



UNIVERSITY OF DELAWARE

Consolidated Financial Statements

June 30, 2013

(With Independent Auditors' Report Thereon)

UNIVERSITY OF DELAWARE

Table of Contents

	Page(s)
Independent Auditors' Report	1
Consolidated Statement of Financial Position, June 30, 2013	3
Consolidated Statement of Activities, Year ended June 30, 2013	4
Consolidated Statement of Expenses by Natural Classification, Year ended June 30, 2013	5
Consolidated Statement of Cash Flows, Year ended June 30, 2013	6
Notes to Consolidated Financial Statements	7



KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

The Board of Trustees
University of Delaware:

We have audited the accompanying consolidated financial statements of the University of Delaware and subsidiaries (the University), which comprise the consolidated statement of financial position as of June 30, 2013, and the related consolidated statements of activities, expenses by natural classification, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the University of Delaware and its subsidiaries as of June 30, 2013, and the changes in their net assets and their cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.



Report on Summarized Comparative Information

We have previously audited the University's 2012 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated November 7, 2012. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2012 is consistent, in all material respects, with the audited financial statements from which it has been derived.

KPMG LLP

Philadelphia, Pennsylvania
October 28, 2013

UNIVERSITY OF DELAWARE

Consolidated Statement of Financial Position

June 30, 2013

(with summarized financial information as of June 30, 2012)

(In thousands)

Assets	2013	2012
Cash and cash equivalents	\$ 41,717	45,433
Accounts and notes receivable	38,637	45,268
Prepaid expenses and inventories	4,624	5,813
Restricted deposits	146,452	58,321
Contributions receivable	34,771	32,273
Student loan receivables	13,286	14,123
Endowment funds and other investments	1,460,586	1,314,530
Annuity and life income funds	8,377	7,731
Funds held in trust by others	60,653	58,209
Property, plant, and equipment, net of depreciation	1,321,631	1,195,830
Total assets	\$ 3,130,734	2,777,531
Liabilities and Net Assets		
Accounts payable and accrued liabilities	\$ 88,820	77,451
Deferred revenues and student deposits	8,943	8,329
Financing obligations	17,985	6,557
Notes and bonds payable	489,049	353,993
Interest rate swap liabilities	24,478	41,487
Annuity and life income funds payable	4,986	4,785
Compensated absences payable	13,904	13,465
Postretirement benefit obligation	264,738	283,690
Advances from federal government for student loans	15,094	14,995
Asset retirement obligation	22,112	20,889
Total liabilities	950,109	825,641
Unrestricted	1,248,794	1,085,224
Unrestricted – noncontrolling interest in First State Marine Wind, LLC	1,341	1,551
Temporarily restricted	587,306	533,671
Permanently restricted	343,184	331,444
Total net assets	2,180,625	1,951,890
Total liabilities and net assets	\$ 3,130,734	2,777,531

See accompanying notes to consolidated financial statements.

UNIVERSITY OF DELAWARE
Consolidated Statement of Activities
Year ended June 30, 2013
(with summarized financial information for the year ended June 30, 2012)
(In thousands)

	2013			2012	
	Unrestricted	Temporarily restricted	Permanently restricted	Total	Total
Operating revenue:					
Tuition and fees (less scholarships and fellowships of \$117,508 during 2013, \$106,186 during 2012)	\$ 370,912	—	—	370,912	354,844
Contributions	22,040	1,443	—	23,483	25,048
Contracts and other exchange transactions	172,725	—	—	172,725	165,692
State operating appropriations	115,072	—	—	115,072	112,427
Endowment spending payout	46,557	—	—	46,557	44,603
Other investments payout (includes net realized gain of \$4,141 during 2013 and \$3,473 during 2012)	6,056	54	—	6,110	6,294
Activities of educational departments	16,466	—	—	16,466	13,919
Sales and services of auxiliary enterprises (less scholarships and fellowships of \$1,930 during 2013, \$1,113 during 2012)	116,795	—	—	116,795	110,657
Other revenue	16,300	—	—	16,300	17,501
Total operating revenue	<u>882,923</u>	<u>1,497</u>	<u>—</u>	<u>884,420</u>	<u>850,985</u>
Operating expenses:					
Educational and general:					
Instruction and departmental research	359,645	—	—	359,645	346,420
Sponsored research	139,473	—	—	139,473	135,079
Extension and public service	47,905	—	—	47,905	46,780
Academic support	65,316	—	—	65,316	58,566
Student services	30,541	—	—	30,541	28,821
General institutional support	90,260	—	—	90,260	82,114
Student aid	6,521	—	—	6,521	5,884
Total educational and general expenses	<u>739,661</u>	<u>—</u>	<u>—</u>	<u>739,661</u>	<u>703,664</u>
Auxiliary enterprises	100,209	—	—	100,209	95,633
Independent operations	884	—	—	884	679
Total operating expenses	<u>840,754</u>	<u>—</u>	<u>—</u>	<u>840,754</u>	<u>799,976</u>
Change in net assets from operating activities	42,169	1,497	—	43,666	51,009
Nonoperating activities:					
Net realized and unrealized gains (losses)	59,237	75,380	4,009	138,626	(61,428)
Decrease (increase) in postretirement benefit obligation	38,387	—	—	38,387	(59,476)
Endowment income	2,869	8,026	718	11,613	15,832
Endowment spending payout	(46,557)	—	—	(46,557)	(44,603)
Contributions for endowment and life income funds	—	135	9,688	9,823	13,033
Contributions for buildings and program activities	2,498	14,503	—	17,001	25,707
State capital appropriations	14,380	—	—	14,380	3,889
Hotel operations – net	912	—	—	912	(1,370)
Wind turbine operations – net	(380)	—	—	(380)	(194)
Net change in asset retirement obligation liability	(425)	—	—	(425)	38
Other	2,595	397	(1,303)	1,689	6,471
Reclassifications of funds	(1,367)	2,739	(1,372)	—	—
Net assets released from restrictions	49,042	(49,042)	—	—	—
Change in net assets	<u>163,360</u>	<u>53,635</u>	<u>11,740</u>	<u>228,735</u>	<u>(51,092)</u>
Net assets at beginning of year	<u>1,086,775</u>	<u>533,671</u>	<u>331,444</u>	<u>1,951,890</u>	<u>2,002,982</u>
Net assets at end of year	<u>\$ 1,250,135</u>	<u>587,306</u>	<u>343,184</u>	<u>2,180,625</u>	<u>1,951,890</u>

See accompanying notes to consolidated financial statements.

UNIVERSITY OF DELAWARE

Consolidated Statement of Expenses by Natural Classification
 Year ended June 30, 2013
 (with summarized financial information for the year ended June 30, 2012)
 (In thousands)

	2013									2012	
	Instruction and departmental research	Sponsored research	Extension and public service	Academic support	Student services	General institutional support	Student aid	Auxiliary enterprises	Independent operations	Total	Total
Operating expenses:											
Expenses:											
Salaries and wages	\$ 200,548	64,046	23,483	28,366	14,119	40,965	3,419	8,374	—	383,320	365,067
Employee fringe benefits	54,878	14,878	6,988	11,184	4,342	15,589	—	2,852	—	110,711	107,598
Employee postretirement benefits	16,003	2,821	1,182	1,463	523	1,988	—	371	—	24,351	19,742
Supplies and general	36,387	37,584	9,990	8,381	6,697	24,338	834	64,755	549	189,515	177,201
Travel	14,983	3,248	1,265	777	850	582	125	144	2	21,976	21,473
Operation and maintenance of plant	24,609	7,319	2,848	5,360	1,290	10,053	—	—	330	51,809	49,877
Information processing	60	7	1	(30)	2,939	8,460	—	—	—	11,437	11,819
Interest expense	2,645	517	—	—	251	37	—	13,975	—	17,425	16,551
Scholarships, fellowships and awards	—	—	—	—	—	—	119,613	—	—	119,613	107,375
Depreciation and accretion	13,443	9,189	2,213	10,490	579	7,238	—	10,960	3	54,115	53,014
Loss on disposals	248	389	26	16	2	272	—	234	—	1,187	4,640
Amortization of bond discount (premium)	24	23	—	—	(45)	—	—	(295)	—	(293)	(169)
Internal service (credits) charges	(2,856)	(62)	30	(672)	(991)	(19,262)	—	(1,161)	—	(24,974)	(26,914)
Expense before scholarship allowance	360,972	139,959	48,026	65,335	30,556	90,260	123,991	100,209	884	960,192	907,274
Reconciliation to statement of activities:											
Scholarship allowance	(1,327)	(486)	(121)	(19)	(15)	—	(117,470)	—	—	(119,438)	(107,298)
Total operating expenses	\$ 359,645	139,473	47,905	65,316	30,541	90,260	6,521	100,209	884	840,754	799,976

Notes:

- (a) Includes salaries and wages of \$24,746, fringe benefits of \$13,502, employee postretirement benefits of \$455, and depreciation expense for plant facilities of \$1,043 during 2013.
- (b) Includes salaries and wages of \$24,613, fringe benefits of \$13,555, employee postretirement benefits of \$344, and depreciation expense for plant facilities of \$955 during 2012.

See accompanying notes to consolidated financial statements.

