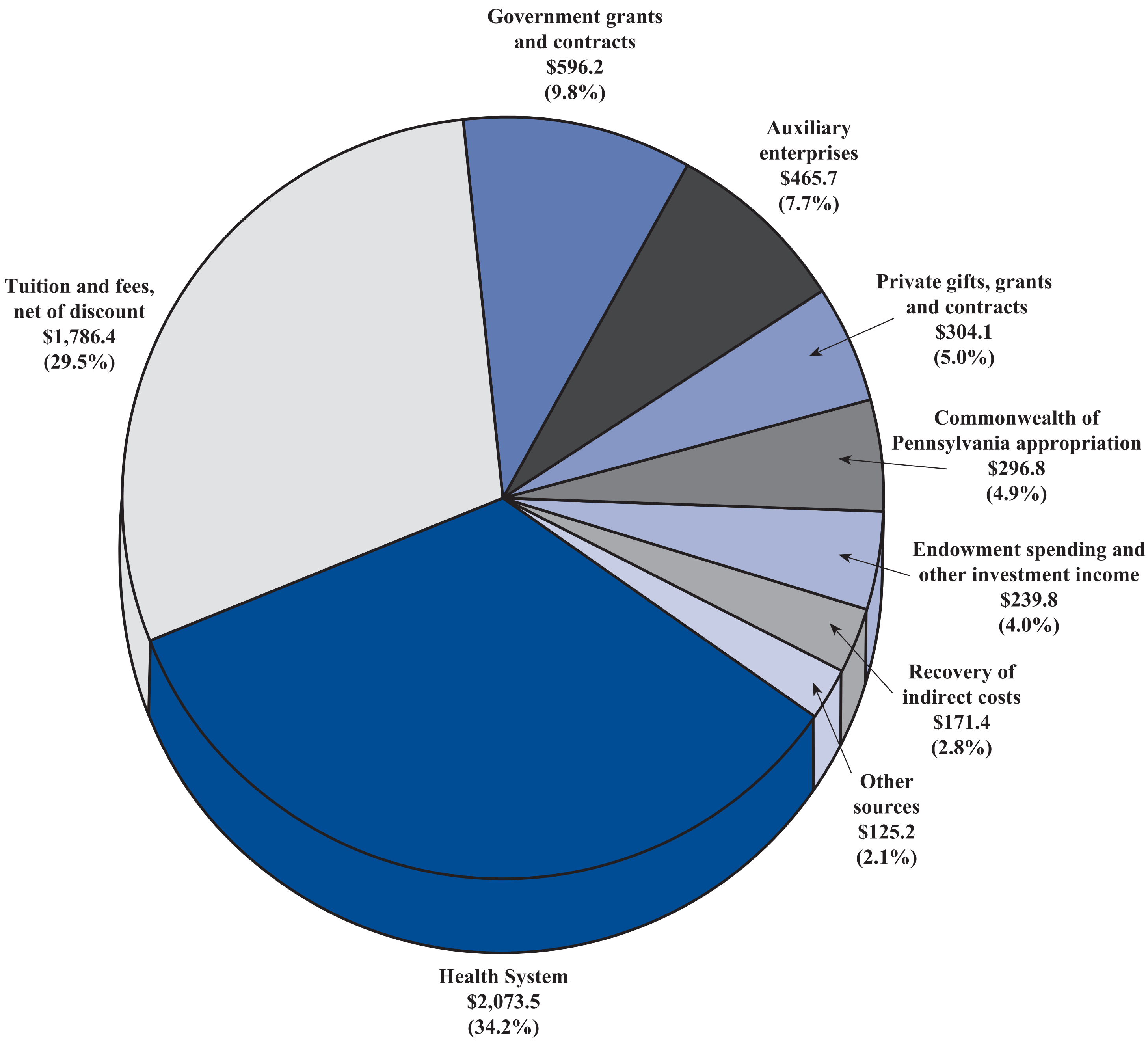
OPERATING REVENUES BY SOURCE ($6.1 billion)

For the Year Ended June 30, 2017

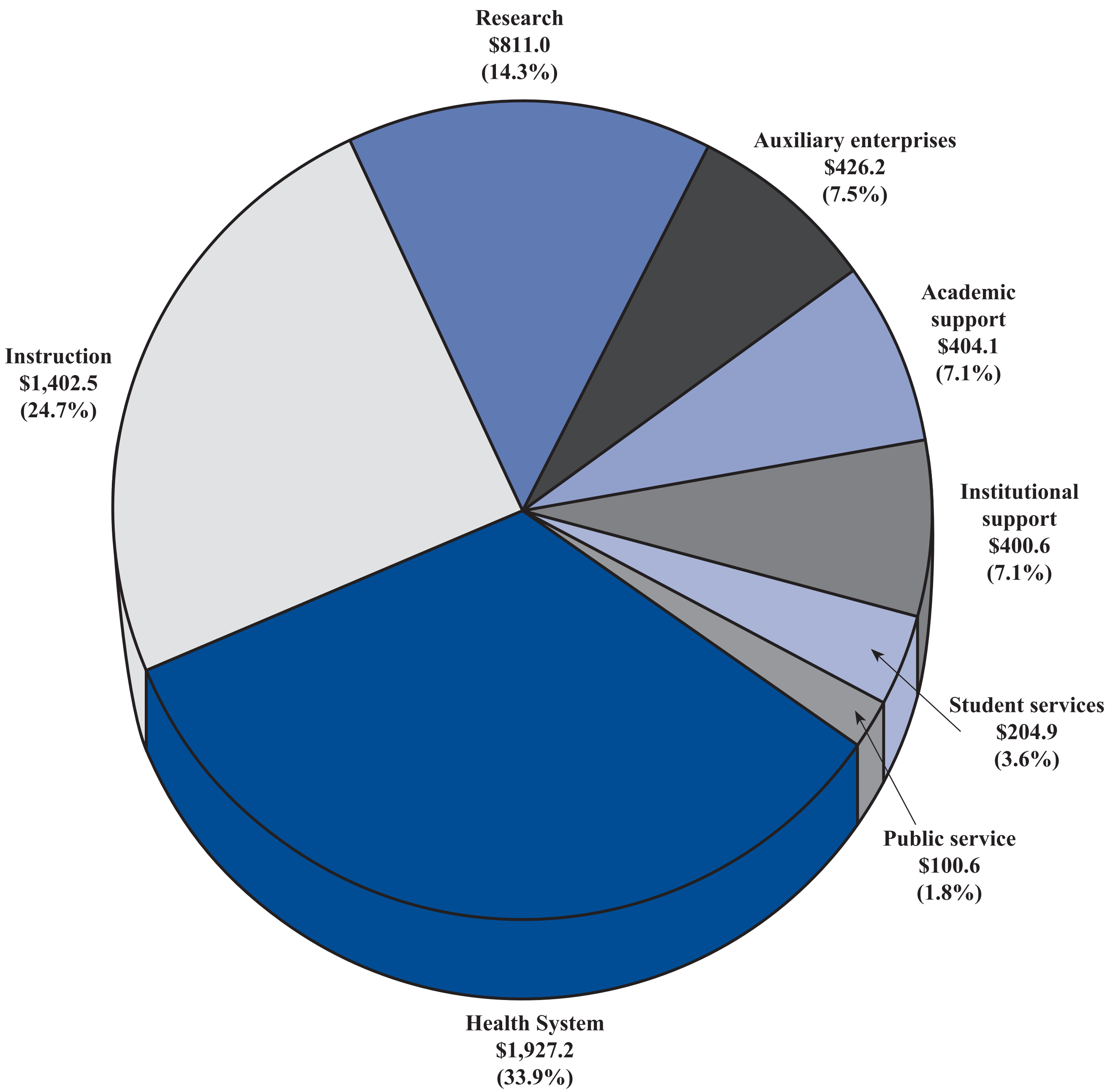
($ in millions)



OPERATING EXPENSES BY FUNCTION ($5.7 billion)

For the Year Ended June 30, 2017

($ in millions)



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PennState

Office of the Corporate Controller

The Pennsylvania State University
408 Old Main
University Park, PA 16802-1505
(814) 865-1355
FAX: (814) 863-0701

October 20, 2017

Dr. Eric J. Barron, President
The Pennsylvania State University
201 Old Main
University Park, PA 16802

Dear Dr. Barron:

The audited consolidated financial statements of The Pennsylvania State University and subsidiaries (the "University") for the fiscal years ended June 30, 2017 and 2016 are presented on the accompanying pages. These financial statements represent a complete and permanent record of the finances of the University as of and for the years then ended.

These financial statements have been audited by Deloitte & Touche LLP, independent auditors, and their report has been made a part of this record.

Respectfully submitted,

Joseph J. Doncsecz
Associate Vice President for Finance and Corporate Controller

David J. Gray
Senior Vice President for Finance and Business, and Treasurer

Deloitte & Touche LLP
1700 Market Street
Philadelphia, PA 19103-3984
USA

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of The Pennsylvania State University
University Park, Pennsylvania

We have audited the accompanying consolidated financial statements of The Pennsylvania State University and its subsidiaries (the "University"), which comprise the consolidated statements of financial position as of June 30, 2017 and 2016, 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 Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the 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 auditor's 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 University'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 University'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 as of June 30, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

October 20, 2017

THE PENNSYLVANIA STATE UNIVERSITY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
ASSETS
JUNE 30, 2017 AND 2016
(in thousands)

	June 30, 2017	June 30, 2016
Current assets:		
Cash and cash equivalents	$ 1,761,703	$ 1,395,514
Short-term investments	325,758	371,363
Deposits held by bond trustees	138,954	109,739
Deposits held for others	37,031	10,240
Accounts receivable, net of allowances of $88,731 and $83,942	542,603	496,100
Contributions receivable, net	60,893	54,565
Loans to students, net of allowances of $570 and $419	9,461	9,304
Inventories	48,152	42,472
Prepaid expenses and other assets	105,807	110,995
Total current assets	3,030,362	2,600,292
Noncurrent assets:		
Deposits held by bond trustees	40,000	21,348
Contributions receivable, net	140,165	124,988
Loans to students, net of allowances of $2,548 and $2,107	49,121	51,602
Total investment in plant, net	4,921,412	4,590,311
Beneficial interest in perpetual trusts	19,854	14,558
Investments	5,716,986	5,279,950
Other assets	112,391	97,932
Total noncurrent assets	10,999,929	10,180,689
Total assets	$14,030,291	$12,780,981

See notes to consolidated financial statements.

