# 2015 BONDHOLDERS REPORT

UNIVERSITY *of* WASHINGTON | TREASURY OFFICE

# 2015 BONDHOLDERS REPORT

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Cover photo courtesy of UW Housing and Food Services.

University of Washington

## 2015 BONDHOLDERS REPORT

This report includes financial and operating information on the University of Washington often requested by bondholders, lenders, underwriters and credit rating agencies.

As a preface to reviewing the materials, we suggest starting with the University's Financial Report, which highlights the accomplishments, opportunities and challenges facing the University of Washington as one of the nation's premier research universities. The enclosed audited financial statements are as of June 30, 2015 and for the year then ended – the University of Washington's fiscal year end. Certain enrollment and other data are for autumn 2015.

The University implemented Governmental Accounting Standards Board (GASB) Statement No. 68, "Accounting and Financial Reporting for Pensions" during fiscal year 2015. An extensive discussion of the impact of GASB Statement No. 68 can be found in the Management's Discussion and Analysis section of the University's 2015 Financial Report.

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# 2015 FINANCIAL REPORT

UNIVERSITY *of* WASHINGTON

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## UNIVERSITY FACTS

| | FISCAL YEAR 2015 Academic Year 2014–2015 | FISCAL YEAR 2010 Academic Year 2009–2010 | FISCAL YEAR 2005 Academic Year 2004–2005 |
|---|---|---|---|
| **STUDENTS** | | | |
| **Autumn Enrollment** [1] | | | |
| Undergraduate | 39,331 | 34,972 | 30,790 |
| Graduate | 13,333 | 11,996 | 10,309 |
| Professional | 2,006 | 1,913 | 1,797 |
| **TOTAL** | **54,670** | **48,881** | **42,896** |
| Extension course and conference registrations | 76,245 | 63,178 | 41,550 |
| **Number of Degrees Awarded** | | | |
| Bachelor's | 10,145 | 9,290 | 8,291 |
| Master's | 4,117 | 3,269 | 2,898 |
| Doctoral | 838 | 703 | 616 |
| Professional | 554 | 523 | 512 |
| **TOTAL** | **15,654** | **13,785** | **12,317** |
| FACULTY [1] (Professorial, Instructional, Research) | 4,561 | 4,169 | 3,623 |
| FACULTY AND STAFF [2] | 27,264 | 24,741 | 19,824 |
| RESEARCH FUNDING – ALL SOURCES *(in thousands of dollars)* | $ 1,302,012 | $ 1,421,643 | $ 1,009,437 |
| SELECTED REVENUES *(in thousands of dollars)* | | | |
| Patient Service and Other Medical-Related Revenues [3] | $2,283,022 | $ 1,473,779 | $ 783,624 |
| Gifts, Grants, and Contracts | 1,396,294 | 1,277,129 | 1,021,565 |
| Tuition and Fees [4] | 914,419 | 527,958 | 331,978 |
| Auxiliary Enterprises and Other Revenues | 614,185 | 315,363 | 228,118 |
| Investment Income | 227,404 | 308,752 | 219,069 |
| State Appropriations (Operating) | 255,156 | 347,425 | 323,417 |
| SELECTED EXPENSES *(in thousands of dollars)* | | | |
| Medical Related [3] | $2,068,941 | $ 1,043,171 | $ 624,074 |
| Instruction, Academic Support, and Student Services | 1,493,807 | 1,198,015 | 888,499 |
| Research and Public Service | 765,036 | 733,769 | 605,433 |
| Institutional Support and Physical Plant | 456,824 | 296,559 | 261,174 |
| Auxiliary Enterprises | 291,628 | 165,612 | 131,884 |
| CONSOLIDATED ENDOWMENT FUND [5] *(in thousands of dollars)* | $3,076,000 | $1,830,000 | $1,366,000 |
| SQUARE FOOTAGE [6] *(in thousands of square feet)* | 22,326 | 18,526 | 17,504 |

1 Headcount
2 Full time equivalents
3 Includes Valley Medical Center (2015 only) and Northwest Hospital (2015 and 2010 only)
4 Net of scholarship allowances of $142,685,000 in 2015, $82,461,000 in 2010, and $48,123,000 in 2005
5 Stated at fair value
6 Gross square footage, all campuses

KPMG LLP
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1918 Eighth Avenue
Seattle, WA 98101

# INDEPENDENT AUDITORS' REPORT

The Board of Regents
University of Washington:

We have audited the accompanying financial statements of the business-type activities of the University of Washington (the University), an agency of the state of Washington, which comprise the statements of net position as of June 30, 2015, and the related statements of revenues, expenses, changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, as well as its discretely presented component units as of and for the year ended June 30, 2015.

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

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

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

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

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

As discussed in note 1, the financial statements of the University of Washington, an agency of the state of Washington, are intended to present the financial position, and the changes in financial position and where applicable, cash flows of only the respective portion of the activities of the state of Washington that is attributable to the transactions of the University of Washington and its discretely presented component units.

They do not purport to, and do not, present fairly the financial position of the state of Washington as of June 30, 2015, the changes in its financial position or, where applicable, its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington as of June 30, 2015, and the changes in its financial position and its cash flows for the year then ended, and the financial position of its discretely presented component units as of June 30, 2015, and the changes in their financial position for the year then ended in accordance with U.S. generally accepted accounting principles.

***Other Matter***

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 10, and the schedules of required supplementary information on pages 46 through 47, be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries with management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Emphasis of Matter***

As discussed in note 1 to the financial statements, on July 1, 2014, the University adopted new accounting guidance requiring governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, as well as recognizing most changes in the net pension liability within pension expense. Our opinion is not modified with respect to this matter.

KPMG LLP

Seattle, Washington
October 23, 2015

# MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis below provides an overview of the financial position and activities of the University of Washington (University) for the year ended June 30, 2015. This discussion has been prepared by management and should be read in conjunction with the financial statements and accompanying notes that follow this section.

## Financial Highlights for Fiscal Year 2015

The University recorded an increase in net position of $235 million in fiscal year 2015; $243 million less than the fiscal year 2014 increase of $478 million. This is primarily related to a decrease in investment income of $254 million in fiscal year 2015, a result of decreased investment market values during the year. The University adjusts the carrying value of investments to market value each year, with the change recorded as investment income or loss. Revenues from tuition and patient services continued to show growth during 2015, while revenues from research activities were mostly unchanged.