UNIVERSITY OF DELAWARE
Consolidated Statement of Cash Flows
Year ended June 30, 2013
(with summarized financial information for the year ended June 30, 2012)
(In thousands)

	<u>2013</u>	<u>2012</u>
Cash flows from operating activities:		
Change in net assets	\$ 228,735	(51,092)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	55,720	54,487
Loss on disposals	1,187	4,640
Amortization of discounts and premiums on notes and bonds payable and capital lease obligations	(283)	(158)
Net realized and unrealized (gains) losses	(122,072)	38,996
Gifts of land, building, and equipment	(473)	(393)
State capital appropriations	(14,380)	(3,889)
Contributions for endowment	(9,823)	(13,033)
Contributions for buildings	(14,503)	(15,476)
Endowment income restricted for reinvestment	(718)	(633)
Changes in assets and liabilities:		
Accounts and notes receivable	6,631	4,645
Prepaid expenses and inventories	1,189	(1,105)
Contributions receivable	(2,498)	(10,232)
Accounts payable, accrued liabilities, and annuity and life income funds payable	11,278	(1,080)
Deferred revenues and students deposits	614	(770)
Interest rate swap liability	(15,038)	20,053
Asset retirement obligation	944	485
Compensated absences payable and postretirement benefit obligation	(18,513)	74,230
Net cash provided by operating activities	<u>107,997</u>	<u>99,675</u>
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	1,665,970	1,201,224
Purchases of investments	(1,693,039)	(1,193,499)
Acquisitions of property, plant, and equipment	(170,169)	(179,688)
Disbursements of loans to students	(1,594)	(1,633)
Repayments of loans	2,431	2,229
Net cash used in investing activities	<u>(196,401)</u>	<u>(171,367)</u>
Cash flows from financing activities:		
Repayments of principal of notes and bonds payable	(13,139)	(9,773)
Net proceeds from issuance of notes and bonds payable	148,501	—
Reduction in principal of capital leases	(595)	(565)
Termination of interest rate swap agreements	(1,971)	—
Increase in financing obligations	500	—
State capital appropriations	14,380	3,889
Endowment income restricted for reinvestment	718	633
Contributions for endowment	9,823	13,033
Contributions for buildings	14,503	15,476
Advances from federal government for student loans	99	92
(Increase) decrease in restricted deposits	(88,131)	53,663
Net cash provided by financing activities	<u>84,688</u>	<u>76,448</u>
Net (decrease) increase in cash and cash equivalents	(3,716)	4,756
Cash and cash equivalents, beginning of year	45,433	40,677
Cash and cash equivalents, end of year	<u>\$ 41,717</u>	<u>45,433</u>
Supplemental disclosure of cash flow information:		
Interest paid	\$ 17,425	16,865

See accompanying notes to consolidated financial statements.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(1) Summary of Significant Accounting Policies

(a) Description of Operations

The University of Delaware (the University), a privately chartered university with public support, is a Doctoral/Research Institution-Extensive, land-grant, sea-grant, space-grant, and urban-grant institution. The University, with origins in 1743, was chartered by the State of Delaware (the State) in 1833. A Women's College was opened in 1914, and in 1945, the University became permanently co-educational. The main campus is located in Newark, Delaware, a suburban community of 30,000, situated midway between Philadelphia and Baltimore. Also, courses are offered at other locations throughout the State, including Wilmington, Lewes, Dover, Milford, and Georgetown.

The significant accounting principles and practices followed by the University are presented below to assist the reader in analyzing the consolidated financial statements and accompanying notes.

(b) Basis of Presentation

The consolidated financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. generally accepted accounting principles (U.S. GAAP). Accordingly, such information should be read in conjunction with the University's consolidated financial statements for the year ended June 30, 2012, from which the summarized information was derived.

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Restricted gifts, which may be expended only for the purpose indicated by the donor/grantor, are maintained in separate accounts in the University's system. Accordingly, net assets of the University and changes therein are classified and reported as follows:

- Unrestricted net assets – Net assets that are not subject to donor-imposed stipulations.
- Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that may or will be met by actions of the University and/or the passage of time.
- Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the University. Generally, the donors of these assets permit the University to use all of, or part of, the total investment return on related investments for general or specific purposes.

There are three financial statements presented under U.S. GAAP for not-for-profit organizations:

Statement of Financial Position – is a listing of the total assets, total liabilities, and net assets as of the end of a fiscal year.

Statement of Activities – is a summary of the financial activity during a fiscal year and reports the amounts of the changes in unrestricted net assets, temporarily restricted net assets, permanently restricted net assets, and total net assets.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Statement of Cash Flows – is a summary of the cash receipts and cash payments during a fiscal year.

As a supplement to the financial statements, the statement of expenses by natural classification presents expenses by natural classification within functional categories. Operation and maintenance of plant, depreciation and accretion expense, and disposals are allocated based on square footage. Postretirement benefit obligation expense and fringe benefit expense are allocated based on salaries and wages. Interest expense and amortization of bond discount are allocated to the functional classification that benefited from the use of the proceeds of the debt.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as released from restrictions between the applicable classes of net assets.

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value.

Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the unrestricted net asset class. Income and realized and unrealized net gains on investments of endowment and similar funds are reported as follows:

- as increases in permanently restricted net assets if the terms of the gift or the University's interpretation of relevant state law require that they be added to the principal of a permanent endowment fund.
- as increases in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income or the income is not available to be used until appropriated by the University under state law.

(c) *Reclassifications of Funds*

The reclassification of funds includes transfers of operating funds designated by the University for investment in endowment or in plant, and financial transactions between net asset classes.

(d) *Auxiliary Operations*

The operation of auxiliaries is supplementary to the primary educational function of the University. Accordingly, revenues of auxiliary enterprises provide for debt service, and renewal and replacement of equipment. Auxiliary operations primarily include the residence and dining halls, the bookstore, and student health service.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(e) Cash and Cash Equivalents

Cash equivalents include all highly liquid interest-bearing deposits and short-term investments with maturities of three months or less at time of purchase, excluding amounts held for long-term investments as disclosed in note 6.

(f) Restricted Deposits

Restricted deposits as of June 30, 2013 and 2012 consisted of the following (in thousands):

	<u>2013</u>	<u>2012</u>
Unexpended bond proceeds	\$ 125,467	41,333
Debt service reserve funds	16,861	14,008
Other deposits	4,124	2,980
	<u>\$ 146,452</u>	<u>58,321</u>

Unexpended bond proceeds represent the amount of unspent revenue bond proceeds that remain on deposit with the trustee. Under terms of the trust agreement, proceeds are not released to the University until expenditures related to the specific purpose of the bond indenture have occurred. These amounts are generally invested in cash equivalents and short-term U.S. government or commercial securities with maturities that support the anticipated cash flow of the underlying construction projects.

Debt service reserve funds are also held with the trustee. The University transfers funds to the trustee in accordance with bond covenant agreements to meet future bond payments. These funds remain on deposit until scheduled interest payments and scheduled or optional redemption principal payments are made, as disclosed in note 11. These funds are generally invested in cash equivalents.

Other deposits are under the control of the University but are restricted in their use. These funds may be held for federal loan programs or for the benefit of or under regulations promulgated by the federal government. These funds are generally invested in cash equivalents.

(g) Endowment Funds and Other Investments

Investments are stated at estimated fair value, as described in note 3.

(h) Compensated Absences Payable

Compensated absences payable represents vacation time earned by full-time professional and salaried staff employees, but not yet taken as of fiscal year-end. An employee is entitled to receive pay in lieu of vacation upon separation from the University. Employees may accrue a maximum of 25 days to 40 days based upon years of service.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(i) *Operating Versus Nonoperating*

Operating activities consist principally of revenues and expenses related to the University's ongoing educational, research and public service mission, including endowment and other investment income appropriated by the University to support these programs.

(j) *Income Taxes*

The University has been recognized by the Internal Revenue Service (IRS) as exempt from federal income tax under Section 501(c)(3) of the U.S. Internal Revenue Code, except for taxes on income from activities unrelated to its exempt purpose. Accordingly, no provisions for income taxes have been made in the accompanying consolidated financial statements. U.S. GAAP require management to evaluate tax positions taken by the University and recognize a tax liability (or asset) if the University has taken an uncertain tax position that more likely than not would not be sustained upon examination by the IRS. Management has analyzed the tax positions taken by the University, and has concluded that as of June 30, 2013, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the consolidated financial statements. The University is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

(k) *Estimates*

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amount of revenue and expenses during the reporting period. Actual results could differ from these estimates.

(l) *Impact of Recent Accounting Pronouncements*

In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs* (ASU 2011-04), which does not extend the use of fair value, but rather provides guidance about how fair value should be determined where it is already required or permitted under International Financial Reporting Standards (IFRS) or U.S. GAAP. For U.S. GAAP, most of the changes are clarifications of existing guidance or wording changes to align with IFRS. For public entities, the ASU was effective for periods beginning after December 15, 2011. The adoption of ASU 2011-04 only required additional disclosures and did not have a material impact on the consolidated financial statements.

In December 2011, the FASB issued ASU 2011-11, *Balance Sheet (Topic 210) Disclosure about Offsetting Assets and Liabilities* (ASU 2011-11). The amendments enhance disclosures about financial instruments and derivative instruments that are either offset in accordance with U.S. GAAP or are subject to an enforceable master netting arrangement or similar agreement. The disclosure provisions of ASU 2011-11 are effective for annual reporting periods beginning on or after January 1, 2013, and should be applied retrospectively for all comparative periods presented. In January 2012, the FASB issued ASU 2013-01, *Balance Sheet (Topic 210) Clarifying the Scope of*

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Disclosures about Offsetting Assets and Liabilities (ASU 2013-01), which clarifies that the scope of ASU 2011-11 applies to derivatives accounted for in accordance with *Topic 815, Derivatives and Hedging*. Entities with other types of financial assets and financial liabilities subject to a master netting arrangement, or similar agreement, also are affected because the amendments make them no longer subject to the disclosure requirements in ASU 2011-11. The adoption of ASU 2011-11 and ASU 2013-01 will not have a material impact on the consolidated financial statements.