THE PENNSYLVANIA STATE UNIVERSITY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
LIABILITIES AND NET ASSETS
JUNE 30, 2017 AND 2016
(in thousands)

	June 30, 2017	June 30, 2016
Current liabilities:		
Accounts payable and other accrued expenses	$ 689,885	$ 596,027
Deferred revenue	341,261	314,682
Long-term debt	49,432	40,729
Present value of annuities payable	6,574	6,361
Accrued postretirement benefits	56,466	52,665
Total current liabilities	1,143,618	1,010,464
Noncurrent liabilities:		
Deposits held in custody for others	32,724	35,710
Deferred revenue	1,218	1,477
Long-term debt	1,419,961	1,130,547
Present value of annuities payable	51,496	47,498
Accrued postretirement benefits	2,261,996	2,095,857
Refundable United States Government student loans	46,713	47,687
Other liabilities	230,067	204,797
Total noncurrent liabilities	4,044,175	3,563,573
Total liabilities	5,187,793	4,574,037
Net assets:		
Unrestricted -		
Undesignated	1,692	1,658
Designated for specific purposes	3,350,691	3,144,389
Net investment in plant	3,169,239	2,987,299
Total unrestricted - The Pennsylvania State University	6,521,622	6,133,346
Noncontrolling interest	4,609	3,687
Total unrestricted	6,526,231	6,137,033
Temporarily restricted	708,103	551,073
Permanently restricted	1,608,164	1,518,838
Total net assets	8,842,498	8,206,944
Total liabilities and net assets	$14,030,291	$12,780,981

See notes to consolidated financial statements.

THE PENNSYLVANIA STATE UNIVERSITY
CONSOLIDATED STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2017
(in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues and other support:				
Tuition and fees, net of discounts of $205,002	$ 1,786,430	$ -	$ -	$ 1,786,430
Commonwealth of Pennsylvania -				
Appropriations	296,764	-	-	296,764
Special contracts	68,933	-	-	68,933
Department of General Services projects	47,500	-	-	47,500
United States Government grants and contracts	479,717	-	-	479,717
Private grants and contracts	216,596	-	-	216,596
Gifts and pledges	62,906	24,631	-	87,537
Endowment spending	98,521	-	-	98,521
Other investment income	140,235	1,046	-	141,281
Sales and services of educational activities	84,508	-	-	84,508
Recovery of indirect costs	171,442	-	-	171,442
Auxiliary enterprises	465,716	-	-	465,716
Health System revenue, net of provision for bad debts of $46,251	2,073,496	-	-	2,073,496
Other sources	40,628	-	-	40,628
Net assets released from restrictions	2,859	(2,859)	-	-
Total operating revenues and other support	6,036,251	22,818	-	6,059,069
Operating expenses:				
Educational and general -				
Instruction	1,402,451	-	-	1,402,451
Research	810,985	-	-	810,985
Public service	100,573	-	-	100,573
Academic support	404,098	-	-	404,098
Student services	204,943	-	-	204,943
Institutional support	400,646	-	-	400,646
Total educational and general	3,323,696	-	-	3,323,696
Auxiliary enterprises	426,204	-	-	426,204
Health System expense	1,927,155	-	-	1,927,155
Total operating expenses	5,677,055	-	-	5,677,055
Increase in net assets from operating activities	359,196	22,818	-	382,014
Nonoperating activities:				
Gifts and pledges	-	-	83,529	83,529
Current year investment returns	160,882	136,561	9,056	306,499
Endowment appreciation utilized	(75,871)	-	-	(75,871)
Changes in funds held by others in perpetuity	-	-	5,204	5,204
Write-offs and disposals of assets	(4,815)	-	-	(4,815)
Nonperiodic change in postretirement benefit plan	(51,116)	-	-	(51,116)
Actuarial adjustment on annuities payable	-	(2,349)	(8,463)	(10,812)
Increase in net assets from nonoperating activities	29,080	134,212	89,326	252,618
Increase in net assets - The Pennsylvania State University	388,276	157,030	89,326	634,632
Noncontrolling interest:				
Excess of revenues over expenses	922	-	-	922
Increase in net assets - noncontrolling interest	922	-	-	922
Increase in total net assets	389,198	157,030	89,326	635,554
Net assets at the beginning of the year	6,137,033	551,073	1,518,838	8,206,944
Net assets at the end of the year	$ 6,526,231	$ 708,103	$ 1,608,164	$ 8,842,498

See notes to consolidated financial statements.

THE PENNSYLVANIA STATE UNIVERSITY
CONSOLIDATED STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2016
(in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues and other support:				
Tuition and fees, net of discounts of $178,312	$ 1,727,826	$ -	$ -	$ 1,727,826
Commonwealth of Pennsylvania -				
Appropriations	294,949	-	-	294,949
Special contracts	74,239	-	-	74,239
Department of General Services projects	41,406	-	-	41,406
United States Government grants and contracts	480,463	-	-	480,463
Private grants and contracts	169,980	-	-	169,980
Gifts and pledges	66,824	11,507	-	78,331
Endowment spending	95,439	-	-	95,439
Other investment income	85,336	1,937	-	87,273
Sales and services of educational activities	76,051	-	-	76,051
Recovery of indirect costs	163,302	-	-	163,302
Auxiliary enterprises	445,562	-	-	445,562
Health System revenue, net of provision for bad debts of $62,414	1,996,546	-	-	1,996,546
Other sources	33,442	-	-	33,442
Net assets released from restrictions	12,220	(12,220)	-	-
Total operating revenues and other support	5,763,585	1,224	-	5,764,809
Operating expenses:				
Educational and general -				
Instruction	1,326,628	-	-	1,326,628
Research	799,237	-	-	799,237
Public service	87,440	-	-	87,440
Academic support	405,207	-	-	405,207
Student services	193,891	-	-	193,891
Institutional support	371,203	-	-	371,203
Total educational and general	3,183,606	-	-	3,183,606
Auxiliary enterprises	416,600	-	-	416,600
Health System expense	1,843,196	-	-	1,843,196
Total operating expenses	5,443,402	-	-	5,443,402
Increase in net assets from operating activities	320,183	1,224	-	321,407
Nonoperating activities:				
Gifts and pledges	-	-	75,317	75,317
Current year investment returns	(25,789)	(114,512)	10,020	(130,281)
Endowment appreciation utilized	(69,619)	-	-	(69,619)
Changes in funds held by others in perpetuity	-	3	(931)	(928)
Acquisition of restricted net assets	-	4,730	10,862	15,592
Write-offs and disposals of assets	(10,287)	-	-	(10,287)
Nonperiodic change in postretirement benefit plan	41,641	-	-	41,641
Actuarial adjustment on annuities payable	-	(986)	(10,537)	(11,523)
Increase (decrease) in net assets from nonoperating activities	(64,054)	(110,765)	84,731	(90,088)
Increase (decrease) in net assets - The Pennsylvania State University	256,129	(109,541)	84,731	231,319
Noncontrolling interest:				
Excess of revenues over expenses	2,127	-	-	2,127
Increase in net assets - noncontrolling interest	2,127	-	-	2,127
Increase (decrease) in total net assets	258,256	(109,541)	84,731	233,446
Net assets at the beginning of the year	5,878,777	660,614	1,434,107	7,973,498
Net assets at the end of the year	$ 6,137,033	$ 551,073	$ 1,518,838	$ 8,206,944

See notes to consolidated financial statements.

THE PENNSYLVANIA STATE UNIVERSITY
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016
(in thousands)

	June 30, 2017	June 30, 2016
Cash flows from operating activities:		
Increase in net assets	$ 635,554	$ 233,446
Adjustments to reconcile change in net assets to net cash provided by operating activities -		
Actuarial adjustment on annuities payable	10,812	11,523
Contributions restricted for long-term investment	(98,202)	(100,877)
Interest and dividends restricted for long-term investment	(78,598)	(75,605)
Net realized and unrealized (gains) losses on long-term investments	(408,457)	83,251
Depreciation expense	350,531	331,193
Amortization expense	(52)	(371)
Loss on early extinguishment of debt	3,688	6,405
Write-offs and disposals of assets	5,126	11,043
Contributions of land, buildings and equipment	(2,960)	(3,946)
Buildings and equipment provided by Pennsylvania Department of General Services	-	(95)
Contribution to government student loan funds	154	154
Provision for bad debts	63,136	68,655
Increase in deposits held for others	(26,792)	(618)
Increase in receivables	(95,725)	(35,868)
Increase in inventories	(5,679)	(1,317)
Increase in prepaid expenses and other assets	(954)	(44,735)
Increase in accounts payable and other accrued expenses	118,800	39,572
Increase in deferred revenue	26,319	25,390
Increase in accrued postretirement benefits	169,939	57,436
Net cash provided by operating activities	666,640	604,636
Cash flows from investing activities:		
Purchase of land, buildings and equipment	(647,429)	(597,267)
Increase in deposits held by bond trustees	(47,867)	(69,377)
Advances on student loans	(10,652)	(10,766)
Collections on student loans	10,900	10,618
Proceeds from sale of donated financial assets	236	522
Purchase of investments	(3,761,462)	(4,475,766)
Proceeds from sale of investments	3,720,543	4,789,221
Net cash used in investing activities	(735,731)	(352,815)
Cash flows from financing activities:		
Contributions restricted for long-term investment	98,202	100,877
Interest and dividends restricted for long-term investment	78,598	75,605
Payments of annuity obligations	(6,602)	(6,385)
Proceeds from long-term debt	368,213	437,193
Principal payments on long-term debt	(103,303)	(323,335)
Proceeds related to government student loan funds, net of collection costs	172	729
Net cash provided by financing activities	435,280	284,684
Net increase in cash and cash equivalents	366,189	536,505
Cash and cash equivalents at the beginning of the year	1,395,514	859,009
Cash and cash equivalents at the end of the year	$ 1,761,703	$ 1,395,514

Supplemental disclosures of cash flow information (Note 2)

See notes to consolidated financial statements.