**Key Financial Results for Fiscal Years 2015 and 2014**

| (in millions) | 2015 | 2014 |
|---|---|---|
| Total operating revenues | $ 4,217 | $ 3,914 |
| Total operating expenses | 4,668 | 4,384 |
| Operating loss | (451) | (470) |
| State appropriations | 255 | 262 |
| Investment income | 227 | 481 |
| Gifts | 200 | 191 |
| Other nonoperating revenues, net | 4 | 14 |
| Increase in net position | 235 | 478 |
| Net position, beginning of year | 6,643 | 6,165 |
| Cumulative effect of accounting change | (832) | – |
| Net position, beginning of year as restated | 5,811 | 6,165 |
| **Net position, end of year** | **$6,046** | **$ 6,643** |

Operating revenues minus operating expenses typically result in an operating loss in the University's financial statements. Nonoperating items, however, including state support, investment income, and gifts have typically enabled the University to reflect an increase in the net position, or "equity" each year. This surplus has been reinvested within the University to add a margin of educational excellence, upgrade the University's facilities and provide a prudent reserve for contingencies such as the recent period of economic instability.

The University implemented Governmental Accounting Standards Board (GASB) Statement No. 68, "Accounting and Financial Reporting for Pensions" during fiscal year 2015. This Statement changed how the University reports its participation in certain cost sharing, defined benefit pension plans administered by the state of Washington Department of Retirement Systems (DRS). It requires governments providing defined-benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, which is measured as the total pension liability less the amount of the pension plan's fiduciary net position. This Statement requires most changes in the net pension liability be included in pension expense in the period of the change, and others to be reported as deferred outflows of resources or deferred inflows of resources on the Statement of Net Position. Prior to adopting this Statement, the University reported pension expense based on cash contributions paid to the pension plan administrator. With the adoption of GASB Statement No. 68, net position was restated at July 1, 2014 by $832 million. Fiscal year 2015 financial results reflect application of the accounting changes required by Statement No. 68, but those changes have not been applied to fiscal year 2014 amounts due to the constraints of available information.

## Economic Factors Affecting the Future

A number of contingencies face the University over the next few years. The slow economic recovery is a primary source of uncertainty.

The state of Washington, which provided 6% of the University's total revenues in fiscal year 2015, continues to emerge from the recession. The effect of required increases to K-12 funding over the next several years, together with other economic factors such as slow growth and insufficient tax revenues, could result in added uncertainty for other state programs, including higher education.

The University's 2016 general operating appropriation from the state (excluding amounts appropriated for specific purposes) is approximately $292 million, an increase from 2015. This increase is largely attributed to targeted investments in medical and computer science education, as well as a significant backfill of lost tuition revenue from a reduction in the 2016 tuition rate for resident undergraduate students.

During the previous biennium, in exchange for biennial increases in state funding affecting both fiscal years 2014 and 2015, the University committed to freezing tuition rates for resident undergraduate students in both years. The University's Board of Regents continues to have broad tuition and fee setting authority for categories other than resident undergraduate tuition. State funding for capital appropriations continues to be under pressure, though some state bonding capacity was provided this biennium for critical renovation projects.

Since 2009, Federal ARRA funding for basic research and activities in the health sciences has totaled $366 million. The University has $17 million of unspent ARRA awards that will be expended in fiscal year 2016 or later. The federal budget remains under significant pressure; ongoing federal funding for research could be impacted.

In 2014, UW Medicine formed an Accountable Care Network (ACN) with certain other health care organizations and healthcare professionals in Western Washington. The ACN has entered into agreements to provide health care services to a

Unaudited – see accompanying notes to basic financial statements

large local employer with coverage that began January 2015, and with the Washington Health Care Authority to participate in its new Puget Sound Accountable Care Program (ACP) for Public Employees Benefits Board (PEBB) members. The Puget Sound ACP will initially be offered to PEBB members in five Western Washington counties beginning in January 2016, with possible statewide expansion in 2017. These arrangements include provisions for shared risk as well as shared savings between the ACN and the contracted entity based on achieving certain agreed upon quality and financial benchmarks.

Rising benefit costs, particularly for pensions and healthcare, continue to impact the University as well. Employer pension funding rates for the Public Employees' Retirement System (PERS) pension plans were unchanged during fiscal year 2015, but will be increasing 19% to 11% of covered salary during fiscal year 2016. Likewise, although the monthly employer base rate paid by the University for employee healthcare decreased during fiscal year 2015, it will be increasing 27% to $840 per active employee during fiscal year 2016. Both rates are likely to continue increasing over the next few years.

## Using the Financial Statements

The University's financial statements include the Statements of Net Position, the Statements of Revenues, Expenses and Changes in Net Position, the Statement of Cash Flows and the Notes to the Financial Statements. These financial statements are prepared in accordance with GASB principles, which establish standards for external financial reporting for public colleges and universities. GASB standards require that financial statements be presented on a consolidated basis in order to focus on the University as a whole.

On January 1, 2010, the University affiliated with Northwest Hospital & Medical Center (Northwest Hospital). GASB standards require that this entity be presented as a discrete component unit; therefore, its financial position at June 30, 2015, and the results of its operations for the year ended June 30, 2015, are included with Valley Medical Center in a separate column for financial statement presentation purposes (see Note 1 and Note 18 to the Financial Statements).

On July 1, 2011, the University affiliated with Valley Medical Center, a Washington public hospital district which owns and operates a 321-bed full-service acute care hospital and 45 clinics located throughout southeast King County. Valley Medical Center is also being reflected as a discrete component unit; therefore its financial position and the results of its operations are included with Northwest Hospital in a separate column for financial statement presentation purposes (see Note 1 and Note 18 to the Financial Statements).

The analysis presented below includes the consolidated balances of the University of Washington and its blended component units (see Note 1), but excludes the financial position and results of operations of its discrete component units (Northwest Hospital and Valley Medical Center), unless otherwise noted.