In October 2012, the FASB issued ASU 2012-05, *Statement of Cash Flows (Topic 230) Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows*, (ASU 2012-05), which requires a Not-for-Profit (NFP) to classify cash receipts from the sale of donated financial assets consistently with cash donations received in the statement of cash flows if those cash receipts were from the sale of donated financial assets that upon receipt were directed without any NFP-imposed limitations for sale and were converted nearly immediately into cash. Accordingly, the cash receipts from the sale of those financial assets should be classified as cash inflows from operating activities, unless the donor restricted the use of the contributed resources to long-term purposes, in which case those cash receipts should be classified as cash flows from financing activities. Otherwise, cash receipts from the sale of donated financial assets should be classified as cash flows from investing activities by the NFP. ASU 2012-05 is effective prospectively for fiscal years, and interim periods within those years, beginning after June 15, 2013. Retrospective application to all prior periods presented upon the date of adoption is permitted, as is early adoption from the beginning of the fiscal year of adoption. The University does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

In February 2013, the FASB issued ASU 2013-04, *Liabilities (Topic 405) Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date* (ASU 2013-04). This ASU applies to all entities that have obligations resulting from joint and several liability arrangements for which the total amount of the obligation within this guidance is fixed at the reporting date and for which no specific guidance exists. It specifies that the obligation be measured at the reporting date as the sum of the amount the reporting entity agreed to pay on the basis of its arrangement amount its co-obligors, plus any additional amount the reporting entity expects to pay on behalf of its co-obligors. The ASU also requires an entity to disclose the nature, amount and other specified information about the obligation. ASU 2013-04 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. The University does not expect the adoption of this ASU to have a material impact on its consolidated financial statements.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

In April 2013, the FASB issued ASU 2013-06, *Not-for-Profit Entities (Topic 958), Services Received from Personnel of an Affiliate* (ASU 2013-06), which require a recipient NFP entity to recognize all services received from personnel of an affiliate that directly benefit the recipient not-for-profit entity. The ASU is effective prospectively for fiscal years beginning after June 15, 2014, and interim and annual periods thereafter, but allows a recipient NFP entity to apply the amendments using a modified retrospective approach under which all periods presented upon the date of adoption should be adjusted, but no adjustment should be made to the beginning balance of net assets of the earliest period presented. Early adoption is permitted. The University does not expect the adoption of ASU 2013-06 to have a material impact on its consolidated financial statements.

(m) *Reclassifications*

Certain prior year financial information has been reclassified to conform to the current year presentation.

(2) **Subsidiary Operations**

In October 2009, Blue Hen Wind, Inc. was created as a wholly owned, for-profit, subsidiary of the University. Simultaneously, Blue Hen Wind, Inc. entered into a Limited Liability Company Agreement with Gamesa Technology Corporation, Inc. and formed First State Marine Wind, LLC for the purpose of constructing and operating a wind turbine adjacent to the University's Hugh R. Sharp campus in Lewes. At inception, Blue Hen Wind, Inc. had a 49% ownership interest in First State Marine Wind, LLC. Blue Hen Wind, Inc.'s ownership interest has subsequently increased to approximately 67% at June 30, 2013.

The operations of Blue Hen Wind, Inc. are consolidated into the University's financial statements. Operations for the year ended June 30, 2013, resulted in revenues from third parties of \$29,000 and expenses of \$409,000 being recognized. Operations for the year ended June 30, 2012, resulted in revenues from third parties of \$56,000 and expenses of \$250,000 being recognized. Gamesa Technology Corporation, Inc.'s noncontrolling interest in First State Marine Wind, LLC is presented as a separate component of net assets in the consolidated statement of financial position.

In December 2008, 1743 Holdings, LLC was created as a wholly owned subsidiary of the University for the purpose of purchasing and managing a 272-acre site that was formerly occupied by a Chrysler Corporation automobile assembly plant, which is contiguous to the University's 968-acre Newark campus. That property was acquired during fiscal 2010 for a purchase price of \$24,250,000 and is known as the Science, Technology and Advanced Research (STAR) campus.

The operations of 1743 Holdings, LLC are consolidated into the University's financial statements. Operations for the year ended June 30, 2013 resulted in operating expenses of \$884,000, nonoperating expenses of \$496,000 and nonoperating revenue – other of \$4,008,000, which are presented in independent operations and nonoperating activities in the consolidated statement of activities. Operations for the year ended June 30, 2012 resulted in operating expenses of \$679,000 and nonoperating revenue – other of \$6,786,000, which are presented in independent operations and nonoperating activities, respectively, in the consolidated statement of activities.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The University is the sole owner of Blue Hen Hotel, LLC and therefore the operations of Blue Hen Hotel, LLC are consolidated into the University's financial statements. Shaner Hotel Group Limited Partnership manages the hotel under a management contract that provides for a management fee of 3% of gross operating revenues of the LLC.

Operations of Blue Hen Hotel, LLC are reported as nonoperating activities and for the years ended June 30, 2013 and 2012 resulted in total revenues of \$5,480,000 and \$4,996,000, respectively, and gain of \$912,000 and loss of \$1,370,000, respectively. See note 11 for the impact of a related interest rate swap.

(3) Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability (exit price) in the principal or most advantageous market in an orderly transaction between participants at the measurement date and establishes a framework for measuring fair value.

The three levels of the fair value hierarchy are defined as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities that are traded in an active exchange market, as well as U.S. Treasury securities.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets and liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted market prices that are traded less frequently than exchange-traded instruments. This category generally includes certain U.S. government and agency mortgage backed securities, corporate-debt securities certain private debt and equity funds, and certain alternative investments.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category generally includes certain private debt and equity funds and certain other alternative investments.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The above methodology applies in instances in which other accounting pronouncements require or permit fair value measurements; it does not require any new fair value measurements. The carrying amount of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximate fair value because of the short-term maturity of these financial instruments. The University measures its investments, liabilities related to annuity and life-income funds, interest rate swaps related to its debt, and contributions receivable at inception at fair value in accordance with other accounting pronouncements. Additionally, the University discloses the fair value of its outstanding debt. The valuation methodology for each of these items is described below:

(a) Investments

Investments are recorded at fair value as described above. Additional considerations used to categorize investments include:

U.S. government obligations, stock and convertible securities, international investments, and stock futures held directly by the University are classified as Level 1 since quoted prices in active markets are available. When these types of investments are held as part of commingled funds, they are classified as Level 2; although the commingled fund net asset value is available, these funds are not traded in active public markets. Investments in commingled funds can be redeemed at net asset value on at least a monthly basis. Corporate obligations and obligations of agencies of the U.S. government are classified as Level 2 as they are not traded in an active market but are valued using third-party vendor pricing services by custodian banks.

Valuations for limited partnerships, Limited Liability Companies (LLC), and inflation sensitive assets are based on valuations provided by external investment managers or on audited financial statements when available. The University generally uses valuations as reported by investment managers as a practical expedient to estimate fair value without further adjustment. If the manager's reporting date is for a date prior to June 30, the University adjusts the net asset value for any capital contributions or distributions during the period from the investment manager measurement date to June 30. The University has classified those investments that can be redeemed at net asset value at or near the date (within 90 days) of the consolidated statement of financial position as Level 2. The remaining investments contain illiquid underlying assets, which are not publicly traded and for which pricing inputs are unobservable, which may include situations where there is little, if any, market activity for the asset, and require significant judgment or estimation and, therefore, have been classified as Level 3. While manager estimates of fair value are obtained, the University cannot redeem its investments at these estimates for Level 3 assets. The stated lives of the investments vary and they offer no liquidity until the underlying assets are sold.

Other assets classified as Level 2 consist primarily of municipal obligations held in commingled funds, while those classified as Level 3 consist primarily of collateralized mortgage obligations and restricted real estate.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(b) *Annuity and Life Income Funds*

The annuity and life income funds asset represents the fair value of assets held in charitable gift annuities, charitable remainder annuity trusts, and charitable remainder unitrusts. These assets consist primarily of corporate obligations, stock and convertible securities, and international investments and have been classified as Level 2 using the same methodology described above for similar types of underlying assets.

The annuity and life income funds payable represents the present value of future annuity payments due under these agreements, as calculated for each annuity using discount rates and actuarial assumptions consistent with American Council of Gift Annuities standards. These liabilities have been classified as Level 3 as the fair value is determined based upon a discounted cash flow methodology, which required significant judgment and estimation.

(c) *Funds Held in Trust by Others*

Funds held in trust by others represent amounts held by third parties where the University receives an income stream in perpetuity, but the assets are required to be held by a trustee. The University does not own the underlying assets, but rather has a beneficial interest in the trust. These trusts are invested in a combination of readily marketable assets, limited partnerships and land and have been classified as Level 3 since the University will never be able to redeem these assets.

(d) *Debt and Related Interest Rate Swaps*

The fair value of the University's debt is presented in note 11. The fair value of variable rate long-term debt approximates the carrying value because these financial instruments bear interest rates, which approximate current market rates for loans with similar maturities and credit quality. The fair value of the University's fixed rate long-term debt is based upon a discounted cash flow model.

The fair value of the University's interest rate swaps related to its debt obligation is based on a third-party valuation independent of the counterparty. Although a number of observable inputs are utilized in determining the fair value of its swaps, the University has classified this liability as Level 3 as the fair value was determined using a pricing model involving significant judgment and estimation.

(e) *Contributions Receivable*

The University values contributions receivable using the present value of future cash flows as described in note 4. Contributions receivable are not measured at fair value subsequent to this initial measurement because the discount rate selected is to remain constant over time rather than adjusted to reflect changing financial conditions.