THE PENNSYLVANIA STATE UNIVERSITY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016

1. THE UNIVERSITY AND RELATED ENTITIES

The Pennsylvania State University ("the University"), which was created as an instrumentality of the Commonwealth of Pennsylvania ("the Commonwealth" or "Pennsylvania"), is organized as a non-profit corporation under the laws of the Commonwealth. As Pennsylvania's land grant university, the University is committed to improving the lives of the people of Pennsylvania, the nation and the world through its integrated, tri-part mission of high-quality teaching, research and outreach.

Basis of Presentation

The financial statements of the University include, on a consolidated basis, the consolidated financial statements of Penn State Health ("the Health System"), a Pennsylvania non-profit corporation, and its wholly owned subsidiaries, including the Milton S. Hershey Medical Center ("TMSHMC" or "the Medical Center"), Saint Joseph's Regional Health Network and Medical Group ("SJRHN/SJMG"), and Nittany Health, Inc. ("Nittany Health"), and the financial statements of The Corporation for Penn State and its subsidiaries ("the Corporation"). See Note 11 for additional information about the Health System. The Corporation is a non-profit member corporation organized in 1985 for the exclusive purpose of benefiting and promoting the interests of the University, the Corporation's sole member. The Corporation's financial statements consist primarily of the assets and revenues of The Pennsylvania College of Technology ("Penn College"), a wholly owned subsidiary of the Corporation. All transactions among the University, the Health System, and the Corporation have been eliminated.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The University's consolidated financial statements are prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America (GAAP). The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) is the source of authoritative GAAP.

The University's consolidated financial statements include statements of financial position, activities and cash flows. In accordance with FASB ASC requirements, net assets and the changes in net assets are classified as permanently restricted, temporarily restricted or unrestricted.

Permanently restricted net assets consist primarily of the historical amounts of endowed gifts. Additionally, contributions receivable and remainder interests, which are required by donors to be permanently retained, are included at their estimated net present values.

Temporarily restricted net assets consist of contributions receivable and remainder interests whose ultimate use is not permanently restricted. In addition, the excess of current market value over the historical cost of permanently restricted endowments is classified as temporarily restricted net assets.

Unrestricted net assets are all the remaining net assets of the University. Net unrealized losses on permanently restricted endowment funds for which historical cost exceeds market value are recorded as a reduction to unrestricted net assets.

Revenue from temporarily restricted sources is reclassified as unrestricted revenue when the circumstances of the restriction have been fulfilled. Donor-restricted revenues whose restrictions are met within the same fiscal year are reported as unrestricted income.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts on the financial statements and the disclosure of contingencies and commitments. Actual results could differ from those estimates.

Revenue Recognition

Tuition revenue is recognized in the fiscal year in which the substantial portion of the educational term occurs. Institutional financial aid provided by the University for tuition and fees is reflected as a reduction of tuition and fee revenue. Revenues for auxiliary enterprises are recognized as the related goods and services are delivered and rendered. Grant revenues are recognized as the eligible grant activities are conducted. Payments received in advance for tuition, goods and services are deferred.

Unconditional promises to give are recognized as revenues and receivables in the year made and consist of written or oral promises to contribute to the University in the future. Contributions receivable are recorded with the revenue assigned to the appropriate category of restriction. The amounts are present valued based on timing of expected collections.

The Health System has agreements with third-party payors that provide for payments to its subsidiaries at amounts different from their established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. In addition, net patient service revenue is net of provision for bad debts of $46.3 million and $62.4 million for the years ended June 30, 2017 and 2016, respectively. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined or such estimates change.

The subsidiaries of the Health System provide care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. The Health System does not pursue collection of amounts determined to qualify as charity care; they are not reported as net patient service revenue. The amounts of direct and indirect costs for services and supplies furnished under the Health System’s charity care policy totaled approximately $27.4 million and $17.7 million for the years ended June 30, 2017 and 2016, respectively, and is based on a ratio of the Health System’s operational costs to its gross charges. The amount of charges foregone for services and supplies furnished under the Health System’s charity policy during 2017 and 2016 totaled approximately $53.2 million and $53.0 million, respectively.

Fair Value of Financial Instruments

The University has provided fair value estimates for certain financial instruments in the notes to the financial statements. Fair value information presented in the financial statements is based on information available at June 30, 2017 and 2016. The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable and other accrued expenses approximate fair value because of the terms and relatively short maturity of these financial instruments. The carrying values of the University's loans to students are also reasonable estimates of their fair value, as the total outstanding loans to students as of June 30, 2017 and 2016 have been made at the rates available to students for similar loans at such times. Investments are reported at fair value as disclosed in Note 3. The fair value of the University's bonds payable is disclosed in Note 7. See Note 5 for further discussion of fair value measurements.

Cash Flows

The following items are included as supplemental disclosure to the statements of cash flows for the years ended June 30:

(in thousands of dollars)	2017	2016
Interest paid	$ 42,826	$ 43,039
Non-cash acquisitions of land, buildings and equipment	33,010	131,778

Capitalized costs accrued related to construction are $73.6 million and $80.8 million as of June 30, 2017 and 2016, respectively. Taxes paid for 2017 and 2016 are considered immaterial. Cash and cash equivalents include certain investments in highly liquid instruments with initial maturities of 90 days or less, except for such assets held by the University's investment managers as part of their long-term investment strategies. Short-term investments include other current investments held for general operating purposes with maturities greater than 3 months but less than 12 months.

During the year ended June 30, 2016, the Health System finalized the $113.5 million acquisition of SJRHN/SJMG. Of the $113.5 million, $104.4 million relates to property, plant and equipment and is included in 2016 non-cash acquisitions of land, buildings and equipment in the table above. See further discussion related to the acquisition in Note 11.

Accounts Receivable

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

(in thousands of dollars)	2017	2016
Grants and contracts, net of allowance of $2,214 and $1,211	$ 187,903	$ 173,067
Patient accounts receivable, net of allowance of $61,448 and $68,743	197,613	226,381
Student receivables, net of allowance of $18,500 and $7,930	54,162	27,183
Investment and interest receivable	47,197	12,665
Other, net of allowance of $6,569 and $6,058	55,728	56,804
Total accounts receivable, net	$ 542,603	$ 496,100

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 factors, historical experience, and other currently available evidence. Receivables are written off when management determines they will not be collected.

Related to patient accounts receivable associated with services provided to patients who have third-party coverage, management analyzes contractually due amounts and provides an allowance for doubtful accounts (for example, for expected uncollectible deductibles and copayments or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables from self-pay patients, the subsidiaries of the Health System record a provision for bad debts in the period of service on the basis of past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. In estimating the allowance for doubtful accounts, account age is taken into consideration. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Loans to Students

Loans to students are disbursed to qualified students based on need and include loans granted by the University from institutional resources and under federal government loan programs. Students have a grace period until repayment is required based upon the earlier of graduation or no longer achieving at least half-time enrollment status. The grace period varies depending on the type of loan. Loans accrue interest after the grace period and are repaid directly to the University. Loans to students are uncollateralized and carry default risk. At June 30, 2017 and 2016, student loans represent 0.4% and 0.5% of total assets, respectively.

The availability of funds for loans under federal government revolving loan programs is dependent on reimbursements to the pool from repayments of outstanding loans. Funds advanced by the federal government of $46.7 million and $47.7 million at June 30, 2017 and 2016, respectively, are ultimately refundable to the government and are classified as liabilities in the consolidated statements of financial position. Outstanding loans cancelled under the program result in a reduction of the funds available to loan and a decrease in the liability to the federal government.

Loans to students consisted of the following at June 30:

(in thousands of dollars)	2017	2016
Loans to students:		
Federal government loan programs:		
Perkins loan program	$ 42,772	$ 44,381
Health Professions Student Loans and Loans for Disadvantaged Students	39	49
Federal government loan programs	42,811	44,430
Institutional loan programs	18,889	19,002
	61,700	63,432
Less allowance for doubtful accounts:		
Balance, beginning of year	(2,526)	(3,156)
Provision for doubtful accounts	(592)	630
Balance, end of year	(3,118)	(2,526)
Loans to students, net	$ 58,582	$ 60,906

Allowances for doubtful accounts are established based on prior collection experience and current economic factors which, in management's judgment, could influence the ability of loan recipients to repay the amounts according to the terms of the loan. Further, the University does not evaluate credit quality of student loans receivable after the initial approval of the loan. Loans to students are considered past due when payment is not received by the due date, and interest continues to accrue until the loan is paid in full or written off. When loans to students are deemed uncollectible, an allowance for doubtful accounts is established. Further, the University does not evaluate the credit quality of the student loans receivable after the initial approval and calculation of the loans.

The University considers the age of the amounts outstanding in determining the collectability of loans to students. The aging of the loans to students based on days delinquent and the related allowance for doubtful accounts at June 30 are as follows:

(in thousands of dollars)

2017	45 days or less	46-75 days	76-105 days	Over 105 days	Total
Loans to students:					
Federal government loan programs	$ 36,638	$ 31	$ 37	$ 6,105	$ 42,811
Institutional loan programs	16,056	21	16	2,796	18,889
Total loans to students	52,694	52	53	8,901	61,700
Allowance for doubtful accounts:					
Federal government loan programs					(457)
Institutional loan programs					(2,661)
Total allowance for doubtful accounts					(3,118)
Total loans to students, net					$ 58,582

(in thousands of dollars)

2016	45 days or less	46-75 days	76-105 days	Over 105 days	Total
Loans to students:					
Federal government loan programs	$ 37,547	$ 28	$ 20	$ 6,835	$ 44,430
Institutional loan programs	16,194	27	15	2,766	19,002
Total loans to students	53,741	55	35	9,601	63,432
Allowance for doubtful accounts:					
Federal government loan programs					(441)
Institutional loan programs					(2,085)
Total allowance for doubtful accounts					(2,526)
Total loans to students, net					$ 60,906

Inventories

Inventories are stated at the lower of cost or market, generally on the first-in, first-out basis.