## Financial Health

### STATEMENTS OF NET POSITION

The Statements of Net Position present the financial condition of the University and report a snapshot of assets, liabilities, deferrals and net position. A summarized comparison of these balances as of June 30, 2015 and 2014, follows:

| (in millions) | 2015 | 2014 |
|---|---|---|
| Current assets | $ 1,402 | $ 1,537 |
| Noncurrent assets: | | |
| Capital assets, net | 4,172 | 4,045 |
| Investments, net of current portion | 4,297 | 3,959 |
| Other | 491 | 358 |
| Total assets | 10,362 | 9,899 |
| Deferred outflows | 111 | 14 |
| Total assets and deferred outflows | 10,473 | 9,913 |
| Current liabilities | 998 | 872 |
| Noncurrent liabilities: | | |
| Bonds payable | 1,911 | 1,966 |
| Other | 1,249 | 432 |
| Total liabilities | 4,158 | 3,270 |
| Deferred inflows | 269 | – |
| Total liabilities and deferred Inflows | 4,427 | 3,270 |
| **Net position** | **$ 6,046** | **$ 6,643** |

The excess of current assets over current liabilities of $404 million in 2015 and $665 million in 2014 reflects the continuing ability of the University to meet its short-term obligations. Current assets consist primarily of cash, short-term investments and accounts receivable. Current assets decreased $135 million in 2015, due to a decrease in the value of short-term investments, and the receipt of funds from Sound Transit for the mitigation of costs resulting from the construction of the light rail tunnel beneath campus. The Sound Transit amount was reflected as a receivable at the end of fiscal year 2014.

Long-term investments, a component of noncurrent assets, increased $338 million during 2015, as a result of market value changes during the year for the University's investments. Realized and unrealized gains in fiscal year 2015 totaled $151 million, versus $398 million in 2014.

Deferred outflows of resources and deferred inflows of resources both increased in 2015, primarily due to the implementation of GASB Statement No. 68. The University recorded $86 million of pension-related deferred outflows at the end of fiscal year 2015, primarily representing the deferral of pension contributions paid during the year for the University's participation in cost-sharing, defined benefit pension plans administered by the DRS. In addition, $269 million of pension-related deferred inflows were recorded for the University's proportionate share of collective deferred inflows reported by the DRS. These deferred inflow amounts represent the difference between projected and actual investment earnings on pension plan assets during the measurement period.

Other noncurrent liabilities also increased during 2015 due to the implementation of GASB Statement No. 68. As of June 30, 2015, a net pension liability of $623 million has been recorded and represents the University's proportionate share of the collective net pension liability reported by the DRS.

The difference between total assets and deferred outflows, and total liabilities and deferred inflows, is referred to as net position or "equity," and is one indicator of the current financial condition of the University. The change in net position measures whether the overall financial condition has improved or deteriorated during the year.

The University reports its "equity" in four categories:

- Net Investment in Capital Assets – This is the University's total investment in capital assets, net of accumulated depreciation and amortization and outstanding debt obligations related to those capital assets;
- Restricted Net Position:
  - Nonexpendable net position, primarily endowments, consists of funds on which the donor or other external party has imposed the restriction that the corpus is not available for expenditures but rather for investment purposes only;
  - Expendable net position consists of resources which the University is legally or contractually obligated to spend in accordance with time or purpose restrictions placed by donors and/or other external parties;
- Unrestricted Net Position – This is all other funds available to the University for any purpose associated with its mission. Unrestricted net position is often internally designated for specific purposes.

The University's net position at June 30, 2015 and 2014 is summarized as follows:

| (in millions) | 2015 | 2014 |
|---|---|---|
| Net investment in capital assets | $ 2,156 | $ 2,018 |
| Restricted: | | |
| Nonexpendable | 1,322 | 1,257 |
| Expendable | 1,699 | 1,629 |
| Unrestricted | 869 | 1,739 |
| **Total net position** | **$ 6,046** | **$ 6,643** |

Net investment in capital assets increased $138 million, or 7%, in 2015. This balance increases as debt is paid off, or when the University funds fixed asset purchases without the use of external financing, for example by using internal reserves. This balance decreases as assets are depreciated.

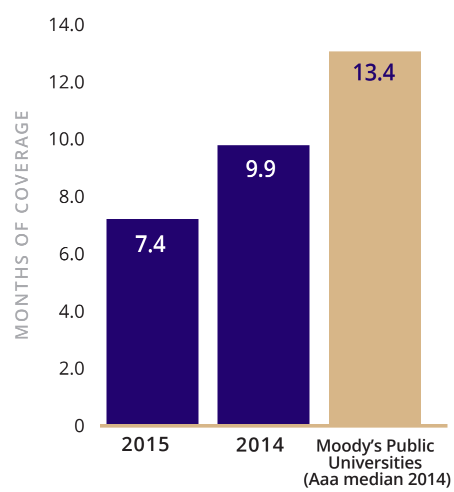
Restricted nonexpendable net position increased $65 million, or 5%, in 2015. This increase primarily reflects the receipt of new endowment gifts during the year.

Restricted expendable net position increased $70 million, or 4%, in 2015. This category is primarily affected by new operating and capital gifts, and earnings or losses on restricted investments, including endowments. The increase in market value for the Consolidated Endowment Fund was the main reason for the increase.

Unrestricted net position decreased by $870 million, or 50%, in 2015, primarily due to the impact of restating fiscal year 2015 beginning net position as a result of implementing GASB Statement No. 68. The change in accounting treatment required by Statement No. 68 reduced unrestricted net position by $913 million, representing the University's proportionate share of the beginning net pension liability, less $81 million of pension plan contributions paid by the University in the prior fiscal year. In addition, during fiscal year 2015 the University began a formal program to fund the construction of capital assets using internal reserves, by directing that a limited portion of the Invested Funds Pool be available for investment in institutional infrastructure, as opposed to financial assets. As a result, $51 million of construction costs associated with Phase 2 of the UW Medical Center Montlake Tower, and $77 million of costs associated with the construction of new student housing, were sourced during 2015 using internal reserves. These amounts have been reflected as a reduction of unrestricted net position, and an increase in net investment in capital assets.

The ratio of expendable financial resources to operations (as defined by Moody's Investors Service) measures the strength of net position as the coverage of annual operating expenses by financial resources that are ultimately expendable. This ratio, illustrated in the chart below, shows that in 2015 the University had enough expendable resources from various sources to fund operations for a period of 7.4 months. The decrease in this ratio during 2015 is primarily due to the implementation of GASB Statement No. 68, and the resulting decrease in Unrestricted Net Position.