(f) *Student Loan Programs*

An estimate of the fair value of loans receivable from students under government loan programs cannot be made because the notes are not marketable and can only be assigned to the U.S. government or its designees.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The following tables present the University's fair value hierarchy for financial instruments that are measured at fair value on a recurring basis as shown on the June 30, 2013 and 2012 consolidated statements of financial position (in thousands):

		June 30, 2013			
		Fair value	Level 1	Level 2	Level 3
Financial assets:					
Investments:					
Money market and other liquid funds	\$	16,986	16,637	349	—
U.S. government obligations:					
Mortgage-backed securities		42,513	5,539	36,974	—
Treasury obligations		48,250	44,724	3,526	—
Other		14,373	7,149	7,224	—
		<u>105,136</u>	<u>57,412</u>	<u>47,724</u>	<u>—</u>
Corporate obligations		221,064	—	221,064	—
Stock and convertible securities		162,911	159,761	3,150	—
International investments		28,179	45	28,134	—
Limited partnerships and LLCs		840,149	—	324,815	515,334
Inflation sensitive asset fund		29,520	—	29,520	—
Stock futures fund		35,972	—	35,972	—
Real estate investment trust		22,807	—	22,807	—
Other		6,239	—	1,472	4,767
Funds held in trust by others		60,653	—	—	60,653
Total	\$	<u><u>1,529,616</u></u>	<u><u>233,855</u></u>	<u><u>715,007</u></u>	<u><u>580,754</u></u>
Financial liabilities:					
Annuity and life income funds payable	\$	4,986	—	—	4,986
Interest rate swaps		24,478	—	—	24,478
Total	\$	<u><u>29,464</u></u>	<u><u>—</u></u>	<u><u>—</u></u>	<u><u>29,464</u></u>

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

		June 30, 2012			
		<u>Fair value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Financial assets:					
Investments:					
Money market and other liquid funds	\$	17,614	17,313	301	—
U.S. government obligations:					
Mortgage-backed securities		40,650	9,316	31,334	—
Treasury obligations		51,327	48,014	3,313	—
Other		5,298	2,757	2,541	—
		<u>97,275</u>	<u>60,087</u>	<u>37,188</u>	<u>—</u>
Corporate obligations		167,715	—	167,715	—
Stock and convertible securities		177,518	174,901	2,617	—
International investments		83,759	81,747	2,012	—
Limited partnerships and LLCs		666,617	—	173,726	492,891
Inflation sensitive asset fund		45,614	—	45,614	—
Stock futures fund		33,117	—	33,117	—
Real estate investment trust		25,568	—	25,568	—
Other		7,464	—	1,758	5,706
Funds held in trust by others		58,209	—	—	58,209
Total	\$	<u>1,380,470</u>	<u>334,048</u>	<u>489,616</u>	<u>556,806</u>
Financial liabilities:					
Annuity and life income funds payable	\$	4,785	—	—	4,785
Interest rate swaps		41,487	—	—	41,487
Total	\$	<u>46,272</u>	<u>—</u>	<u>—</u>	<u>46,272</u>

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The following tables present a reconciliation of the consolidated statements of financial position amounts for financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended June 30, 2013 and 2012 (in thousands):

	<u>Limited Partnerships and LLCs</u>	<u>Funds held in trust by others</u>	<u>Other</u>	<u>Total</u>
Financial assets:				
Balance at June 30, 2012	\$ 492,891	58,209	5,706	556,806
Net realized and unrealized gains	42,597	6,363	—	48,960
Purchases	35,166	28,945	217	64,328
Sales	<u>(55,320)</u>	<u>(32,864)</u>	<u>(1,156)</u>	<u>(89,340)</u>
Total at June 30, 2013	\$ <u>515,334</u>	<u>60,653</u>	<u>4,767</u>	<u>580,754</u>
Change in unrealized gains related to financial instruments still held at June 30, 2013				
	\$ 31,414	4,662	—	36,076
	<u>Interest rate swaps</u>	<u>Annuity and life income funds payable</u>	<u>Total</u>	
Financial liabilities:				
Balance at June 30, 2012	\$ 41,487	4,785	46,272	
Net realized and unrealized (gains) losses	(17,009)	147	(16,862)	
Purchases	—	680	680	
Sales	<u>—</u>	<u>(626)</u>	<u>(626)</u>	
Total at June 30, 2013	\$ <u>24,478</u>	<u>4,986</u>	<u>29,464</u>	
Change in unrealized (gains) losses related to financial instruments still held at June 30, 2013				
	\$ (15,038)	147	(14,891)	

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

	<u>Limited Partnerships and LLCs</u>	<u>Funds held in trust by others</u>	<u>Other</u>	<u>Total</u>
Financial assets:				
Balance at June 30, 2011	\$ 460,889	60,566	7,135	528,590
Net realized and unrealized gains (losses)	18,904	(753)	—	18,151
Purchases	61,598	26,925	282	88,805
Sales	<u>(48,500)</u>	<u>(28,529)</u>	<u>(1,711)</u>	<u>(78,740)</u>
Total at June 30, 2012	\$ <u>492,891</u>	<u>58,209</u>	<u>5,706</u>	<u>556,806</u>
Change in unrealized gains (losses) related to financial instruments still held at June 30, 2012	\$ 10,606	(3,642)	—	6,964
		<u>Interest rate swaps</u>	<u>Annuity and life income funds payable</u>	<u>Total</u>
Financial liabilities:				
Balance at June 30, 2011	\$ 21,434		4,721	26,155
Net realized and unrealized (gains) losses		20,053	(31)	20,022
Purchases		—	698	698
Sales		<u>—</u>	<u>(603)</u>	<u>(603)</u>
Total at June 30, 2012	\$ <u>41,487</u>		<u>4,785</u>	<u>46,272</u>
Change in unrealized (gains) losses related to financial instruments still held at June 30, 2012	\$ 20,053		(31)	20,022

Transfers between leveled assets are based upon beginning of year value of the asset. As of June 30, 2013 and 2012 there were no transfers between Levels.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(4) Contributions Receivable and Conditional Promises

Contributions receivable at June 30, 2013 and 2012 are summarized as follows (in thousands):

	2013	2012
Unconditional promises expected to be collected in:		
Less than one year	\$ 10,015	13,869
One year to five years	24,756	18,404
	\$ 34,771	32,273

The unamortized discount for contributions to be received after one year amounted to \$1,288,000 and \$1,163,000 in 2013 and 2012, respectively. Contributions to be received after one year are discounted at discount rates ranging from 1.5% to 5.0% for the years ended June 30, 2013 and 2012, respectively.

(5) Student Loan Programs

The student loan programs consist primarily of the Perkins Loan and Nursing Student Loan Programs. The U.S. government provides 75% of the funds for the Perkins loans and 90% for Nursing Student loans. The University provides 25% and 10% of the funds, respectively, to support these programs. The portion of the loan program funds that are returnable to the federal government in event of termination of the programs is reflected as advances from federal government for student loans on the consolidated statement of financial position.

(6) Investments

Investments are recorded at fair value as described below and in note 3. Included in investments are endowment funds and other investments. The cost and market value at June 30, 2013 and 2012 were as follows (in thousands):

	2013		2012	
	Cost	Fair value	Cost	Fair value
Money market and other liquid funds	\$ 16,972	16,986	17,614	17,614
U.S. government obligations	104,767	105,136	93,740	97,275
Corporate obligations	219,194	221,064	164,897	167,715
Stock and convertible securities	126,032	162,911	156,686	177,518
International equity investments	34,908	28,179	97,430	83,759
Limited partnerships and LLCs	606,540	840,149	496,909	666,617
Inflation sensitive asset fund	30,823	29,520	44,413	45,614
Stock futures fund	30,614	35,972	33,892	33,117
Real estate investment trust	19,999	22,807	24,380	25,568
Other	6,239	6,239	7,464	7,464
Total	\$ 1,196,088	1,468,963	1,137,425	1,322,261

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Included in the investments table above are \$8,377,000 and \$7,731,000 of annuity and life income funds, which are shown separately on the consolidated statement of financial position at June 30, 2013 and 2012, respectively. Additionally, the University has \$60,653,000 and \$58,209,000 of funds held in trust by others that are shown separately on the consolidated statement of financial position at June 30, 2013 and 2012, respectively, and which are not included in the above table of investments.

The asset allocation of the University's investments involves exposure to a diverse set of markets. The investments within these markets involve various risks such as interest rate, market, sovereign, and credit risks. The University anticipates that the value of its investments may, from time to time, fluctuate substantially as a result of these risks.

The following table presents at June 30, 2013, the attributes of the University's investments in alternative assets that estimate fair value using the net asset value reported by the funds (in thousands):

	<u>Fair value</u>	<u>Estimated remaining lives</u>	<u>Unfunded commitments</u>	<u>Redemption frequency</u>	<u>Redemption notice frequency</u>
Inflation sensitive asset fund	\$ 29,520	N/A	\$ N/A	Monthly	15 days
Stock futures fund	35,972	N/A	N/A	Monthly	30 days
Real estate investment trust	22,807	N/A	N/A	Quarterly	15 days
Limited partnerships and LLCs:					
U.S. corporate debt funds	41,211	N/A	N/A	Monthly	45 days
U.S. equity funds	33,337	N/A	N/A	Monthly	30 days
International equity funds	250,267	N/A	N/A	Monthly	10 days
Multi-strategy fund of funds	197,213	N/A	N/A	Annually	100 days
Long-short hedge fund	29,922	N/A	N/A	Annually	90 days
Private equity	45,502	2 – 8 years	24,795	Not eligible	N/A
Venture capital	37,099	4 – 10 years	9,782	Not eligible	N/A
Hybrid fund of funds	49,283	2 – 8 years	23,445	Not eligible	N/A
Distressed securities	14,507	2 – 9 years	18,745	Not eligible	N/A
Real estate	64,502	1 – 12 years	21,568	Not eligible	N/A
Natural resources	37,454	5 – 11 years	18,445	Not eligible	N/A
Oil and gas	39,852	4 – 8 years	30,302	Not eligible	N/A
	<u>840,149</u>		<u>147,082</u>		
	<u>\$ 928,448</u>		<u>\$ 147,082</u>		

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The following table presents at June 30, 2012, the attributes of the University's investments in alternative assets that estimate fair value using the net asset value reported by the funds (in thousands):

	<u>Fair value</u>	<u>Estimated remaining lives</u>	<u>Unfunded commitments</u>	<u>Redemption frequency</u>	<u>Redemption notice frequency</u>
Inflation sensitive asset fund	\$ 45,614	N/A	\$ N/A	Monthly	15 days
Stock futures fund	33,117	N/A	N/A	Monthly	30 days
Real estate investment trust	25,568	N/A	N/A	Quarterly	15 days
Limited partnerships and LLCs:					
U.S. corporate debt funds	23,640	N/A	N/A	Monthly	45 days
U.S. equity funds	6,469	N/A	N/A	Monthly	30 days
International equity funds	143,617	N/A	N/A	Monthly	10 days
Multi-strategy fund of funds	187,278	N/A	N/A	Annually	100 days
Long-short hedge fund	28,672	N/A	N/A	Annually	90 days
Private equity	45,025	2 – 8 years	29,395	Not eligible	N/A
Venture capital	35,015	4 – 10 years	13,136	Not eligible	N/A
Hybrid fund of funds	53,181	2 – 8 years	6,180	Not eligible	N/A
Distressed securities	23,290	2 – 9 years	17,333	Not eligible	N/A
Real estate	49,159	1 – 12 years	18,626	Not eligible	N/A
Natural resources	37,560	5 – 11 years	13,513	Not eligible	N/A
Oil and gas	33,711	4 – 8 years	11,790	Not eligible	N/A
	<u>666,617</u>		<u>109,973</u>		
	<u>\$ 770,916</u>		<u>\$ 109,973</u>		

Inflation Sensitive Asset Fund

Inflation sensitive assets include liquid investments in assets that are viewed as positively correlated with inflation, including common stocks in energy and other extractive industries, commodities and inflation linked bonds. The investment is made through a commingled fund vehicle.