Investments

The University's noncurrent investments represent the University's endowment and other investments held for general operating purposes. The University's investments are reported at fair value in the accompanying financial statements. Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair values with gains and losses included in the consolidated statements of activities. In the management of investments, the University authorizes certain investment managers to purchase derivative securities to attain a desired market position; and the University may directly invest in derivative securities to attain a desired market position. The University does not trade or issue derivative financial instruments other than through the investment management practices noted above. The University records derivative securities at fair value with gains and losses reflected in the consolidated statements of activities.

The estimated fair value amounts for marketable debt, equity and fixed income securities held by the University have been reviewed by the University and determined using available market information as supplied by the various financial institutions that act as trustees or custodians for the University. For non-liquid holdings, generally limited partnership investments in private real estate, venture capital, private equity, natural resources, and private debt, estimated fair value is determined based upon financial information provided by the general partner. This financial information includes assumptions and methods that were reviewed by University management. The University believes that the estimated fair value is a reasonable estimate of market value as of June 30, 2017 and 2016. Because the limited partnerships are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market existed, and such differences could be material.

Income on operating investments and income used for the annual distribution under the annual spending policy for endowments are reported in operating revenues within the consolidated statement of activities.

Beneficial Interest in Perpetual Trusts

The University is the beneficiary of certain perpetual trusts held and administered by outside trustees. The fair value of these trust assets has been recorded as permanently restricted net assets and related beneficial interest in perpetual trusts in the consolidated financial statements.

Investment in Plant

Total investment in plant as of June 30 is comprised of the following:

(in thousands of dollars)	2017	2016
Land	$ 134,153	$ 133,473
Buildings	6,771,677	6,272,904
Improvements other than buildings	678,049	650,696
Equipment	1,497,053	1,382,532
Total plant	9,080,932	8,439,605
Less accumulated depreciation	(4,159,520)	(3,849,294)
Total investment in plant, net	$ 4,921,412	$ 4,590,311

The value of land, buildings, and equipment is recorded at cost or, if received as gifts, at fair value at date of gift. The University does not capitalize the cost of library books. Depreciation is computed over the estimated useful lives of the assets using the straight-line method. Useful lives range from 4 to 50 years for buildings, 10 to 20 years for improvements other than buildings, and 1 to 20 years for equipment. Depreciation expense was $350.5 million and $331.2 million for the fiscal years ended June 30, 2017 and 2016, respectively. The University has certain building and equipment lease agreements in effect which are considered capital leases that are included as long-term debt in the statements of financial position. These leases have been capitalized at the lower of fair market value or net present value of the minimum lease payments. Buildings and equipment held under capital leases are amortized on a straight-line basis over the shorter of the lease terms or the estimated useful lives of the assets. The capitalized cost and accumulated depreciation of the leases at June 30, 2017 and 2016 was $188.0 million and $85.4 million, and $169.2 million and $72.5 million, respectively.

Accounts Payable and Other Accrued Expenses

Accounts payable and other accrued expenses at June 30 consist of the following:

(in thousands of dollars)	2017	2016
Accounts payable (non-Health System)	$ 265,025	$ 248,897
Health System accounts payable and other accrued expenses	262,722	268,324
Accrued payroll and other related liabilities	143,546	64,690
Accrued bond interest	15,705	9,027
Student deposits	2,887	5,089
Total accounts payable and other accrued expenses	$ 689,885	$ 596,027

Impairment of Long-Lived Assets

Long-lived assets, which include investment in plant and definite-lived intangible assets, are assessed for impairment whenever events or changes in circumstances indicate the carrying amount of the asset may not be recoverable. An impairment loss is recognized in change in net assets in the period that the impairment occurs.

Asset Retirement Obligations

The University has recognized liabilities for asset retirement obligations. The University has identified asbestos abatement and the decommissioning of the Breazeale Nuclear Reactor as conditional asset retirement obligations. These obligations are reported as part of other noncurrent liabilities within the consolidated statement of financial position. The following table details the change in liabilities for the years ended June 30:

	(in thousands of dollars)
Balance as of June 30, 2015	$ 71,585
Adjustment to liability	2,615
Accretion expense	2,924
Liabilities settled	(3,022)
Balance as of June 30, 2016	74,102
Adjustment to liability	12,892
Accretion expense	3,164
Liabilities settled	(6,945)
Balance as of June 30, 2017	$ 83,213

Annuities Payable

Annuities payable consist of annuity payments currently due and the actuarial amount of annuities payable. The actuarial amount of annuities payable is the present value of the aggregate liability for annuity payments over the expected lives of the beneficiaries.

Net Assets

Net assets consist of the following at June 30:

(in thousands of dollars)	2017	2016
Unrestricted net assets	$ 6,526,231	$ 6,137,033
Temporarily restricted net assets:		
Future contributions	$ 146,180	$ 124,003
Annuity and life income funds	32,070	21,587
Contributions for property, plant and equipment	6,278	5,876
Term endowments and accumulated endowment gains	523,575	399,607
Total temporarily restricted net assets	$ 708,103	$ 551,073
Permanently restricted net assets:		
Future contributions	$ 89,734	$ 100,641
Annuity and life income funds	36,069	37,356
Student loan funds	16,890	16,560
Perpetual trusts and other funds	28,013	22,444
Endowment funds	1,437,458	1,341,837
Total permanently restricted net assets	$ 1,608,164	$ 1,518,838
Total net assets	$ 8,842,498	$ 8,206,944

Income Taxes

The University files U.S. federal and state tax returns. The statute of limitations on the University's federal returns generally remains open for three years following the year they are filed. In accordance with ASC 740 Income Taxes Topic, the University continues to evaluate tax positions and has determined there is no material impact on the University financial statements.

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update ("ASU") 2014-09, *"Revenue from Contracts with Customers."* This guidance clarifies the principles for recognizing revenue that (1) removes inconsistencies and weaknesses in revenue requirements, (2) provides a more robust framework for addressing revenue issues, (3) improves comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets, (4) provides more useful information to users of financial statements through improved disclosure requirements, and (5) simplifies the preparation of financial statements by reducing the number of requirements to which an entity must refer. In August 2015, the FASB issued ASU 2015-14, *"Revenue from Contracts with Customers; Deferral of the Effective Date."* This guidance defers the effective date of the original ASU. This guidance is now effective for the University beginning July 1, 2018. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, *"Consolidation; Amendments to the Consolidation Analysis."* This update provides enhanced guidance for entities to apply in performing consolidation analyses and was effective for the University beginning July 1, 2016. The adoption of this guidance did not have a material impact on the consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, *"Inventory; Simplifying the Measurement of Inventory."* This guidance requires entities to measure inventory within the scope of the update at the lower of cost and net realizable value. This guidance is effective for the University beginning July 1, 2017 with early adoption permitted. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, *"Financial Instruments – Overall; Recognition and Measurement of Financial Assets and Financial Liabilities."* This guidance addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. This guidance is effective for the University beginning July 1, 2018. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In February 2016, the FASB issues ASU 2016-02, *"Leases."* This guidance requires substantial changes to lease accounting to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The main difference between previous GAAP and this guidance is the recognition of lease assets and lease liabilities by lessees for those leases classified as operating under previous GAAP. This guidance is effective for the University beginning July 1, 2019 with early adoption permitted. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14, *"Not-for-Profit Entities; Presentation of Financial Statements of Not-for-Profit Entities."* This guidance amends the requirements for financial statements and notes in Topic 958, Not-for-Profit Entities. The most significant amendment requires a not-for-profit entity ("NFP") to present on the face of the statement of financial position amounts for two classes of net assets at the end of the period, rather than for the currently required three classes. That is, an NFP will report amounts for *net assets with donor restrictions* and *net assets without donor restrictions*, as well as the currently required amount for total net assets. This guidance is effective for the University beginning July 1, 2018 with early adoption permitted. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *"Statement of Cash Flows; Classification of Certain Cash Receipts and Cash Payments."* This update provides guidance on eight specific cash flows issues with the objective of reducing the existing diversity in practice. This guidance is effective for the University beginning July 1, 2018 with early adoption permitted. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-02, *"Not-for-Profit Entities—Consolidation; Clarifying When a Not-for-Profit Entity That Is a General Partner or a Limited Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity."* This update amends the consolidation guidance in Subtopic 958-810, Not-for-Profit Entities—Consolidation, to clarify when a NFP that is a general partner or a limited partner should consolidate a for-profit limited partnership or similar legal entity once the amendments in ASU 2015-02 become effective. This guidance is effective for the University beginning July 1, 2017 with early adoption permitted. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, *"Compensation – Retirement Benefits; Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost."* This update requires that an employer report the service cost component in the same line items as other compensation costs arising from services rendered by the pertinent employees during the period. In addition, the other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations. This guidance is effective for the University beginning July 1, 2018 with early adoption permitted. The University has not yet evaluated the impact this guidance may have on its consolidated financial statements.

3. INVESTMENTS

Investments by major category as of June 30 are summarized as follows:

(in thousands of dollars)	2017	2016
Money markets	$ 144,065	$ 93,741
Fixed income:		
U.S. government/agency	1,030,281	1,158,474
U.S. corporate	972,121	908,609
Foreign	183,270	199,586
Other	228,070	243,678
Equities	1,911,096	1,566,626
Private capital	1,573,841	1,480,599
Total	$ 6,042,744	$ 5,651,313

Other fixed income investments consist of collateralized mortgage obligations, mortgage-backed securities and asset-backed securities. Equity investments are comprised of domestic and foreign common stocks. Private capital consists primarily of interests in private real estate, venture capital, private equity, natural resources, private debt, commodities and hedge fund limited partnerships.