**Expendable Financial Resources to Operations**[1]




1 The sum of Unrestricted Net Position and Restricted Expendable Net Position, divided by Total Operating Expenses (Operating Expenses plus interest expense). The result is multiplied by 12 to arrive at months of coverage. Net Position amounts include Northwest Hospital and Valley Medical Center.

Unaudited – see accompanying notes to basic financial statements

### Endowment and Other Investments

Investment returns provide an important source of revenue for the University's programs. Among the funds invested by the University are endowments, operating reserves, life income trusts, annuities and gifts.

Endowed gifts supply permanent capital and an ongoing stream of current earnings to the University. Most endowments are commingled in the Consolidated Endowment Fund (CEF), a diversified investment fund. As in a mutual fund, each individual endowment maintains a separate identity and owns units in the fund.

The CEF has experienced considerable growth over the past 10 years due to new gifts and endowment returns. The number of individual endowments in the CEF has grown to 4,363 and the market value of the CEF has more than doubled, rising from $1.4 billion at June 30, 2005 to $3.1 billion at June 30, 2015.

The impact to program support has been substantial, with $827 million distributed over the past 10 years touching every part of the University. Programs supported by endowment returns include academic programs, scholarships, fellowships, professorships, chairs and research activities. Under the Board of Regents' approved long-term spending policy for the CEF, quarterly distributions to programs are made based on an annual percentage rate of 4%, applied to the five-year rolling average of the CEF's market valuation. An additional 1% is distributed to support fundraising and stewardship activities (0.80%) and investment management (0.20%). Similar to program distributions, the fee is based on the endowment's five-year average market value.

Endowment portfolios are commonly managed around a core set of objectives focused on the need to provide support for endowed programs in perpetuity. The Board of Regents, in conjunction with the University of Washington Investment Committee (UWINCO), establishes the policy asset allocation judged to be most appropriate for the University from a long-term potential return and risk perspective. The policy asset allocation is reviewed annually for its continuing fit with the University's risk profile and with consideration of the changing dynamics of the capital markets.

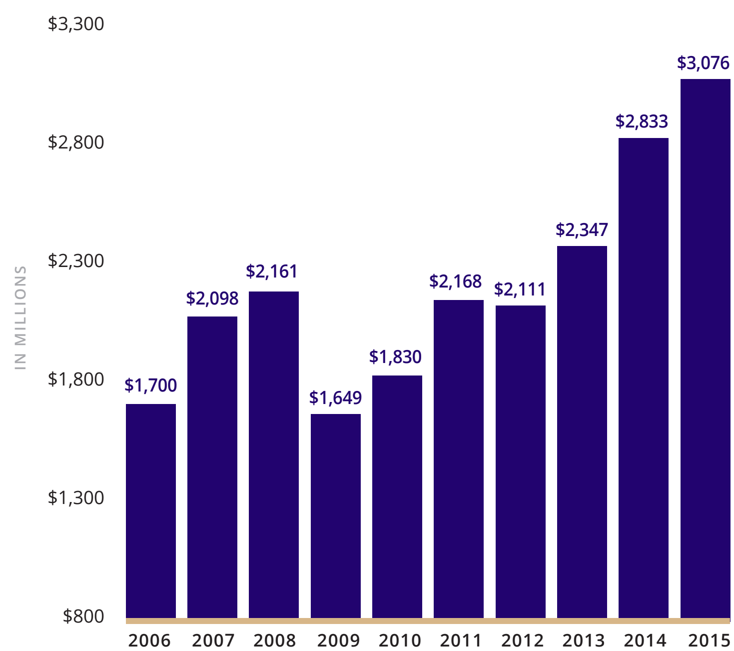
The CEF asset allocation includes two clearly defined categories of investments: those which facilitate growth or appreciation (Capital Appreciation), and those which preserve endowment values (Capital Preservation). At June 30, 2015, 73% of the CEF was invested in Capital Appreciation and 27% in Capital Preservation. Following our expectation that market returns for equities will exceed bonds over the next decade, a medium-to-long-term objective of generally overweighting equity-oriented strategies with a focus on quality companies and downside protection is being maintained. The University also maintains ample liquidity within Capital Preservation to meet its funding requirements, as well as to take advantage of market dislocations if opportunities arise.

For the fiscal year ended June 30, 2015, the CEF earned an investment return of +6.8%, significantly outperforming the blended benchmark (70% MSCI ACWI and 30% BC Gov't Bond). All individual CEF strategies had strong relative performance against their benchmarks with the exception of Fixed Income, which underperformed. It was a mixed year for global equities with the US leading market returns, while international developed and emerging markets were both negative for the year as Europe and China struggled with economic and political headwinds. Despite this, the CEF's Emerging Market strategy performed well, posting gains of +11.0% for the year.

With a five-year average of +10.0% and a ten-year average of +7.5%, the CEF has consistently maintained solid absolute and relative performance, outperforming the blended benchmark across all time periods.

A portion of the University's operating funds are invested in the CEF. As of June 30, 2015, these funds comprise $806 million of the CEF market value.

Consolidated Endowment Fund Market Value
*(in millions)*




### Debt and Related Capital Improvements

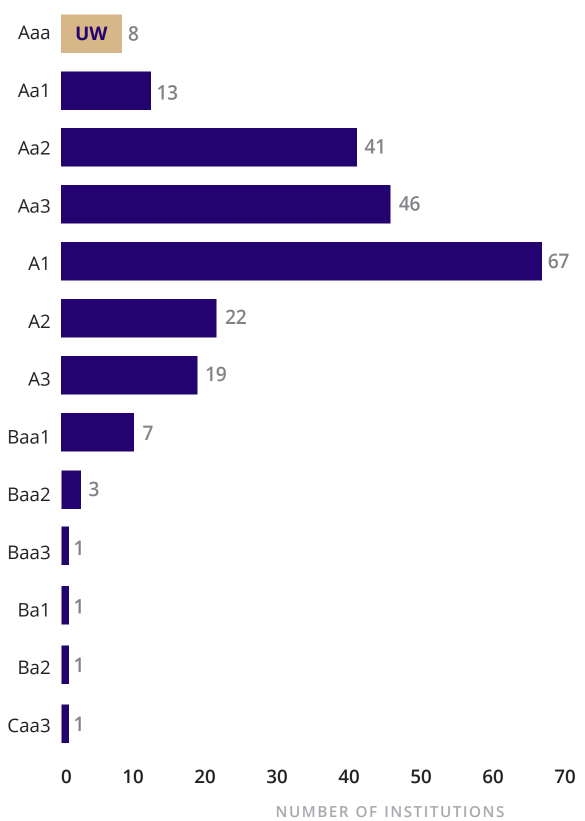
The University's general revenue borrowing platform, established in 2003, has been used to fund buildings that support the educational, research and service missions of the institution. The University's debt portfolio consists primarily of fixed rate debt, including General Revenue Bonds, Lease Revenue Bonds and state issued bonds, as well as variable rate debt such as commercial paper.