Stock Futures Fund

The stock futures fund is a pooled fund that uses stock index futures and options in combination with short-term and other liquid debt instruments to approximate the total return of the Standard & Poor's 500 Index. The derivatives are not used to leverage the underlying cash position of this investment, but rather to meet the endowment asset allocation and spending policy targets. The futures contracts and options are stated at fair market value based on their quoted daily settlement prices.

Real Estate Investment Trust

This category is an investment in a common trust fund that invests primarily in securities of entities with activities in or related to the development, operation, and/or ownership of real estate, including real estate investment trusts. The fund may also invest in real estate service companies and non-U.S. companies.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

U.S. Corporate Debt Funds, U.S. Equity Funds, International Equity Funds

These categories are investments that can be redeemed at net asset value at or near the date of the statement of financial position and therefore classified as level 2 assets in the fair value hierarchy tables in note 3.

Multi-Strategy Fund of Funds

This category includes investments in funds of funds that pursue multiple strategies to diversify risks and reduce volatility. The hedge funds that make up these funds of funds invest in a variety of marketable securities, including stocks, bonds, credit-oriented securities, and arbitrage investments. The managers have the ability to shift investments between strategies and between net long and net short positions. The investments in this category are classified as level 3 assets.

Long-Short Hedge Fund

This category includes investments both long and short in U.S. and non-U.S. stocks and other marketable assets. The investment is made through a commingled fund vehicle. The fund is redeemable annually at December 31, and therefore classified as a level 3 asset.

All of the following University partnerships and LLCs receive distributions through the liquidation of the underlying assets of the fund. These investments can never be redeemed with the funds. Distributions from each fund will be received as the underlying investments of the funds are liquidated.

The University is obligated, under certain limited partnership agreements, to make additional capital contributions up to contractual levels. The timing and amounts of the contributions will be determined by the general partner of the respective limited partnership.

Private Equity, Venture Capital, Hybrid Fund of Funds, and Distressed Securities

These categories include illiquid investments in buyout, mezzanine, venture capital, growth equity, and distressed debt held in commingled limited partnership funds and are classified as level 3 assets in the fair value hierarchy tables in note 3.

Real Estate

This category includes illiquid investments in residential and commercial real estate assets, projects, or land held in commingled limited partnership funds. The investments in this category are classified as level 3 assets.

Natural Resources and Oil and Gas

These categories include illiquid assets in timber, oil and gas production, mining, energy, and related businesses held in commingled limited partnership funds and are classified as level 3 assets in the fair value hierarchy tables in note 3.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Return on investments during the periods was as follows (in thousands):

	2013	2012
Interest and dividends	\$ 13,646	18,725
Net realized and unrealized gains (losses)	128,855	(38,986)
Return (loss) on investments	\$ 142,501	(20,261)

Return on investments is classified on the consolidated statement of activities as follows (in thousands):

	2013	2012
Other investments payout	\$ 6,110	6,294
Sales and services of auxiliary enterprises	64	72
Net realized and unrealized gains (losses)	124,714	(42,459)
Endowment income	11,613	15,832
Return (loss) on investments	\$ 142,501	(20,261)

(7) Endowment Funds

The University endowment consists of approximately 932 individual funds established for a variety of purposes. The endowment funds are subdivided into appropriate net asset classifications. The permanently restricted endowment funds, primarily consisting of funds whose return is unrestricted, represent gifts received under circumstances indicating a stipulation of the donor that principal is not to be expended. Temporarily restricted and unrestricted endowment funds represent funds where there is no requirement to maintain the principal.

(a) Interpretation of Relevant Law

Based upon its interpretation of the provisions of Delaware's enacted version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA), the University classifies the portion of donor-restricted endowment funds that is not classified as permanently restricted net assets as temporarily restricted net assets, unless it has previously been appropriated for use by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. At the time of appropriation by the University, and providing there are no additional purpose restrictions in place, the temporarily restricted net assets will be reclassified to unrestricted net assets. As of June 30, 2013 and 2012, the amount of temporarily restricted endowment funds having no purpose restriction was \$370,457,000 and \$342,664,000, respectively. The University classifies as permanently restricted net assets the historical cost value of the original donor-restricted endowment.

(b) Return Objectives and Risk Parameters

The University has adopted investment and spending policies for endowment assets that attempt to provide in perpetuity financial support of the University's educational goals. Toward that end, the University's Board of Trustees, Investment Visiting Committee, and administration have a shared

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

mission to maximize the endowment fund's total return consistent with the University's prudent investment risk constraints. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified period, as well as board-designated funds. Under this policy approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to achieve an average annual real return of at least 5% over time while assuming an acceptable level of investment risk. Actual returns in any year may vary from that amount. To monitor the effectiveness of the investment strategy of endowment funds, performance goals are established and monitored related to benchmark indices and returns earned by comparable endowment funds.

(c) *Strategies Employed for Achieving Objectives*

To satisfy its long-term rate of return objectives, the University employs a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current income (interest and dividends). The University's investment policy includes a target asset allocation, well diversified among suitable asset classes, that is expected to generate, on average, the level of expected return necessary to meet endowment objectives while assuming a level of risk (volatility) consistent with achieving that return.

(d) *Spending Policy and How the Investment Objectives Relate to Spending Policy*

In accordance with Delaware's enacted version of UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund; (2) the purposes of the organization and the donor-restricted endowment fund; (3) general economic conditions; (4) the possible effect of inflation and deflation; (5) the expected total return from income and the appreciation of investments; (6) other resources of the organization; and (7) the investment policies of the organization.

The University endowment spending policy guidelines target an annual distribution in the range of 4.0% to 5.0% of the endowment pooled portfolio average market value over the 12 trailing quarters through December 31 of the year prior to the new fiscal year. The actual rate is set annually by the Board of Trustees, and was 4.5% and 4.2% at June 30, 2013 and 2012, respectively.

In establishing this policy, the University considered the long-term expected return on its funds. Accordingly, over the long term, the University expects the current spending policy to allow its endowment to grow at a rate in excess of inflation. This is consistent with the University's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

(e) *Funds with Deficiencies*

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the original gift amount maintained as permanently restricted net assets. Deficiencies of this nature were approximately \$9,000 and \$563,000 as of June 30, 2013 and June 30, 2012, respectively. Such deficiencies are recorded in unrestricted net assets. These

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

(f) Net Asset Classification of Endowment Funds

Net asset composition by type of fund consists of the following as of June 30, 2013 (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (9)	523,056	279,434	802,481
Board-designated endowment funds	<u>299,617</u>	<u>8,415</u>	<u>—</u>	<u>308,032</u>
	<u>\$ 299,608</u>	<u>531,471</u>	<u>279,434</u>	<u>1,110,513</u>

Net asset composition by type of fund consists of the following as of June 30, 2012 (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (563)	473,394	270,809	743,640
Board-designated endowment funds	<u>278,473</u>	<u>7,548</u>	<u>—</u>	<u>286,021</u>
	<u>\$ 277,910</u>	<u>480,942</u>	<u>270,809</u>	<u>1,029,661</u>

Board-designated temporarily restricted funds represent the income on nonendowed purpose restricted gifts to the University that the Board of Trustees has designated as endowment, but which cannot reasonably be expended within a year.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Changes in endowment net assets for the year ended June 30, 2013 (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 277,910	480,942	270,809	1,029,661
Investment return:				
Investment income	2,869	8,026	718	11,613
Net (depreciation) appreciation – realized and unrealized	<u>33,076</u>	<u>74,556</u>	<u>(2,055)</u>	<u>105,577</u>
Total investment return	313,855	563,524	269,472	1,146,851
Contributions	—	7	8,776	8,783
Endowment spending payout	(12,099)	(34,458)	—	(46,557)
Other changes	<u>(2,148)</u>	<u>2,398</u>	<u>1,186</u>	<u>1,436</u>
	<u>\$ 299,608</u>	<u>531,471</u>	<u>279,434</u>	<u>1,110,513</u>

Changes in endowment net assets for the year ended June 30, 2012 (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 295,189	526,079	256,369	1,077,637
Investment return:				
Investment income	7,715	7,484	633	15,832
Net (depreciation) appreciation – realized and unrealized	<u>(15,068)</u>	<u>(19,685)</u>	<u>1,107</u>	<u>(33,646)</u>
Total investment return	287,836	513,878	258,109	1,059,823
Contributions	—	171	12,700	12,871
Endowment spending payout	(11,496)	(33,107)	—	(44,603)
Other changes	<u>1,570</u>	<u>—</u>	<u>—</u>	<u>1,570</u>
	<u>\$ 277,910</u>	<u>480,942</u>	<u>270,809</u>	<u>1,029,661</u>

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(8) Annuity and Life-Income Funds

The University held \$8,377,000 and \$7,731,000 in investments related to annuity and life-income funds as of June 30, 2013 and 2012, respectively. A related liability of \$4,986,000 and \$4,785,000 as of June 30, 2013 and 2012, respectively, represents the present value of future annuity payments due under these agreements, and was calculated for each annuity using discount rates and actuarial assumptions consistent with the terms of the gift.

The University's annuity and life income funds include charitable gift annuities, charitable remainder annuity trusts, and charitable remainder unitrusts.