Futures contracts, which are fully cash collateralized, comprise the University's beneficially held derivative instruments at June 30, 2017 and 2016, are marked to market daily, and are included in the fair value of the University's investments. The fair value of derivative instruments is included in the fair value of the University's investments within the money market category. Futures contracts have minimal credit risk because the counterparties are the exchanges themselves. Fully cash collateralized derivative securities comprised $5.2 million, 0.09% of total investments, and $4.4 million, 0.08% of total investments at June 30, 2017 and 2016, respectively. The University's derivatives consist of S&P 500 futures at June 30, 2017 and 2016 and are employed as a low cost, passive investment vehicle with daily liquidity which allows the University to maintain desired market exposure in light of irregular cash flows.

The following schedules summarize the investment return and its classification in the consolidated statement of activities for the years ended June 30:

(in thousands of dollars) 2017	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Dividends and interest	$ 162,885	$ 1,046	$ 9,056	$ 172,987
Net realized gains	82,810	43,339	-	126,149
Net unrealized gains	78,072	93,222	-	171,294
Total returns	$ 323,767	$ 137,607	$ 9,056	$ 470,430

(in thousands of dollars) 2016	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Dividends and interest	$ 111,156	$ 1,937	$ 10,020	$ 123,113
Net realized gains (losses)	62,289	(17,965)	-	44,324
Net unrealized losses	(88,078)	(96,547)	-	(184,625)
Total returns	$ 85,367	$ (112,575)	$ 10,020	$ (17,188)

4. ENDOWMENT NET ASSETS

The University's endowment includes both donor-restricted endowment funds and funds designated to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The ASC Not-for-Profit Entities Presentation of Financial Statements Subtopic (ASC Subtopic 958-205) provides guidance on the net asset classification of donor-restricted endowment funds for not-for-profit organizations subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") and improves disclosure about an organization's endowment funds regardless of whether the organization is subject to UPMIFA. The Commonwealth of Pennsylvania has not adopted UPMIFA but rather has enacted Pennsylvania Act 141 ("PA Act 141"). PA Act 141 permits an organization's trustees to define income as a stipulated percentage of endowment assets (between 2% and 7% of the fair value of the assets averaged over a period of at least three preceding years) without regard to actual interest, dividend, or realized and unrealized gains.

The University has interpreted PA Act 141 to permit the University to spend the earnings of its endowment based on a total return approach, without regard to the fair value of the original gift. As a result of this interpretation, the University classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, the original value of subsequent gifts to the permanent endowment, and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. Funds functioning as endowments are established at the direction of University management and are classified as unrestricted net assets due to the lack of external donor restrictions. Gains and losses attributable to permanent endowments are recorded as temporarily restricted net assets and gains and losses attributable to funds functioning as endowments are recorded as unrestricted net assets.

From time to time, due to unfavorable market fluctuations, the fair value of some assets associated with individual donor-restricted endowment funds may fall below the level that donors require to be retained as a perpetual fund, while other assets are unaffected to the same extent and maintain or exceed the level required. The aggregate amount of deficiencies at June 30, 2017 and 2016 was $1.3 million and $7.4 million, respectively, reported in unrestricted net assets on the consolidated statement of activities. Subsequent investment gains will be used to restore the balance up to the fair market value of the original gift. Subsequent gains above that amount will be recorded as temporarily restricted net assets.

Endowment net asset composition by type of fund as of June 30:

(in thousands of dollars) 2017	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ (1,299)	$ 521,602	$ 1,424,224	$ 1,944,527
Funds functioning as endowments	651,647	-	-	651,647
Total net assets	$ 650,348	$ 521,602	$ 1,424,224	$ 2,596,174

(in thousands of dollars) 2016	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ (7,353)	$ 398,384	$ 1,330,966	$ 1,721,997
Funds functioning as endowments	594,587	-	-	594,587
Total net assets	$ 587,234	$ 398,384	$ 1,330,966	$ 2,316,584

Changes in endowment net assets for the years ended June 30:

(in thousands of dollars) 2017	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of the year	$ 587,234	$ 398,384	$ 1,330,966	$ 2,316,584
Endowment return:				
Endowment earnings	22,650	20	3,398	26,068
Net realized gains	89,401	41,482	-	130,883
Net unrealized gains	27,652	87,277	-	114,929
Reclassification of funds with deficiencies	6,054	(6,054)	-	-
Total endowment return	145,757	122,725	3,398	271,880
Contributions	-	493	89,860	90,353
Endowment spending	(98,521)	-	-	(98,521)
Transfers to create funds functioning as endowments	15,878	-	-	15,878
Endowment net assets, end of the year	$ 650,348	$ 521,602	$ 1,424,224	$ 2,596,174

(in thousands of dollars) 2016	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of the year	$ 618,419	$ 500,533	$ 1,249,838	$ 2,368,790
Endowment return:				
Endowment earnings	25,820	19	3,727	29,566
Net realized gains (losses)	63,939	(17,736)	-	46,203
Net unrealized losses	(30,090)	(91,831)	-	(121,921)
Reclassification of funds with deficiencies	(5,899)	5,899	-	-
Total endowment return	53,770	(103,649)	3,727	(46,152)
Contributions	-	1,500	77,401	78,901
Endowment spending	(95,439)	-	-	(95,439)
Transfers to create funds functioning as endowments	10,484	-	-	10,484
Endowment net assets, end of the year	$ 587,234	$ 398,384	$ 1,330,966	$ 2,316,584

Not included above are the endowment net assets of subsidiaries of $18.1 million and $14.7 million as of June 30, 2017 and 2016, respectively.

The University has adopted investment and spending policies for endowment assets that attempt to provide a relatively predictable stream of funding to programs supported by its endowment while seeking to maintain, over time, the purchasing power of the endowment assets. The overall management objective for the University's pooled endowment funds is to preserve or grow the real (inflation-adjusted) purchasing power of the assets through a prudent long-term investment strategy. This objective would be achieved on a total return basis. Under these policies, as approved by the Board of Trustees and the Penn State Investment Council, the primary investment objective of the University's pooled endowment is to attain a real total return (net of investment management fees) that at least equals a total annual effective spending rate of 5.25% (program spending of 4.5% plus administrative costs of 0.75%) over the long term.

To satisfy its long-term rate-of-return objectives, the University relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The University targets diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints. The endowment assets of the University are invested in a broad range of equities and fixed income securities, thereby limiting the market risk exposure in any one institution or individual investment.

The University has a policy of appropriating for distribution each year a certain percentage (4.5% for 2017 and 2016) of its pooled endowment fund's average fair market value over the prior five years preceding the fiscal year in which the distribution is planned. Accordingly, over the long term, the University expects the current spending policy to allow its endowment to provide generous current spending while preserving "intergenerational equity". This is consistent with the University's objective to maintain the purchasing power of the endowment assets held in perpetuity as well as to provide additional real growth through new gifts and investment returns.

5. FAIR VALUE MEASUREMENTS

The University utilizes the following fair value hierarchy, which prioritizes into three broad levels the inputs to valuation techniques used to measure fair value:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets as of the measurement date. Such instruments valued at Level 1 primarily consist of securities that are directly held and actively traded in public markets.

Level 2 – Inputs other than unadjusted quoted prices that are observable for the asset or liability, directly or indirectly, including quoted prices for similar assets or liabilities in active markets, inputs other than quoted prices that are observable for the asset or liability, and inputs that are derived from observable market data by correlation or other means.

Level 3 – Unobservable inputs that cannot be corroborated by observable market data.

In instances in which the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The University's assessment of significance of a particular item to the fair value measurement in its entirety requires judgment, including consideration of inputs specific to the asset.

The following table presents information as of June 30, 2017 about the University's financial assets and liabilities that are measured at fair value on a recurring basis:

(in thousands of dollars)	Quoted Prices in Active Markets For Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Total Fair Value
Assets:				
Long-term Investment Pool:				
Money markets	$ 128,632	$ -	$ -	$ 128,632
Fixed income				
U.S. government/agency	85,021	80,107	-	165,128
U.S. corporate	-	243,578	-	243,578
Foreign	-	86,431	-	86,431
Other	-	32,905	-	32,905
Equities	1,102,498	-	-	1,102,498
Total	$ 1,316,151	$ 443,021	$ -	$ 1,759,172
Operating investments:				
Money markets	$ 15,424	$ 9	$ -	$ 15,433
Fixed income				
U.S. government/agency	633,619	231,535	-	865,154
U.S. corporate	82,513	646,029	-	728,542
Foreign	11,948	84,892	-	96,840
Other	20,031	175,134	-	195,165
Equities	146,726	16	4,688	151,430
Total	$ 910,261	$ 1,137,615	$ 4,688	$ 2,052,564
Deposits held by bond trustees:				
Money markets	$ 178,954	$ -	$ -	$ 178,954
Fixed income				
U.S. government/agency	-	-	-	-
Total	$ 178,954	$ -	$ -	$ 178,954
Beneficial interest in perpetual trusts	$ -	$ -	$ 19,854	$ 19,854
Liabilities:				
Present value of annuities payable	$ -	$ -	$ 58,070	$ 58,070

The following table presents information as of June 30, 2016 about the University's financial assets and liabilities that are measured at fair value on a recurring basis:

(in thousands of dollars)	Quoted Prices in Active Markets For Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3	Total Fair Value
Assets:				
Long-term Investment Pool:				
Money markets	$ 84,516	$ -	$ -	$ 84,516
Fixed income				
U.S. government/agency	284,969	15,881	-	300,850
U.S. corporate	-	190,065	-	190,065
Foreign	-	115,349	-	115,349
Other	-	40,035	-	40,035
Equities	823,912	102,341	-	926,253
Total	$ 1,193,397	$ 463,671	$ -	$ 1,657,068
Operating investments:				
Money markets	$ 9,215	$ 10	$ -	$ 9,225
Fixed income				
U.S. government/agency	615,449	242,175	-	857,624
U.S. corporate	79,241	639,303	-	718,544
Foreign	11,272	72,965	-	84,237
Other	25,114	178,529	-	203,643
Equities	127,318	59	4,214	131,591
Total	$ 867,609	$ 1,133,041	$ 4,214	$ 2,004,864
Deposits held by bond trustees:				
Money markets	$ 130,639	$ -	$ -	$ 130,639
Fixed income				
U.S. government/agency	-	448	-	448
Total	$ 130,639	$ 448	$ -	$ 131,087
Beneficial interest in perpetual trusts	$ -	$ -	$ 14,558	$ 14,558
Liabilities:				
Present value of annuities payable	$ -	$ -	$ 53,859	$ 53,859

The fair value tables above exclude investments of $2,231.0 million and $1,989.4 million as of June 30, 2017 and 2016, respectively, which are measured at NAV and are not classified in the fair value hierarchy.