Credit ratings are a reflection of the University's strength. During fiscal year 2015, the University was rated Aaa (the highest rating) by Moody's Investors Service and AA+ (with a positive outlook) by Standard & Poor's. These strong ratings carry substantial advantages for the University: continued and wider access to capital markets when the University issues debt, lower interest rates on bonds and the ability to negotiate favorable bond terms.

The University takes its role of financial stewardship seriously and works hard to manage its financial resources effectively. Continued high debt ratings are important indicators of the University's success in this area.

**Moody's Fiscal Year 2014 Public College and University Rating Distribution**

(As of the July 2015 Moody's Median Report)




In March 2015, the University issued $218 million of General Revenue Bonds at an interest rate of 4.4%. Proceeds from this issuance refunded existing bonds and commercial paper.

In September 2015, the University issued $196 million of General Revenue Bonds at an interest rate of 4.03%. A portion of the debt will be used to pay off $112 million of commercial paper. The balance will be used to fund various projects such as the renovation of Denny Hall, construction of the new Animal Care and Research Facility, the SW Campus Central Utilities Plant, and other projects.

During fiscal year 2015, capital expenditures included $81 million for the construction of new student housing, and $62 million for Phase 2 of the UW Medical Center Montlake Tower.

Key projects substantially completed in 2015 include:

Demolition of the existing 1101 Café building and Terry Hall, and the construction of two new residential buildings named Maple Hall and Terry Hall. These new eight-story residential buildings include five wood-frame stories of housing, above a concrete plinth, consisting of two-bedroom suites, all with private bathrooms. The lower two floors of each building will be occupied by Housing and Food Services administration offices, common space for students, and some additional two-bedroom suites. A below-grade parking garage connected to the Lander Hall garage and the Lander Hall loading dock will extend below the new Maple and Terry residence halls. The two new buildings will total approximately 440,000 square feet, with a target bed count of 1,150 beds.

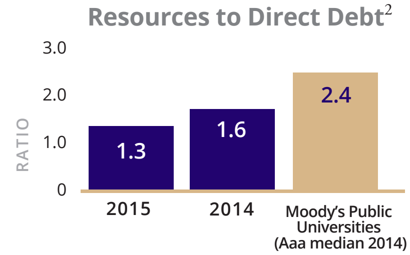
UW Medical Center Expansion Phase 2, which will provide a build-out of three inpatient bed floors, an OR suite within the new Montlake Tower (Phase I), and renovation of approximately 125,000 square feet within the existing Cascade and Pacific Towers.

HR/Payroll Modernization, which is a major initiative to replace the University's 33-year-old legacy payroll system with a modern, integrated human resources and payroll system. HR/Payroll Modernization will also provide a set of standardized processes to significantly improve support for critical HR and payroll work across the University, including the Medical Centers.

Construction of a new 3-story building adjacent to the existing North Creek Events Center on the UW Bothell and Cascadia Community College (CCC) campus. The 36,000 gross square feet facility will be used jointly by UW Bothell and CCC students, faculty, and staff. The Student Activities Center will provide for student leadership and clubs, fitness and recreation, casual study, and a multi-purpose room/events center. The project will also support the recently completed sports and recreation complex (adjacent to the project site) with restroom and equipment checkout facilities.

One measure of the University's ability to repay debt is the ratio of expendable financial resources to debt. The 2015 ratio of expendable financial resources to debt (as defined by Moody's) shows that the University has sufficient expendable resources to pay its long-term debt obligations 1.3 times over. The decrease in this ratio during 2015 is primarily due to the implementation of GASB Statement No. 68, and the resulting decrease in Unrestricted Net Position.

**Expendable Financial Resources to Direct Debt**[2]




2 The sum of Unrestricted Net Position and Restricted Expendable Net Position, divided by total capital lease obligations, bonds and notes payable outstanding. Includes Northwest Hospital and Valley Medical Center.

## STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

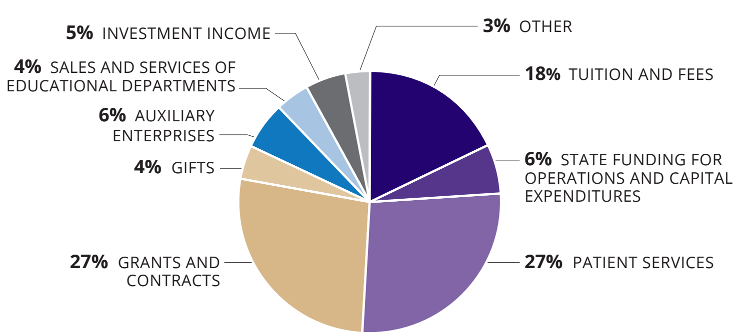
The Statements of Revenues, Expenses and Changes in Net Position present the University's results of operations and nonoperating items that result in the changes in net position for the year. In accordance with GASB reporting principles, revenues and expenses are classified as either operating or nonoperating. A condensed comparison of the University's revenues, expenses and changes in net position for the years ended June 30, 2015 and 2014 follows:

| (in millions) | 2015 | 2014 |
|---|---|---|
| Total operating revenues | $ 4,217 | $ 3,914 |
| Total operating expenses | 4,668 | 4,384 |
| Operating loss | (451) | (470) |
| Nonoperating revenues, net of expenses | 576 | 859 |
| Other revenues | 110 | 89 |
| Increase in net position | 235 | 478 |
| Net position, beginning of year | 6,643 | 6,165 |
| Cumulative effect of accounting change | (832) | – |
| Net position, beginning of year as restated | 5,811 | 6,165 |
| **Net position, end of year** | **$ 6,046** | **$ 6,643** |

Nonoperating revenues decreased $283 million, or 33%, in 2015, primarily due to a decrease in investment income during the year resulting from decreased investment market values.