The University is required by the laws of certain states to maintain reserves against charitable gift annuities. Such reserves amounted to \$151,000 as of June 30, 2013 and 2012.

(9) Property, Plant, and Equipment

Land is recorded at cost or appraised value at time of receipt if contributed, including land deeded by the Board of Trustees of Delaware College to the State in the early 1900s and thereafter used by the University, as successor, for the purposes of the University.

Buildings are recorded at cost of initial construction, including buildings on land deeded to the State and thereafter used for the purposes of the University. Costs of major renovations to buildings are capitalized. Costs of equipment in excess of \$5,000 with a useful life expectancy of two or more years are also capitalized.

The University uses the straight-line method of depreciation for its plant assets based on the following estimated useful lives:

	Estimated lives (years)
Land improvements	15
Buildings	40
Equipment and furnishings	2 – 20

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Property, plant, and equipment as of June 30, 2013 and 2012 consisted of the following (in thousands):

	2013	2012
Land and improvements	\$ 93,999	101,346
Buildings	1,415,789	1,223,193
Equipment and furnishings	450,747	423,016
Collections and works of art	8,756	8,872
Capital leasehold	15,235	15,235
Construction in progress	164,359	203,740
Total property, plant, and equipment	2,148,885	1,975,402
Less accumulated depreciation	(827,254)	(779,572)
Total property, plant, and equipment, net	\$ 1,321,631	1,195,830

The University has three major building and renovation projects as of June 30, 2013 budgeted to cost \$126,800,000. At year-end, \$109,456,000 has been disbursed with \$17,344,000 committed to complete these projects.

(10) Financing Obligations

The University has obligations under capital leases that amounted to \$5,985,000 and \$6,557,000 as of June 30, 2013 and 2012, respectively. The University's obligation at June 30, 2013 includes a building lease with Delaware Technology Park for the Delaware Biotechnology Institute, a unit of the University. The lease consists of annual lease payments ranging from \$345,000 to \$900,000 to be paid over a 20-year term.

The aggregate amount of principal and interest payments on the University's obligation under capital leases is due as follows (in thousands):

	Principal	Interest	Total
2014	\$ 607	287	894
2015	642	254	896
2016	682	214	896
2017	717	177	894
2018	761	154	915
Thereafter	2,576	138	2,714
	\$ 5,985	1,224	7,209

In August 2012, 1743 Holdings, LLC entered into a ground lease with a third-party for approximately six acres of land, and the structures thereon, for the purpose of renovating and expanding the existing structures and then leasing the space in the renovated unit to the University for use primarily by the College of Health Sciences. The ground lease has an initial term of 75 years, with a nominal rent while the

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

University is occupying the unit. Rent reverts to a market-based rent at the time the University ceases to lease the unit. The space lease was entered into simultaneously with the ground lease and has an initial term of 29 ½ years, with the option of twelve additional 5-year extensions. Construction of the unit is underway, and the University anticipates the renovations to cost approximately \$30,500,000.

These transactions were structured to create the same economic effect as if the University built and owned the building, and as such, the University has reflected the costs associated with the renovation of the unit as construction in progress in the consolidated statement of financial position, and also recorded a corresponding financing obligation of \$12,000,000 at June 30, 2013.

Occupying the unit is expected to begin in January 2014, at that time rent payments are to begin. The estimated future minimum rental payments are as follows (in thousands):

2014	\$	999
2015		1,998
2016		1,998
2017		1,998
2018		1,998
Thereafter		49,959
		49,959
	\$	58,950

(11) Notes and Bonds Payable

Indebtedness at June 30, 2013 and 2012 consisted of the following (in thousands):

		2013	2012
Series 2004B Revenue Bonds (a)	\$	33,375	39,720
Series 2005 Revenue Bonds (b)		34,615	43,750
Series 2009A Revenue Bonds (c)		—	68,600
Series 2009B Revenue Bonds (d)		49,305	55,085
Series 2010A Revenue Bonds(e)		119,580	119,580
Series 2010B Revenue Bonds (f)		11,080	11,080
Series 2013A Revenue Bonds (g)		119,210	—
Series 2013B Revenue Bonds (h)		29,755	—
Series 2013C Revenue Bonds (i)		57,475	—
Blue Hen Hotel LLC Bonds (j)		8,700	9,055
University Early Learning Center Line of Credit (k)		3,027	3,251
		466,122	350,121
Premiums on notes and bonds payable		22,927	3,872
Notes and bonds payable	\$	489,049	353,993

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(a) *Series 2004B Revenue Bonds*

In April 2004, the University issued \$40,835,000 of Series 2004B Variable Rate Demand Revenue Bonds. The Series 2004B Bonds were used to construct a parking garage, to demolish existing University dormitories, to construct three new dormitory buildings, and for other capital improvements.

The Series 2004B Bonds initially bear interest at a Daily Rate (0.07% at June 30, 2013) and will continue to bear interest at a Daily Rate until converted to bear interest at a Weekly, Flexible, Term, or Fixed Rate to maturity. The interest rate to be in effect for a particular period of time will be reset by the Remarketing Agent and will never exceed 12% per annum. A 3.25% interest cost through fiscal year 2035 is anticipated based on an existing interest rate exchange agreement, with additional costs of remarketing and a Standby Bond Purchase Agreement (SBPA) with a scheduled termination date of April 5, 2015. The Bonds are secured by a pledge of gross revenues received by the University from the operations of all project facilities including housing, dining, parking, and other revenue producing facilities. The Series 2004B Bonds mature on November 1, 2034, but are subject to optional redemption and tender for purchase prior to maturity. On May 1, 2013, \$5,195,000 from 2013A Bonds was used to refund a portion of the Series 2004B Bonds.

(b) *Series 2005 Revenue Bonds*

In July 2005, the University issued \$49,945,000 of Series 2005 Variable Rate Demand Revenue Bonds. \$37,880,000 of the Series 2005 Bonds were used to complete the construction of three new dormitory buildings, the demolition of some existing University dormitories, and other capital improvements started with proceeds of the Series 2004B Revenue Bonds. In addition, \$12,065,000 was used to advance refund a portion of the Series 1997 Bonds.

The Series 2005 Bonds initially bear interest at a Daily Rate (0.05% at June 30, 2013) and will continue to bear interest at a Daily Rate until converted to bear interest at a Weekly, Flexible, Term, or Fixed Rate to maturity. The interest rate to be in effect for a particular period of time will be reset by the Remarketing Agent and will never exceed 12% per annum. A 3.87% interest cost through fiscal year 2036 is anticipated on the \$37,880,000 of project funds and 3.75% interest cost through fiscal year 2022 on the \$12,065,000, both based on existing interest rate exchange agreements, with additional costs of remarketing and a SBPA with scheduled termination date of May 31, 2016 at which time it may be terminated, extended or replaced. The Bonds are secured by a pledge of gross revenues received by the University from the operations of all project facilities including housing, dining, parking, and other revenue producing facilities. The Series 2005 Bonds mature on November 1, 2035, but are subject to optional redemption and tender for purchase prior to maturity. On May 1, 2013, \$7,505,000 from 2013A Bonds was used to refund a portion of the Series 2005 Bonds.

(c) *Series 2009A Revenue Bonds*

In March 2009, the University issued \$71,310,000 of Series 2009A Variable Rate Revenue Bonds in term mode with a termination date of May 31, 2011. On June 1, 2011, replacement term mode bonds were issued for \$68,600,000 with a mandatory remarketing date of June 4, 2013, at which time, the

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

bonds could be converted to any mode consistent with and as permitted by the Supplemental Agreement to the Trust Agreement for the 2009A bonds. These bonds were issued for the purpose of refinancing a taxable bank demand note, which was entered into on July 10, 2008, the proceeds of which the University used to redeem its Auction Rate Revenue Bonds Series 2007.

The Series 2009A Bonds issued June 1, 2011 initially bear interest at a Term Rate of 0.85% and will continue to bear interest at a Term Rate until converted to bear interest at a Daily, Weekly, Flexible, or Fixed Rate to maturity. The interest rate to be in effect for a particular Interest Period when the Term Rate is in effect, will be set by the Remarketing Agent as the minimum per annum rate of interest that is necessary to market the Series 2009A Bonds at a price equal to 100% of their principal amount plus accrued interest. The initial interest period extended until June 4, 2013 with interest payments on each June 1 and December 1. On June 4, 2013, the University refunded all 2009A bonds outstanding.

(d) Series 2009B Revenue Bonds

In December 2009, the University issued \$64,000,000 of Series 2009B Revenue Bonds in fixed rate mode with the sole purpose of refunding the Series 1998, 2001A, and 2001B Variable Rate Demand Bonds and terminating related interest rate exchange agreements as discussed above.

The Series 2009B Bonds will bear interest rates ranging from 2% to 4%, maturing over various dates through November 2026, and are secured by a pledge of gross revenues received by the University from the operations of all project facilities including housing, dining, parking, and other revenue producing facilities.

(e) Series 2010A Revenue Bonds

In November 2010, the University issued \$119,580,000 of Series 2010A Revenue Bonds in fixed rate mode with the purposes of providing funds for certain project facilities. The American Recovery and Reinvestment Act of 2009 (ARRA) permitted the University to issue the 2010A Bonds as “Build America Bonds” to finance capital expenditures for the purposes for which it could have issued tax-exempt bonds and to elect to receive payments from U.S. Treasury equal to 35% of the corresponding interest payable on 2010A Bonds (the Subsidy Payments). For the year ended June 30, 2013, the University received Subsidy Payments of \$2,348,000, which are included in other operating revenue on the consolidated statement of activities. Interest income on these bonds is taxable to the bond holder. The Series 2010A Bonds are subject to mandatory redemption from November 1, 2028 through November 1, 2040, but are subject to optional redemption and tender for purchase prior to maturity.

The Series 2010A Bonds will bear the fixed interest rate of 5.866% (3.8129% after Subsidy Payments are received) and are secured by a pledge of gross revenues received by the University from the operations of all project facilities including housing and other revenue producing facilities.