The Long-term Investment Pool (LTIP) is a mutual fund-like vehicle used for investing the University's endowment funds, funds functioning as endowments, and other operating funds that are expected to be held long-term. A share method of accounting for the LTIP is utilized by the University. Each participating fund enters into and withdraws from the LTIP based on monthly share values. At June 30, 2017 and 2016, fair value of endowment funds and funds functioning as endowments within the LTIP totaled $2,615.6 million and $2,362.2 million, respectively. At June 30, 2017 and 2016, fair value of operating funds included in the LTIP totaled $1,370.9 million and $1,280.0 million, respectively.

The following tables present information related to changes in Level 3 for each category of financial assets and liabilities for year ended June 30, 2017:

(in thousands of dollars)	Operating Investments	Beneficial Interest in Perpetual Trusts
Assets:		
Beginning balance	$ 4,214	$ 14,558
Total realized and unrealized gains	540	5,296
Sales	(66)	-
Ending balance	$ 4,688	$ 19,854

	Present Value of Annuities Payable
Liabilities:	
Beginning balance	$ 53,859
Actuarial adjustment of liability	3,460
Gifts	3,144
Sales	(2,393)
Ending balance	$ 58,070

The following tables present information related to changes in Level 3 for each category of financial assets and liabilities for year ended June 30, 2016:

(in thousands of dollars)	Operating Investments	Beneficial Interest in Perpetual Trusts
Assets:		
Beginning balance	$ 5,779	$ 15,471
Total realized and unrealized gains (losses)	502	(913)
Purchases	599	-
Sales	(2,666)	-
Ending balance	$ 4,214	$ 14,558

	Present Value of Annuities Payable
Liabilities:	
Beginning balance	$ 48,721
Actuarial adjustment of liability	(1,556)
Gifts	6,886
Sales	(192)
Ending balance	$ 53,859

There were no transfers of assets between Level 3 and Level 2 and between Level 1 and Level 2 in 2017 and 2016.

The following table presents the fair value and redemption frequency for those investments whose fair value is not readily determinable and is estimated using the net asset value per share or its equivalent as of June 30, 2017 and 2016:

(in thousands of dollars)	Fair Value 2017	Fair Value 2016	Unfunded Commitments At June 30, 2017	Redemption Frequency	Redemption Notice Period
Commingled Funds:					
Non-U.S. Equity	$ 627,998	$ 508,782		Quarterly/ Daily/Monthly	5-90 days
Subtotal	$ 627,998	$ 508,782			
Marketable Investment Partnerships:					
Absolute Return	$ 56,471	$ 30,811		Quarterly	60 days
Distressed Debt	60,406	53,557		Quarterly/ Semi Annual	60-90 days
Commodities	126,846	94,795		Monthly	30-60 days
Opportunistic	123,387	186,635		Quarterly	30 days
Directional Long/Short	289,472	287,482		Monthly	30 days
Subtotal	$ 656,582	$ 653,280			
Non-Marketable Investment Partnerships:					
Private Real Estate	$ 83,925	$ 97,089	$ 39,566		
Venture Capital	323,408	271,898	168,357		
Private Equity	297,386	248,969	262,795		
Natural Resources	130,146	116,307	66,729		
Private Debt	111,563	93,056	166,911		
Subtotal	$ 946,428	$ 827,319	$ 704,358		
Total	$ 2,231,008	$ 1,989,381	$ 704,358		

Commingled Funds include investments that aggregate assets from multiple investors and are managed collectively following a prescribed strategy. Redemptions vary from daily to quarterly with required notification of 90 days or less. The non-U.S. equity strategy is invested in developed and developing countries outside of the United States, and spans the entire equity capitalization spectrum. These collective portfolios preclude the need to obtain securities registration in foreign countries.

Marketable Investment Partnerships include several hedge funds whose underlying positions are traded via public securities markets. Liquidity terms range from quarterly to annually with advance notification for redemption ranging from 30 to 90 days. The fair values of the investments for each fund in this category have been estimated using the net asset value of the LTIP's share holdings in the fund. Five major investment strategies are included within this category. Absolute Return refers to relative value strategies. Directional refers to equity long/short strategies in both U.S. and non-U.S. markets. Opportunistic refers to global multi-strategy. Distressed Debt refers to securities rated below investment grade, along with non-rated debt. Commodities refer to publicly traded commodity instruments primarily including futures and options.

Nonmarketable Investment Partnerships include limited partnership interests in a variety of illiquid investments. The fair values of the investments for each fund in this category have been estimated using the net asset value of the LTIP's ownership interest in partner's capital and cannot be redeemed. Realizations from each fund are received as the underlying investments are liquidated or distributed, typically within 10 years after initial commitment. Unfunded commitments represent remaining commitments of the LTIP's drawdown funds as of June 30, 2017. Five major investment strategies are included within this category. Private Real Estate includes properties primarily located in the U.S. Venture Capital includes non-public startups and enterprises in early stages of growth located globally. Private Equity includes buyouts of previously public companies as well as enterprises that are planning to go public in the near future, including funds focusing on opportunities outside the U.S. Natural Resources largely include companies primarily involved in oil and natural gas in addition to a variety of other natural resources. Private Debt includes global private credit securities rated below investment grade as well as non-rated debt.

6. CONTRIBUTIONS RECEIVABLE

Contributions receivable are summarized as follows as of June 30:

(in thousands of dollars)	2017	2016
In one year or less	$ 66,076	$ 59,567
Between one year and five years	78,025	63,646
More than five years	112,650	113,277
Contributions receivable, gross	256,751	236,490
Less allowance	(4,299)	(4,065)
Less discount	(51,394)	(52,872)
Contributions receivable, net	$ 201,058	$ 179,553

Contributions received during the years ended June 30, 2017 and 2016 are discounted at rates ranging from 1.24% to 2.46% and 0.45% to 1.69%, respectively. The discount rates for prior periods ranged from 0.11% to 6.28%.

At June 30, 2017 and 2016, the University has received bequest intentions and certain other conditional promises to give of $103.3 million and $97.7 million, respectively. These intentions and conditional promises to give are not included in the consolidated financial statements.

The following table summarizes the change in contributions receivable, net during the year ended June 30, 2017:

	(in thousands of dollars)
Balance at the beginning of year	$ 179,553
New pledges	97,203
Collections on pledges	(76,942)
Increase in allowance	(234)
Decrease in unamortized discounts	1,478
Balance at the end of year	$ 201,058

7. LONG-TERM DEBT

The various bond issues, notes payable and capital lease obligations that are included in long-term debt in the statements of financial position consist of the following at June 30:

(in thousands of dollars)	2017	2016
The Pennsylvania State University Bonds		
Series 2017A	$ 157,080	$ -
Series 2017B	125,000	-
Series 2016A	122,165	122,165
Series 2016B	229,775	229,775
Series 2015A	63,780	65,210
Series 2015B	108,000	111,580
Series 2010	131,380	135,035
Series 2009B	74,235	74,235
Series 2008B	-	1,050
Series 2007B	51,065	54,415
Refunding Series 2002	-	4,835
Pennsylvania Higher Educational Facilities Authority University Revenue Bonds (issued for The Pennsylvania State University)		
Series 2006	2,655	2,890
Series 2004	2,840	3,125
Series 2002	2,435	2,860
Lycoming County Authority College Revenue Bonds (issued for Penn College)		
Series 2016	54,190	-
Series 2015	6,390	7,660
Series 2012	24,275	24,685
Series 2011	37,810	37,880
Series 2008	-	55,000
Total bonds payable	1,193,075	932,400
Unamortized bond premiums	142,442	118,332
Unamortized deferred bond costs	(5,952)	(5,267)
Notes payable and capital leases		
Notes payable	26,983	29,000
Capital lease obligations	112,845	96,811
Total notes payable and capital leases	139,828	125,811
Total long-term debt	$ 1,469,393	$ 1,171,276

Debt issuance	Interest rate mode	Interest rates	Payment ranges and maturity *(in thousands of dollars)*
The Pennsylvania State University Bonds			
Series 2017A	Fixed	2.00% - 5.00%	$2,400 to $5,965 through September 2037 with $34,750 and $44,620 due September 2042 and September 2047, respectively.
Series 2017B	Fixed	1.275% - 3.793%	$2,660 to $3,830 through September 2032 with $21,305 and $56,595 due September 2037 and September 2047, respectively
Series 2016A	Fixed	4.00% - 5.00%	$2,585 to $6,465 through September 2036 with $37,520 due September 2041
Series 2016B	Fixed	4.00% - 5.00%	$7,165 to $22,195 through September 2036
Series 2015A	Fixed	4.00% - 5.00%	$1,460 to $3,445 through September 2035 with $20,000 due September 2040
Series 2015B	Fixed	4.00% - 5.00%	$3,665 to $8,435 through September 2035
Series 2010	Fixed	3.375% - 5.00%	$3,800 to $6,595 through March 2030 with $21,805 and $44,245 due March 2035 and March 2040, respectively
Series 2009B	Variable	1.05%	June 2031
Series 2007B	Fixed	5.25%	$3,520 to $5,955 through August 2027
Pennsylvania Higher Educational Facilities Authority ("PHEFA") University Revenue Bonds			
Series 2006	Fixed	4.30% - 5.125%*	$245 to $280 through September 2020 with $1,610 due September 2025
Series 2004	Fixed	4.60% - 5.00%*	$300 to $325 through September 2019 with $1,905 due September 2024
Series 2002	Fixed	5.00%*	$2,435 due March 2022
*Annual interest costs to the University for interest rates greater than 3.00% are subsidized by PHEFA.			
Lycoming County Authority College Revenue Bonds			
Series 2016	Fixed	2.125% - 5.00%	$1,545 to $3,615 through October 2032 with $19,345 due October 2037
Series 2015	Fixed	2.50% - 4.00%	$465 to $1,590 through January 2025
Series 2012	Fixed	2.00% - 5.00%	$1,020 to $1,170 through May 2020 with $2,565, $6,395 and $12,045 due May 2022, May 2026 and May 2032, respectively
Series 2011	Fixed	4.00% - 5.24%	$1,565 to $1,850 through July 2021 with $14,170 and $18,705 due July 2026 and July 2030, respectively

The Series 2017A Bonds are general obligation bonds issued in April 2017 for the purpose of financing various construction and renovation projects. The Series 2017A Bonds are subject to early redemption provisions, at the option of the University, beginning September 2027. The bonds maturing in September 2042 are subject to mandatory sinking fund redemption.