The University has a diversified revenue base. No single source generated more than 27% of the total fiscal year 2015 revenues of $5.0 billion.

Sources of Funds




The following table summarizes revenues from all sources for the years ended June 30, 2015 and 2014:

| (in millions) | 2015 | 2014 |
|---|---|---|
| Tuition and fees | $ 914 | $ 839 |
| Patient services | 1,362 | 1,207 |
| Grants and contracts | 1,334 | 1,327 |
| Sales and services of educational departments | 223 | 213 |
| Auxiliary enterprises | 319 | 261 |
| State funding for operations | 255 | 262 |
| Gifts | 200 | 191 |
| Investment income | 227 | 481 |
| State funding for capital projects | 21 | 8 |
| Other | 128 | 164 |
| **Total revenue - all sources** | **$ 4,983** | **$ 4,953** |

### Grant Revenue

One of the largest sources of revenue (27%) continues to be grants and contracts. Total grant revenue of $1,334 million in fiscal year 2015 is mostly unchanged from the prior year, as a slight decrease in receipts from federal sources was offset by increases in nongovernmental grant and contract revenue. Receipts from federal sponsors made up 75% of total grant and contract revenue in 2015, compared with 77% in 2014, due primarily to a decline in revenues from the National Institutes of Health. Revenues generated by federal ARRA research funding decreased to less than $1 million in fiscal year 2015, compared to $10 million in the prior year, and contributed to the decrease from federal sources.

Grants and contracts provide the opportunity for graduate and undergraduate students to work with nationally recognized faculty in research as part of their educational experience.

Grant and contract revenue is earned when direct expenditures (such as researchers' compensation or purchases of goods and services) are made; therefore, there is little effect on the University's operating margin as a result of this direct expense reimbursement process.

Facility and administrative (F&A) expenses necessary to support grants and contracts are reimbursed by sponsors, along with direct costs, by an indirect cost recovery. The current F&A, or indirect cost recovery rate, for research grants is approximately 29 cents on every direct expenditure dollar.

### Primary Nongrant Funding Sources

The University relies primarily on student tuition and fees and state appropriations as revenue sources to support its nongrant funded educational operating expenses. State support for education increased during fiscal years 2014 and 2015, but is still significantly below historical levels.

Operating Support for Instruction

| (in millions) | 2015 | | 2014 | |
|---|---|---|---|---|
| State operating appropriations | $ 255 | 22% | $ 262 | 24% |
| Operating tuition and fees | 638 | 55% | 594 | 54% |
| Fees for self-sustaining educational programs | 276 | 23% | 245 | 22% |
| **Total educational support** | **$ 1,169** | **100%** | **$ 1,101** | **100%** |

Unaudited – see accompanying notes to basic financial statements

Noncapital state appropriations are considered nonoperating revenue under GASB Statement No. 35, "Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities," and are reflected in the nonoperating section of the Statements of Revenues, Expenses and Changes in Net Position; however, they are used solely for operating purposes.

Tuition and fees, net of scholarship allowances, increased $75 million (9%) to $914 million in fiscal year 2015. The increase was primarily due to higher enrollment during the year for most enrollment categories, together with selective increases in some tuition rates, mainly for non-resident students.

Tuition increases were partially offset by an increase in scholarships and fellowships, and scholarship allowances of $11 million in 2015.

Self-sustaining educational programs (fee-supported programs) include the following amounts for each of the fiscal years 2015 and 2014: UW Educational Outreach (the continuing education branch of the University), $97 million and $96 million, respectively, summer quarter tuition $59 million and $42 million, respectively, and for Business School and School of Medicine programs $47 million and $45 million, respectively.

### Patient Services – UW Medicine

The financial statements of the University include the operations of the School of Medicine, three hospitals, associated physicians and clinics, Airlift Northwest, and the University's share of two joint ventures. These entities, together with Harborview Medical Center (not included in the University's financial statements—see Note 13) comprise UW Medicine, an umbrella organization serving to coordinate these activities and promote quality healthcare in the Pacific Northwest and beyond, and to conduct cutting-edge medical research with worldwide benefit.

Patient care activities included in the University's financial statements include:

**UW Medical Center** (UWMC) is a 450-bed hospital that provides comprehensive healthcare services to the Puget Sound community and patients from throughout the Pacific Northwest. UWMC also serves as the major clinical, teaching and research site for students and faculty in the Health Sciences at the University. Over 18,000 patients receive inpatient care at UWMC each year. Specialized inpatient care needs are met by the Cancer Center, the Regional Heart Center, the Neonatal Intensive Care Unit (NICU) and the Organ Transplantation program.

Strategic growth initiatives were implemented in FY14 with the expansion of primary care and urgent care, the opening of the Eastside Specialty Center and other clinics, as well as continued progress on Phase 2 of the UW Medical Center Montlake Tower.

**Valley Medical Center** (VMC) is a 321-bed acute care hospital and network of clinics, treats over 17,000 inpatients per year, and is the oldest and largest public district hospital in the state of Washington. VMC joined UW Medicine in July 2011. VMC's Statement of Net Position and Statement of Revenues, Expenses and Changes in Net Position are presented in a discrete column together with NWH on the financial statements of the University.

**Northwest Hospital & Medical Center** (NWH) is a full-service medical facility with 281 beds, and treats approximately 10,000 inpatients per year. NWH joined UW Medicine in January 2010. NWH's Statement of Net Position and Statement of Revenues, Expenses and Changes in Net Position are presented in a discrete column together with VMC on the financial statements of the University.

**UW Neighborhood Clinics** (Neighborhood Clinics) is a network of primary care clinics with ten neighborhood locations throughout the greater Seattle area, providing primary care, urgent care and selected specialty care with a staff of approximately 85 healthcare providers. The revenues, expenses, assets and liabilities of Neighborhood Clinics are included in the University's financial statements.

**UW Physicians** (UWP) is the physician practice group for more than 1,800 faculty physicians and healthcare providers associated with UW Medicine. The revenues, expenses, assets and liabilities of UWP are included in the University's financial statements.

**Airlift Northwest** is the preeminent provider of air medical transport services in the Pacific Northwest. The revenues, expenses, assets and liabilities of Airlift Northwest are included in the University's financial statements.

The University is also a participant in two joint ventures: Seattle Cancer Care Alliance and Children's University Medical Group. The University's share of these activities is reflected in the University's financial statements.