(f) Series 2010B Revenue Bonds

In November 2010, the University issued \$12,080,000 of Series 2010B Revenue Bonds in fixed rate mode with the purpose of providing funds for certain project facilities.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The Series 2010B Bonds will bear interest rates ranging from 0.65% to 3.796%, maturing on November 1 from 2012 to 2019. Interest income on these bonds is taxable to the bond holder. The Bonds are subject to optional redemption and tender for purchase prior to maturity.

(g) Series 2013A Revenue Bonds

In March 2013 (settlement in April) the University issued \$119,210,000 of Series 2013A Revenue Bonds in fixed rate mode to fund certain capital projects, refund portions of the 2004B, 2005, and 2009A issues, and terminate the maturities of interest rate swap agreements related to the refunded bonds.

The Series 2013A Bonds will bear interest rates ranging from 3.00% to 5.00%, maturing on November 1, from 2014 to 2033. In addition there is a 5.00% term bond maturity in the amount of \$27,825,000 on November 1, 2043. The Bonds are subject to optional redemption and tender for purchase prior to maturity.

(h) Series 2013B Revenue Bonds

In March 2013 (settlement in April) the University issued \$29,755,000 of Series 2013B Federally Taxable Revenue Bonds in fixed rate mode to fund certain capital projects.

The Series 2013B Bonds will bear interest rates ranging from 0.488% to 2.997%, maturing from 2014 to 2026. In addition there is a 3.831% term bond in the amount of \$6,770,000 maturing on November 1, 2033 and a 3.981% Term Bond in the amount of \$13,555,000 maturing on November 1, 2043. The Bonds are subject to optional redemption and tender for purchase prior to maturity.

(i) Series 2013C Revenue Bonds

In March 2013 (settlement in April) the University issued \$57,475,000 of Series 2013C Variable Rate Revenue Bonds with a mandatory remarketing date of May 1, 2016, at which time the Bonds will be converted to any mode consistent with and as permitted by the Supplemental Agreement to the Trust Agreement for the 2013C Bonds. The bond proceeds together with a University Equity contribution of approximately \$4,295,500 was used to refund the remaining Series 2009A that were not refunded by the Series 2013A Bonds described above.

The Series 2013C Bonds will initially bear interest at a Term Rate of 0.70% and will continue to bear interest at a term rate until converted to bear interest at a Daily, Weekly, Flexible, or Fixed Rate to maturity. The interest rate to be in effect for a particular Interest Period when the Term Rate is in effect, will be set by the Remarketing Agent as the minimum per annum rate of interest that is necessary to market the Series 2013C Bonds at a price equal to 100% of their principal amount plus accrued interest. The initial period extends until May 1, 2016 with interest payments on each May 1 and November 1.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(j) *Blue Hen Hotel LLC Bonds*

In September 2001, the Blue Hen Hotel, LLC, a Company wholly owned (note 2) by the University and consolidated into the University's financial statements, issued \$11,500,000 of Blue Hen Hotel, LLC Variable Rate Demand Bonds, Series 2001 (Series 2001 Bonds), which were also guaranteed by the University. The Series 2001 Bonds funded the design, construction, and start-up operating costs of the hotel.

The Series 2001 Bonds will initially bear interest at a Weekly Rate (0.23% at June 30, 2013) and will continue to bear interest at a Weekly Rate until converted to bear interest at a Daily, Flexible, Term, or Fixed Rate to maturity. The interest rate to be in effect for a particular period of time will be reset by the Remarketing Agent and will never exceed 18% per annum. A 5.50% interest cost through September 1, 2027 is anticipated based on an existing interest rate exchange agreement, with additional costs of remarketing and a SBPA that was renewed on November 15, 2012 with a scheduled termination date of December 12, 2014. The swap agreement counterparty has the right to terminate the agreement under certain market conditions in which the daily weighted average of the one-month LIBOR equals or exceeds 9.00% for the previous six-month period. If such right is exercised, the bond interest would revert to the market rate for weekly traded variable rate demand bonds.

The Series 2001 Bonds mature on September 1, 2027, but are subject to optional redemption and tender for purchase prior to maturity.

(k) *Early Learning Center Line of Credit*

In December 2008, the University obtained a five-year extension to the \$5,000,000 line of credit that was originally opened in December 2003 to renovate the University Early Learning Center facility. The interest rate is a variable rate of 65% of the Bank's National Commercial Rate (calculated to be 2.60% at June 30, 2013) and there is an outstanding balance of \$3,027,000 at June 30, 2013.

The University has entered into SBPAs for the variable rate demand bonds of the Series 2004B and 2005 Bonds with Bank of America and TD Bank respectively to provide liquidity for the purchase of the bonds should the remarketing agent be unable to sell the bonds on the open market. The SBPAs provide for the banks to purchase any outstanding bonds not remarketed for a period of up to 90 days at variable interest rates as defined in the SBPAs. Remarketing efforts on the open market would continue during the 90-day period. Should efforts to remarket any or all of the bonds be unsuccessful throughout the 90-day period, the University would be required to use available cash resources to redeem the bonds from the SBPA provider.

The University's debt agreements require that the University meet certain financial, and other, covenants. The University was in compliance with these covenants at June 30, 2013 and 2012.

The carrying amount of variable rate long-term debt approximates fair value because these financial instruments bear interest at rates, which approximate current market rates for loans with similar maturities and credit quality. The fair value of fixed and variable rate Revenue Bonds (par amount of \$454,395,000) approximates \$482,983,000. Such amount has been estimated by discounting the future cash outflows associated with such debt by current market rates for loans with similar maturities and credit quality.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Certain long-term debt obligations expose the University to cash flow risk related to changes in interest rates. Management believes it is prudent and cost effective to hedge some of its exposure to interest rate risk. To achieve this objective, management has interest rate swap agreements for approximately \$142,340,000 (including \$8,700,000 related to the Blue Hen Hotel, LLC, note 2) of long-term debt obligations as of June 30, 2013. In accordance with FASB standards, not-for-profit organizations recognize the gain or loss on a hedging instrument as a change in net assets in the period of change. Accordingly, for the year ended June 30, 2013, the University has recognized an unrealized gain of \$15,038,000 (including a gain of \$863,000 related to the Blue Hen Hotel, LLC) in the consolidated statement of activities for the increase in fair value of its interest rate swaps and a corresponding decrease in the fair value of its interest rate swap liability in the consolidated statement of financial position.

The aggregate amount of principal payments on the University's notes and bonds payable are due as follows (in thousands):

2014	\$	6,014
2015		12,709
2016		11,094
2017		11,509
2018		11,754
Thereafter		413,042
	\$	<u>466,122</u>

(12) Derivative Instruments

The University employs derivatives in the form of interest rate swap agreements to manage market risk associated with outstanding debt (in thousands).

	<u>Statement of financial position location</u>	<u>Location of gain (loss)</u>	<u>Fair value 2013</u>	<u>Fair value 2012</u>	<u>Amount of gain (loss) 2013</u>	<u>Amount of gain (loss) 2012</u>
Interest rate swap agreements	Interest rate swap liabilities	Net realized and unrealized gains	\$ 24,478	41,487	15,038	(20,053)

Interest rate swaps with a fair value of \$1,971,000 were terminated on March 19, 2013. The termination along with the gain reported in the table above resulted in a net decrease in the liability of \$17,009,000 as of June 30, 2013.

A portion of the total interest rate swap liabilities reported on the consolidated statement of financial position, \$22,495,000 at June 30, 2013, contains provisions that require the University's debt and the counterparty to maintain an investment grade credit rating from one or both of the major credit rating agencies. A downgrade of the University or the counterparty's rating may require that party to provide collateralization above a predetermined threshold on all rate swaps in net liability positions. The University's current rating of AA+ by Standard & Poor's would have to drop five levels or more to a rating

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

of A – or below, at which time the University might be required to post collateral. To date, the University has not posted collateral for any rate swap agreements.

(13) Employee Benefit Plans

The University's 403(b) Retirement Annuity Program is available to substantially all faculty and professional employees. This plan is administered through Fidelity Investments (Fidelity) and Teachers Insurance and Annuity Association (TIAA) – College Retirement Equities Fund (CREF). The University's contribution for this program is fixed at 11 percent of annual base salary for eligible employees who contribute a minimum of four percent of their annual salary. The policy of the University is to pay its share of the annual premium accrued in connection with the University Retirement Annuity Program. As a result, there are no unfunded benefits. Pension plan expense for the University's 403(b) Retirement Annuity Program was \$27,542,000 in 2013 and \$26,330,000 in 2012.

Salaried and hourly staff employees participate in the Delaware State Employees' Pension Plan (the State Plan), a cost sharing defined benefit plan. The State Plan (established in 1970), is one of nine plans encompassed within the Delaware Public Employees' Retirement System (<http://www.delawarepensions.com/financials.shtml>). Under the state pension statute, a mandatory pre-tax contribution of three percent of salary in excess of \$6,000 per year plus five percent of salary in excess of the social security wage base is required. The policy of the University is to pay its share of the annual premium accrued in connection with the State Plan. As a result, there are no unfunded benefits. Pension plan expense for the State Plan was \$11,419,000 and \$10,520,000 in 2013 and 2012, respectively.

The State Plan financial statements and actuarial reports for June 30, 2012 (most recent available) do not include separate reportable information for each participant organization in the plan. However, the following information was derived from the data available:

- The University has 1,346 active participants in the State Plan. The State Plan, in total, has 61,820 participants, 35,427 of which are active participants.
- The University's contribution to the State Plan in fiscal year June 30, 2012 of \$10,520,000 was approximately 7.14% of the \$147,454,000 total annual required plan employer contributions to the plan.
- At June 30, 2012, the State Plan had a 91.5% funded ratio of the actuarial accrued liability, and the accrued benefit funding ratio was 100.2% at this same point in time.
- The funding objective of the State Plan is to establish contribution rates that, over time, will remain level as a percent of payroll. The contribution rate was developed to provide for current cost (i.e., normal cost expressed as a level percent of payroll) plus level percent of payroll amortizations of each layer of the unfunded liability over a specified period. The participant organizations to the State Plan have consistently funded the full amounts required based on the actuarial valuations and specific statutory provisions.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

In addition, the University also offers two additional voluntary retirement benefit plans:

The Voluntary 403(b) Retirement Plan, administered through Fidelity and TIAA-CREF, is available to all eligible full and part-time employees who wish to make additional contributions to their retirement savings. Participation is voluntary and does not require a minimum contribution. The University makes no contributions to this plan, incurs no expense for the operation of this plan and has no unfunded liability.