The Series 2017B Bonds are taxable general obligation bonds issued in April 2017 for the purpose of financing the general corporate purposes of the University. The Series 2017B Bonds are subject to early redemption provisions, at the option of the University, in order of their maturity, at the make-whole redemption price. The bonds maturing in September 2037 are subject to mandatory sinking fund redemption.

The Series 2016 Bonds are Lycoming County Authority (the "Authority") College Revenue Bonds issued by Penn College in August 2016 for the purpose of refunding $55.0 million of the Authority's College Revenue Bond Series 2008. The Series 2008 Bonds were paid in full during the year ended June 30, 2017.

The Series 2009B Bonds are currently paying interest on a variable rate basis at a long term rate for the period June 1, 2017 through May 31, 2018. The University has the option to convert to another variable rate (daily, weekly, monthly or flexible) or to a fixed rate basis (such rates are generally determined on a market basis) at respective conversion dates. The bonds currently pay interest at 1.05% with adjustment on the respective date to the rate the remarketing agent believes will cause the bonds to have a market value equal to the principal. The 2009B bondholders have the right to tender bonds on the purchase dates while such bonds bear interest at the daily, weekly or monthly rate. The 2009B Bonds were issued subject to the self-liquidity program established by the University on the date of issuance pursuant to which the University will provide liquidity for the 2009B Bonds from its general funds in the event of insufficient remarketing proceeds.

The University has complied with all financial debt covenants for the years ended June 30, 2017 and 2016.

Maturities and sinking fund requirements on bonds payable for each of the next five fiscal years and thereafter are summarized as follows:

Year	Annual Installments *(in thousands of dollars)*
2018	$ 28,490
2019	35,825
2020	37,785
2021	39,455
2022	41,315
Thereafter	1,010,205
	$ 1,193,075

The fair value of the University's bonds payable is estimated based on current rates offered for similar issues with similar security, terms and maturities using available market information as supplied by the various financial institutions who act as trustees or custodians for the University. At June 30, 2017, the carrying value and estimated fair value of the University's bonds payable, including issuance premiums and deferred bond costs, are $1,329.6 million and $1,337.5 million, respectively. At June 30, 2016, the carrying value and estimated fair value of the University's bonds payable, including issuance premiums and deferred bond costs, were $1,045.5 million and $1,102.6 million, respectively. Certain bond issues have associated issuance premiums; these issuance premiums total $142.4 million and $118.3 million at June 30, 2017 and 2016, respectively and are presented within the statement of financial position as long-term debt. These issuance premiums will be amortized over the term of the respective outstanding bonds. Certain bond issues have associated deferred bond costs; these deferred bond costs total $6.0 million and $5.3 million at June 30, 2017 and 2016, respectively and are presented within the statement of financial position as a reduction in long-term debt. These deferred bond costs will be amortized over the term of the respective outstanding bonds.

Notes payable and capital leases

The University has three notes payable included within the consolidated statements of financial position at June 30, 2017 with balances of $8.0 million, $9.0 million, and $10.0 million. These notes have payments due annually through June 2024, June 2025, and March 2026 and bear interest at 2.60%, 2.85%, and 2.80%, respectively. The current portion of payments due under these notes totals $2.4 million at June 30, 2017.

The University has certain building and equipment lease agreements in effect which are considered capital leases. Future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of June 30, 2017 are as follows:

Year	*(in thousands of dollars)*
2018	$ 19,521
2019	17,824
2020	14,723
2021	12,361
2022	10,192
Thereafter	139,571
Total minimum lease payments	214,192
Less imputed interest	(101,347)
Capital lease obligation	112,845
Current portion	12,325
Long-term portion	$ 100,520

8. OPERATING LEASES

The University has certain lease agreements in effect which are considered operating leases. During the year ended June 30, 2017, the University recorded expenses of $23.6 million for leased equipment and $30.5 million for leased building space. During the year ended June 30, 2016, the University recorded expenses of $22.0 million for leased equipment and $27.7 million for leased building space.

Future minimum lease payments under operating leases as of June 30, 2017 are as follows:

Year	*(in thousands of dollars)*
2018	$ 27,306
2019	22,141
2020	17,277
2021	11,884
2022	9,835
Thereafter	34,901
Total minimum lease payments	$ 123,344

9. RETIREMENT BENEFITS

The University provides retirement benefits for substantially all regular employees, primarily through either contributory defined benefit plans administered by the Commonwealth of Pennsylvania State Employees' Retirement System ("SERS") and The Public School Employees' Retirement System or defined contribution plans administered by the Teachers Insurance and Annuity Association – College Retirement Equity Fund and Fidelity Investments. The University is billed for its share of the estimated actuarial cost of the defined benefit plans ($104.9 million and $85.9 million for the years ended June 30, 2017 and 2016, respectively). The University's total cost for retirement benefits, included in expenses, is $246.3 million and $219.4 million for the years ended June 30, 2017 and 2016, respectively.

The SERS is the administrator of a cost-sharing, multi-employer retirement system established by the Commonwealth of Pennsylvania to provide pension benefits for employees of state government and certain independent agencies. As provided by statute, the SERS Board of Trustees has exclusive control and management responsibility of the funds and full power to invest the funds. The SERS funding policy provides for periodic member contributions at statutory rates and employer contributions at actuarially determined rates (expressed as a percentage of annual gross pay) that are sufficient to accumulate assets to pay benefits when due. The University's contributions to this plan for the years ended June 30, 2017 and 2016 were $102.6 million and $84.1 million, respectively, and represent approximately 5.7% of total contributions to the plan based on projections for fiscal year 2017. The plan is funded at less than 65% with the funded ratio of the plan at 58.1% as of December 31, 2016.

10. POSTRETIREMENT BENEFITS

The University sponsors a retiree medical plan covering eligible retirees and eligible dependents. This program includes a Preferred Provider Organization (“PPO”) plan (both a traditional and a qualified high deductible option) for retirees and their dependents who are not eligible for Medicare, and a Medicare Advantage PPO plan. In addition, the University provides certain retiree life insurance benefits to the retiree.

Employees who were hired prior to January 1, 2010 are eligible for medical coverage after they retire if either of the following requirements are satisfied:

- they are at least age 60 and have at least 15 years of regular full-time employment and participation in a University-sponsored medical plan immediately preceding the retirement date
- regardless of age, if they have at least 25 years of regular full-time service. The last 10 of those 25 years of University service must be continuous and they must participate in a University-sponsored medical plan during the last 10 years immediately preceding the retirement date.

Effective January 1, 2016, any non-union employee who retires on or before December 31, 2020 will receive a $5,000 term life insurance policy benefit at no cost to the employee. If a non-union employee retires after December 31, 2020, no life insurance benefit is provided. For union employees, a $5,000 term life insurance policy is provided at no cost to the employee regardless of their retirement date.

The retiree PPO medical plan and the life insurance coverage are self-funded programs, and all medical claims, death benefits and other expenses are paid from the unrestricted net assets of the University. The Medicare Advantage PPO plan is fully-insured. The retirees pay varying amounts for coverage under the medical plan.

For those employees who were hired after December 31, 2009, the University will contribute funds each month on their behalf to a Retirement Healthcare Savings Plan. This plan is designed to help pay for qualified medical and health-related expenses in retirement, including the purchase of a health insurance policy.

Retirees will be eligible to access their Retirement Healthcare Savings Plan account when they are no longer actively employed at Penn State and have satisfied either of the following requirements:

- completed 25 years of continuous full-time service and are age 60 or older
- completed a minimum of 15 years of continuous full-time service and are age 65 or older.

Included in unrestricted net assets at June 30, 2017 and 2016 are the following amounts that have not yet been recognized in net periodic postretirement cost: unrecognized prior service cost (benefit) of ($8.5) million and ($21.0) million and unrecognized actuarial loss of $707.6 million and $669.1 million, respectively.

The following sets forth the plan's benefit obligation, plan assets and funded status reconciled with the amounts recognized in the University's consolidated statements of financial position at June 30:

Change in benefit obligation:
(in thousands of dollars)

	2017	2016
Benefit obligation at beginning of year	$ 2,148,522	$ 2,091,086
Service cost	50,368	44,524
Interest cost	90,719	88,671
Actuarial loss (gain)	33,287	(199,832)
Benefits paid	(51,860)	(45,490)
Plan amendment	(6,845)	-
Plan assumptions	54,271	169,563
Benefit obligation at end of year	$ 2,318,462	$ 2,148,522

Change in plan assets:
(in thousands of dollars)

	2017	2016
Fair value of plan assets at beginning of year	$ -	$ -
Employer contributions	51,860	45,490
Benefits paid	(51,860)	(45,490)
Fair value of plan assets at end of year	$ -	$ -
Funded status	$ (2,318,462)	$ (2,148,522)
Unrecognized prior service cost (benefit)	-	-
Unrecognized net actuarial loss	-	-
Accrued postretirement benefit expense	$ (2,318,462)	$ (2,148,522)

Net periodic postretirement cost includes the following components for the years ended June 30:
(in thousands of dollars)

	2017	2016
Service cost	$ 50,368	$ 44,524
Interest cost	90,719	88,671
Amortization of prior service cost	(19,392)	(21,849)
Amortization of unrecognized net loss	48,990	33,222
Net periodic postretirement cost	$ 170,685	$ 144,568

The assumed healthcare cost trend rate used in measuring the accumulated postretirement benefit obligation was 7.50% and 7.00% for the years ended June 30, 2017 and 2016, respectively, reduced each year to an ultimate level of 5.00%. The postretirement benefit obligation discount rate was 4.21% for the years ended June 30, 2017 and 2016.