In combination, these organizations (not including VMC and NWH) contributed $1,362 million in patient services revenue in fiscal year 2015, of which 76% was generated by UWMC. This compares to $1,207 million in patient services revenue in fiscal year 2014, of which 77% was generated by UWMC. UWMC admissions exceeded 18,000 in 2015, a slight increase from 2014. Average patient length of stay was nearly 7.0 days, up from 6.9 days in 2014. The increase in patient services revenue during 2015 is partly due to higher case acuity at UWMC, as well as strong case volumes in oncology, cardiology and neurosurgery.

Considerable progress has been made in implementing the Epic Electronic Medical Record (EMR) system throughout UW Medicine, with over 85 specialty clinics completed in May 2014. This milestone allowed UW Medicine to qualify for Medicare and Medicaid financial incentives, avoid penalties, and improve the quality and safety of care for patients through more timely and complete access to their records. To further enhance patient safety, UW Medicine also implemented barcoded electronic medication administration in all high risk inpatient units at UWMC.

Charity care has decreased as a result of the Medicaid expansion and implementation of the Healthcare Exchanges effective January 1, 2014. While patients continue to be treated from all walks of life including the mission population, the number of uninsured patients served at UW Medicine has declined and been accompanied by an increase in Medicaid patients.

### Gifts, Endowments and Investment Revenues

Net investment returns for the years ended June 30, 2015 and 2014 consisted of the following:

| (in millions) | 2015 | 2014 |
|---|---|---|
| Interest and dividends | $ 66 | $ 73 |
| Metropolitan tract net income | 16 | 8 |
| Investment in Seattle Cancer Care Alliance | 6 | 12 |
| Net appreciation of fair value of investments | 151 | 398 |
| Investment expenses | (12) | (10) |
| **Net investment income** | **$ 227** | **$ 481** |

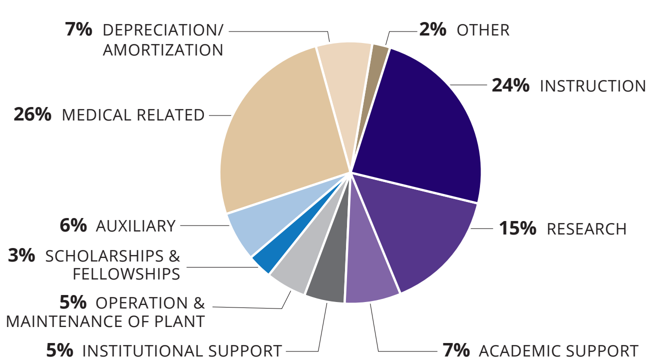
Net appreciation includes both realized and unrealized gains and losses. The unrealized gains, however, are not available until the underlying securities have been sold. Net investment income decreased by $254 million in 2015. The change in realized and unrealized gains and losses was the major factor in the variance.

Donor support increased by $9 million, or 5%, to $200 million in 2015. Gifts are a key and necessary source of support for a variety of purposes including capital improvements, scholarships, research, and endowments for various academic and research positions.

### Expenses

Two primary functions of the University, instruction and research, comprised 39% of total operating expenses. These dollars provided instruction to nearly 55,000 students and funded 5,000 research awards. Medical-related expenses, such as those related to patient care, also continue to be one of the largest individual components.

**Uses of Funds**




A comparative summary of the University's expenses by functional classification (purpose for which the costs are incurred) for the years ended June 30, 2015 and 2014 follows:

| (in millions) | 2015 | 2014 |
|---|---|---|
| Operating expenses: | | |
| Educational and general instruction | $ 1,114 | $ 1,037 |
| Research | 730 | 766 |
| Public service | 35 | 42 |
| Academic support | 337 | 297 |
| Student services | 43 | 43 |
| Institutional support | 215 | 224 |
| Operation and maintenance of plant | 241 | 201 |
| Scholarships and fellowships | 147 | 138 |
| Auxiliary enterprises | 292 | 286 |
| Medical-related | 1,203 | 1,042 |
| Depreciation/amortization | 311 | 308 |
| **Total operating expenses** | **$ 4,668** | **$ 4,384** |

Overall, the University's operating expenses increased by $284 million, or 6%, over 2014. Salaries expense increased $166 million, or 8% due to employee merit increases and a modest increase in FTE's. Despite an increase in the associated salaries, benefits expense decreased by $12 million, or 2%, due primarily to a reduction in pension expense as calculated under GASB Statement No. 68. In accordance with Statement No. 68, the difference between projected and actual investment earnings on plan assets during the measurement period for the net pension liability has been recorded as a deferred inflow and is being amortized to pension expense over five years. The University's proportionate share of that amortization reduced fiscal year 2015 pension expense by $67 million. Supplies and materials expense increased $44 million, or 11%, partly due to higher demand for medical supplies required by UWMC to support an increase in volumes related to patient care. Other operating expense increased by $35 million, or 34%, primarily due to increases in rental expense and costs associated with the University's self-insurance program.

Unaudited – see accompanying notes to basic financial statements

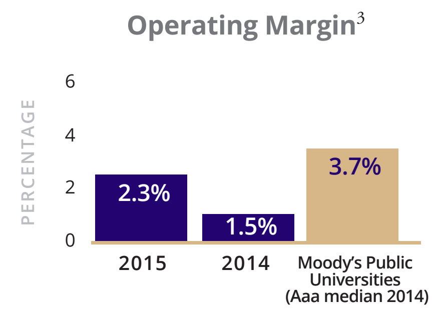
### Operating Loss

The University's operating loss decreased slightly to $451 million in 2015, from $470 million in 2014.

State appropriations are shown as nonoperating revenue, pursuant to GASB standards. If state appropriations were classified as operating revenue, the operating loss would have been $196 million in 2015, and $208 million in 2014. The University continues to rely on nonoperating revenues such as gift revenues and investment income distributions, in addition to state appropriations, to fund its operations.

### Operating Margin

Moody's measures the net result of revenue and expense activity by including several nonoperating revenues in the margin. The 2015 operating margin increased to 2.3%. Operating margin calculations include an estimated return on the University's investments rather than actual investment income. Therefore, variances in investment performance in a given year will not impact the operating margin.