The Voluntary 457(b) Deferred Compensation Plan, administered through Fidelity TIAA-CREF, is available to all eligible full and part-time employees who are already making the maximum allowable contribution to the Voluntary 403(b) Retirement Plan and wish to make additional contributions to their retirement savings. The University makes no contributions to this plan, incurs no expense for the operation of this plan and has no unfunded liability.

In addition to retirement benefits, the University also provides postretirement benefits primarily for medical insurance to retired employees who are not eligible under the State Plan. The University recognizes the funded status (i.e., the difference between the fair value of plan assets and the accumulated postretirement benefit obligation) of its postretirement benefit plan in the consolidated statement of financial position. Also, the University measures the fair value of plan assets and benefit obligations as of the date of the fiscal year-end consolidated statement of financial position. As of June 30, 2013, the University has not funded these benefits.

Net periodic postretirement benefit cost for 2013 and 2012 includes the following components (in thousands):

	2013	2012
Service cost	\$ 9,588	7,513
Interest cost	13,050	12,573
Amortization of unrecognized loss	2,157	—
Net periodic postretirement benefit cost	\$ 24,795	20,086

The accumulated postretirement benefit obligation recognized in the consolidated statement of financial position at June 30, 2013 and 2012 is as follows (in thousands):

	2013	2012
Accrued postretirement liability	\$ 230,195	210,759
Unrecognized net loss	34,543	72,931
Accumulated postretirement benefit obligation	\$ 264,738	283,690

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

Changes in the accumulated postretirement plan benefit obligation and funding status for 2013 and 2012 are as follows (in thousands):

	<u>2013</u>	<u>2012</u>
Benefit obligation at beginning of year	\$ 283,690	209,491
Service cost	9,588	7,513
Interest cost	13,050	12,573
Amortization of unrecognized loss	2,157	—
Actuarial (gain) or loss	(38,387)	59,466
Disbursements	<u>(5,360)</u>	<u>(5,353)</u>
Benefit obligation at end of year	264,738	283,690
Fair value of plan assets at beginning of year	—	—
Employer contributions	5,360	5,353
Benefits paid	(5,360)	(5,353)
Fair value of plan assets at end of year	<u>—</u>	<u>—</u>
Funded status at end of year	\$ <u>264,738</u>	<u>283,690</u>

The University expects to contribute \$7,317,000 to the plan for the year ended June 30, 2014.

The accumulated postretirement benefit obligation was determined using a discount rate of 5.40% and 4.90% in 2013 and 2012, respectively. The health care cost trend rates used reflect the differences between pre-65 and post-65 claims were 7.60% and 5.00%, respectively, in 2013, and 8.00% and 6.50%, respectively, in 2012. This rate gradually decreases to 5.00% by the year 2019 for pre-65 claims and remains constant at 5.00% for post-65 claims.

The impact of a one-percentage-point change in the assumed healthcare cost trend rate, while holding all other assumptions constant, would be as follows (in thousands):

	<u>Increase</u>	<u>Decrease</u>
Effect on service cost and interest cost components of net periodic postretirement benefit cost	\$ 5,577	(4,237)
Effect on benefit obligation as of June 30, 2013	50,814	(40,264)

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

At June 30, 2013, the University's expected future benefit payments for future service are as follows (in thousands):

Year ended June 30:			
2014	\$	7,317	
2015		8,054	
2016		8,760	
2017		9,603	
2018		10,397	
2019 through 2023		65,628	

The effect of federal subsidies enacted by the Medicare Prescription Drug Improvement and Modernization Act of 2003 has been reflected in the measurement of the accumulated postretirement benefit obligation or net periodic postretirement benefit cost.

(14) Asset Retirement Obligations

The University has asset retirement obligations arising from regulatory requirements to perform certain asset retirement activities. When an asset retirement obligation is identified, the University records the fair value of the obligation as a liability. The liability is accreted to its present value and accretion expense is recognized. The corresponding asset retirement costs are capitalized as part of the carrying amount of the related long-lived asset and depreciated over the period of expected remediation.

The University had asset retirement obligations of \$22,111,000 and \$20,889,000 as of June 30, 2013 and 2012, respectively. The following table reconciles the obligation as of June 30, 2013 and 2012 (in thousands):

		2013	2012
Balance at beginning of year	\$	20,889	20,185
Additional obligations incurred		1,154	1,365
Obligations settled in current period		(694)	(1,316)
Changes in estimates, including timing		221	131
Accretion expense		542	524
Balance at end of year	\$	22,112	20,889

(15) Operating Leases

The University has entered into a series of leasing transactions related to the redevelopment of the University's 272 acre STAR campus. The property which comprises the STAR campus was acquired in November 2009 for the purpose of expanding the University's overall campus and to provide a site for, among other things, high technology, medical, and educational partnerships between the University, federal and state government, and leaders in various technology, medical and educational fields.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

In March 2012, 1743 Holdings, LLC entered into a ground lease with a third-party for approximately 50 acres of unimproved land on the southern portion of the STAR campus. The lease has an initial term of 25 years and may be extended for up to 4 consecutive additional terms of 5 years each. Base rent for the initial term of the lease is nominal, and was paid upon execution of the lease. In a related transaction, the University entered into a grant agreement with the Delaware Economic Development Authority to offset certain costs affiliated with infrastructure and other related costs on the STAR campus. As of June 30, 2013, \$2,981,000 has been drawn against the grant.

In August 2012, 1743 Holdings, LLC entered into an additional ground lease with a third-party for an additional nine acres of land, and the structures thereon, adjacent to the unit to be occupied by the College of Health Sciences. The lease was entered into for the purpose of renovating and expanding the existing structures and leasing the units to entities external to the University, and to the extent possible, entities that are related to health sciences. This ground lease has an initial term of 75 years. Rent is based upon formulas contained within the lease, considers factors such as gross rentable square footage of improvements, and approximate market rent. As it is early in the construction phase of these units, it is not currently possible to reasonably estimate the future minimum rental income from this lease.

In December 2012, 1743 Holdings, LLC entered into a ground lease with a third-party for approximately 43 acres of unimproved land on the north-west portion of the STAR campus. The lease has an initial term of 75 years and may be extended for up to 4 consecutive additional terms of 5 years each. Rent is based upon formulas contained within the lease, considers factors such as gross building square footage of constructed improvements, and approximate market rent.

The land and structures subject to the ground leases noted above are included in the consolidated statement of financial position at \$12,887,000 and \$1,824,000, respectively.

The future minimum rental payments to be received under the ground leases noted above and can reasonably be estimated are as follows (in thousands):

Year ended June 30:		
2014	\$	—
2015		—
2016		600
2017		600
2018		600
Thereafter		233,222

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

(16) Net Assets

Temporarily restricted net assets include the following at June 30, 2013 and 2012 (in thousands):

	<u>2013</u>	<u>2012</u>
Contributions receivable	\$ 34,771	32,273
Annuity and life income funds	617	832
Accumulated gains on permanent endowment funds	531,471	480,942
Other time and purpose restrictions	20,447	19,624
	<u>\$ 587,306</u>	<u>533,671</u>

Generally, the donors of these assets permit the University to use all or part of the income earned and net appreciation on related investments for general or specific purposes, such as scholarships, faculty salaries, or other operational support.

Permanently restricted net assets include the following at June 30, 2013 and 2012 (in thousands):

	<u>2013</u>	<u>2012</u>
Permanent loan funds	\$ 323	311
Annuity and life income funds	2,774	2,115
Funds held in trust by others	60,653	58,209
Permanent endowment funds	279,434	270,809
	<u>\$ 343,184</u>	<u>331,444</u>

(17) Scholarship Allowance

The University provides financial assistance to eligible students to partially offset the direct costs of tuition, on-campus housing, and meal contracts. These scholarship allowances are presented as a reduction of tuition and fees and sales and services of auxiliary enterprises.

Scholarships are funded from unrestricted resources, as well as funds from donors, federal and state governments, and endowment income restricted to use for student financial assistance.

UNIVERSITY OF DELAWARE

Notes to Consolidated Financial Statements

June 30, 2013

(with comparative information for the prior year)

The table below identifies this financial assistance by source and by student classification for the year ended June 30, 2013 (in thousands):

	<u>Undergraduate</u>	<u>Graduate</u>	<u>Total</u>
Unrestricted	\$ 45,355	54,950	100,305
Federal grants	665	1,017	1,682
State grants	10,517	46	10,563
Private gifts	2,751	486	3,237
Endowment	3,605	46	3,651
Total	<u>\$ 62,893</u>	<u>56,545</u>	<u>119,438</u>

An additional \$6,521,000 of University-provided financial assistance was utilized by students for books, supplies, and off-campus living expenses.

(18) Fundraising Costs

Fundraising costs were approximately \$11,531,000 and \$10,844,000 for the years ended June 30, 2013 and 2012, respectively.

(19) Related Party Transactions

The University may, from time to time, do business with companies that may be associated, either directly or indirectly, with members of the University's Board of Trustees or senior management. Although not material, the University believes that these transactions are executed on terms comparable to those available from unrelated parties and are in the best interest of the University.

(20) Contingencies

The University is party to certain claims and litigation arising in the ordinary course of business. In the opinion of management, the resolution of such claims and litigation will not materially affect the University's financial position, statement of activities, or cash flows.

(21) Subsequent Events

In connection with the preparation of the consolidated financial statements, the University evaluated subsequent events after the statement of financial position date of June 30, 2013 through October 28, 2013, which was the date the consolidated financial statements were issued.