If the healthcare cost trend rate assumptions were increased by 1% in each year, the accumulated postretirement benefit obligation would be increased by $498.4 million and $461.2 million as of June 30, 2017 and 2016, respectively. The effect of this change on the sum of the service cost and interest cost components of the net periodic postretirement benefit cost would be an increase of $35.5 million and $32.4 million as of June 30, 2017 and 2016, respectively. If the healthcare cost trend rate assumptions were decreased by 1% in each year, the accumulated postretirement benefit obligation would be decreased by $384.9 million and $360.2 million as of June 30, 2017 and 2016, respectively. The effect of this change on the sum of the service cost and interest cost components of the net periodic postretirement benefit cost would be a decrease of $26.6 million and $24.4 million as of June 30, 2017 and 2016, respectively.

Gains and losses in excess of 10% of the accumulated postretirement benefit obligation are amortized over the average future service to assumed retirement of active participants.

Postretirement benefits expected to be paid for the years ended June 30 are as follows:

	(in thousands of dollars)
2018	$ 56,467
2019	61,610
2020	66,645
2021	77,020
2022	77,599
2023-27	477,063

11. PENN STATE HEALTH

Penn State Health was organized exclusively for the charitable, educational, and scientific purposes as defined and limited by Section 501(c)(3) of the Internal Revenue Code of 1986. The Health System's purpose is to promote, support and further the charitable, educational, and scientific purposes of the University. The Health System is controlled by and affiliated with the University. During 2015, the Health System was organized, with the University as the sole owner, to provide oversight and governance of an expanded health enterprise. The Health System will own, in whole or in part, health care facilities which could include hospitals, surgery centers, home health providers and similar organizations.

Medical Center

In May 2016, the ownership of TMSHMC transferred from the University to the Health System. TMSHMC is a 532-bed, not-for-profit acute care academic medical center located in Hershey, Pennsylvania. The University retains ownership of the buildings and land occupied by TMSHMC, which is co-located with the University's College of Medicine. The clinical facilities of the Medical Center complex are leased to TMSHMC. TMSHMC makes certain payments to support the College of Medicine.

Nittany Health

In January 2016, the ownership of Nittany Health transferred from the University to the Health System. Nittany Health is a corporate investor in healthcare joint ventures, which are supportive of the missions of the Health System. Nittany Health's objectives are consistent with the strategic objective to extend the range of healthcare services offered by and through the Health System over a broader geographic region. Nittany Health was organized in 1995 for the purpose of organizing components of an integrated health care delivery system. Nittany Health recorded non-controlling interest related to the acquisition of additional ownership interest in a joint venture. This non-controlling interest is recorded in net assets within the consolidated statements of financial position with a value at June 30, 2017 and 2016 of $4,609,000 and $3,687,000, respectively.

Saint Joseph's Regional Health Network and Medical Group

In July 2015, the Health System acquired SJRHN/SJMG. SJRHN/SJMG is a 144-bed, not-for-profit acute care hospital that provides inpatient, outpatient, and emergency care services to the Berks County Region.

Pursuant to the Health System's purchase accounting for acquisitions policy, the total purchase for SJRHN/SJMG was allocated to both tangible/intangible assets and liabilities based upon their estimated fair values. There was no goodwill associated with this transaction.

The following represents the allocation of the purchase price for the acquisition, as described above (in thousands):

Net accounts receivable	$ 26,042
Property, plant & equipment	104,446
Intangible assets	1,489
Other assets	21,975
Liabilities assumed	(24,812)
Temporarily restricted net assets	(4,730)
Permanently restricted net assets	(10,862)
Total net assets acquired	$113,548
Total purchase price	$113,548

Penn State Community Medical Group

In February 2017, the Health System established the Penn State Community Medical Group, LLC ("PSCMG"). The purpose of PSCMG is to extend the ambulatory clinical footprint of the Health System into broader geographic regions. PSCMG became active on October 1, 2017.

12. CONTINGENCIES AND COMMITMENTS

Contractual Obligations

The University has contractual obligations for the construction of new buildings and for additions to existing buildings in the amount of $1,313.8 million of which $951.7 million has been paid or accrued as of June 30, 2017. The contract costs are being financed from available resources and from borrowings.

Letters of Credit

The University has available letters of credit in the amount of $25.7 million and $23.9 million as of June 30, 2017 and 2016, respectively. These letters of credit are used primarily to comply with minimum state and federal regulatory laws that govern various University activities. The fair value of these letters of credit approximates contract values based on the nature of the fee arrangements with the issuing banks.

Guarantees

The University has a contract with a third party whereby the third party acts as an agent of the University in connection with procurement of electricity. The University guarantees the payment of the obligations of the third party incurred on behalf of the University to counterparties. No liabilities related to guarantees have been recorded as of June 30, 2017.

Self-Insurance

The University has a coordinated program of commercial and self-insurance for medical malpractice claims at TMSHMC through the use of a qualified trust and a domestic captive insurance company in combination with a self-insured retention layer and is supplementing this program through participation in the Pennsylvania Medical Care Availability and Reduction of Error Fund ("MCARE Fund"), in accordance with Pennsylvania law. An estimate of the present value, discounted at 2% for the years ended June 30, 2017 and 2016, of the medical malpractice claims liability in the amount of $120.4 million and $107.4 million is recorded as of June 30, 2017 and 2016, respectively.

The subsidiaries of the Health System are self-insured for all medical malpractice claims asserted on or after July 1, 2003, for all amounts that are below the coverage of excess insurance policies and not included in the insurance coverage of the MCARE Fund. Under the self-insurance program, the Health System is required to maintain a malpractice trust fund in an amount at least equal to the expected loss of known claims. The balance of this trust fund was $27.4 million and $21.5 million at June 30, 2017 and 2016, respectively. The Health System intends to fund any claims due during the next year from cash flows from operations.

With approval from the Pennsylvania Department of Labor and Industry ("PA-DLI"), the University elected to self-insure potential obligations applicable to Pennsylvania workers' compensation. Certain claims under the program are contractually administered by a private agency. The University purchased insurance coverage for excess obligations over $600,000 per incident. An estimate of the self-insured workers' compensation claims liability in the amount of $7.0 million and $8.1 million, discounted at 1.89% and 1.00%, respectively, is recorded as of June 30, 2017 and 2016, respectively. The University has established a trust fund, in the amount of $13.2 million and $13.3 million at June 30, 2017 and 2016, respectively, as required by PA-DLI, to provide for the payment of claims under this self-insurance program. TMSHMC and SJRHN/SJMG are self-insured for workers' compensation claims and have purchased excess policies through commercial insurers which cover individual claims in excess of $750,000 and $575,000 per incident, respectively, for workers' compensation claims.

The University and the Health System are self-insured for certain health care benefits provided to employees. The University, TMSHMC and SJRHN/SJMG have purchased excess policies which cover employee health benefit claims in excess of $600,000, $575,000 and $375,000 per employee per year, respectively. The University and the Health System provide for reported claims and claims incurred but not reported.

<u>Litigation and Contingencies</u>

In November 2011, the University was made aware of certain allegations in a Commonwealth of Pennsylvania Grand Jury presentment. Various legal proceedings and investigations have arisen as a result of such allegations, including criminal proceedings against former officers and employees of the University. Certain claims and civil litigation have been filed against the University with anticipation that other complaints could be filed. The University has accrued $16.0 million and $0.2 million for the years ended June 30, 2017 and 2016, respectively, with such amounts included in institutional support within the consolidated statement of activities. Additional claims could be paid in the future but without having knowledge of the number and nature of such claims the University is unable to predict the outcome of these matters or the ultimate legal and financial liability and at this time cannot reasonably estimate the possible loss or range of loss. Accordingly, no amounts have been accrued in the financial statements for these claims.

In addition to the settlement costs, the University has incurred costs for the fiscal years ended June 30, 2017 and 2016 totaling $4.9 million and $6.6 million, respectively, for internal investigation, legal, communications and other related costs. These costs are included in institutional support within the consolidated statement of activities.

By jury verdict and court orders in October and November 2016 and March 2017, the University was found liable for compensatory and punitive damages of $12.3 million and was ordered to pay attorney's fees and costs of $1.7 million in a lawsuit brought by a former employee alleging whistleblower liability, defamation and misrepresentation. In October 2017, the University agreed to settle with the plaintiff for a lesser amount pursuant to a confidential settlement agreement. The amount per the settlement agreement is accrued as of June 30, 2017 and included in institutional support within the consolidated statement of activities.

The University has submitted claims to insurance carriers related to the claims that have been settled or paid. Some insurance claims have been paid and other insurance claims remain outstanding.

Based on its operation of the Health System (see Note 11), the University, like the rest of the healthcare industry, is subject to numerous laws and regulations of federal, state and local governments. Compliance with these laws and regulations can be subject to government review and interpretation, as well as regulatory actions. Recently, government reviews of healthcare providers for compliance with regulations have increased. Although the University believes it has done its best to comply with these numerous regulations, such government reviews could result in significant repayments of previously billed and collected revenues from patient services.

On July 12, 2013, the University received a preliminary report from the U.S. Department of Education based on the program review of the University's compliance with the Clery Act, a federal law related to campus safety. A final program review determination was made in November 2016, which assessed a fine in the amount of $2.4 million. The fine has been paid and the Department of Education's program review is now closed.

Various other legal proceedings have arisen in the normal course of conducting University business. The outcome of such litigation is not expected to have a material effect on the financial position of the University.

13. SUBSEQUENT EVENTS

The University has evaluated subsequent events through October 20, 2017, the date on which the consolidated financial statements were issued. It did not identify any subsequent events to be disclosed other than those below or previously noted.