3 Operating loss, (including interest expense, operating appropriations, nonoperating federal grants, an assumed 5% spending rate on investments and nonpermanent endowment gifts), divided by operating revenues (less scholarship expenses, and including operating appropriations, nonoperating federal grants, an assumed 5% return on investments and nonpermanent endowment gifts). Excludes Northwest Hospital and Valley Medical Center.

Unaudited – see accompanying notes to basic financial statements

# STATEMENTS OF NET POSITION

| | UNIVERSITY OF WASHINGTON June 30, 2015 | DISCRETE COMPONENT UNITS [1] June 30, 2015 |
|---|---|---|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | |
| **CURRENT ASSETS:** | | |
| CASH AND CASH EQUIVALENTS (NOTE 2) | $ 82,905 | $ 39,960 |
| INVESTMENTS, CURRENT PORTION (NOTE 6) | 679,505 | 24,477 |
| ACCOUNTS RECEIVABLE (NET OF ALLOWANCE OF $66,902) (NOTE 5) | 596,453 | 110,297 |
| OTHER CURRENT ASSETS | 43,459 | 63,444 |
| TOTAL CURRENT ASSETS | 1,402,322 | 238,178 |
| **NONCURRENT ASSETS:** | | |
| DEPOSIT WITH STATE OF WASHINGTON (NOTE 3) | 51,647 | – |
| INVESTMENTS, NET OF CURRENT PORTION (NOTE 6) | 4,297,157 | 66,168 |
| METROPOLITAN TRACT (NOTE 7) | 121,146 | – |
| STUDENT LOANS RECEIVABLE (NET OF ALLOWANCE OF $4,974) (NOTE 4) | 73,384 | – |
| DUE FROM DISCRETE COMPONENT UNITS | 93,240 | – |
| OTHER NONCURRENT ASSETS | 150,323 | 110,753 |
| CAPITAL ASSETS (NET OF ACCUMULATED DEPRECIATION OF $3,566,289) (NOTE 8) | 4,172,378 | 467,701 |
| TOTAL NONCURRENT ASSETS | 8,959,275 | 644,622 |
| TOTAL ASSETS | 10,361,597 | 882,800 |
| **DEFERRED OUTFLOWS OF RESOURCES:** | | |
| UNAMORTIZED LOSS ON BOND REFUNDING | 25,813 | 6,435 |
| PENSION-RELATED DEFERRED OUTFLOWS (NOTE 15) | 85,602 | – |
| TOTAL DEFERRED OUTFLOWS OF RESOURCES | 111,415 | 6,435 |
| **TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES** | **$ 10,473,012** | **$ 889,235** |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | |
| **CURRENT LIABILITIES:** | | |
| ACCOUNTS PAYABLE AND ACCRUED LIABILITIES | $ 626,085 | $ 121,160 |
| UNEARNED REVENUES | 155,114 | – |
| OTHER CURRENT LIABILITIES | 92,982 | 11,743 |
| LONG-TERM LIABILITIES, CURRENT PORTION (NOTES 9-11) | 124,137 | 9,001 |
| TOTAL CURRENT LIABILITIES | 998,318 | 141,904 |
| **NONCURRENT LIABILITIES:** | | |
| U.S. GOVERNMENT GRANTS REFUNDABLE | 51,985 | – |
| DUE TO PRIMARY GOVERNMENT | – | 93,240 |
| LONG-TERM LIABILITIES, NET OF CURRENT PORTION (NOTES 9-11) | 2,484,522 | 320,232 |
| NET PENSION LIABILITY (NOTE 15) | 622,589 | – |
| TOTAL NONCURRENT LIABILITIES | 3,159,096 | 413,472 |
| TOTAL LIABILITIES | 4,157,414 | 555,376 |
| **DEFERRED INFLOWS OF RESOURCES:** | | |
| PROPERTY TAXES | – | 9,625 |
| PENSION-RELATED DEFERRED INFLOWS (NOTE 15) | 269,135 | – |
| TOTAL DEFERRED INFLOWS OF RESOURCES | 269,135 | 9,625 |
| **TOTAL LIABILITIES AND DEFERRED INFLOWS OF RESOURCES** | **4,426,549** | **565,001** |
| NET POSITION | | |
| NET INVESTMENT IN CAPITAL ASSETS | 2,156,229 | 67,033 |
| RESTRICTED: | | |
| NONEXPENDABLE | 1,321,979 | 1,943 |
| EXPENDABLE | 1,699,135 | 8,471 |
| UNRESTRICTED | 869,120 | 246,787 |
| TOTAL NET POSITION | 6,046,463 | 324,234 |
| **TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION** | **$ 10,473,012** | **$ 889,235** |

[1] See Note 18

See accompanying notes to basic financial statements.

Dollars in thousands

# STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

| | UNIVERSITY OF WASHINGTON<br>Year ended June 30, 2015 | DISCRETE COMPONENT UNITS [1]<br>Year ended June 30, 2015 |
|---|---|---|
| **REVENUES** | | |
| **OPERATING REVENUES:** | | |
| STUDENT TUITION AND FEES (NET OF SCHOLARSHIP ALLOWANCE OF $142,685) | $ 914,419 | $ – |
| NET PATIENT SERVICE REVENUES (NET OF PROVISION FOR UNCOLLECTIBLE ACCOUNTS OF $15,947) | 1,362,279 | 822,421 |
| FEDERAL GRANTS AND CONTRACTS | 999,189 | – |
| STATE AND LOCAL GRANTS AND CONTRACTS | 87,629 | – |
| NONGOVERNMENTAL GRANTS AND CONTRACTS | 193,840 | – |
| SALES AND SERVICES OF EDUCATIONAL DEPARTMENTS | 223,494 | – |
| AUXILIARY ENTERPRISES: | | |
| HOUSING AND FOOD SERVICES | 111,531 | – |
| SPORTS PROGRAMS (NET OF SCHOLARSHIP ALLOWANCE OF $6,495) | 67,727 | – |
| OTHER AUXILIARY ENTERPRISES | 139,974 | – |
| OTHER MEDICAL-RELATED REVENUE | 45,157 | 53,165 |
| OTHER OPERATING REVENUE | 71,459 | – |
| **TOTAL OPERATING REVENUES** | **4,216,698** | **875,586** |
| **EXPENSES** | | |
| **OPERATING EXPENSES (NOTE 12):** | | |
| SALARIES | 2,192,781 | 384,254 |
| BENEFITS | 649,923 | 99,346 |
| SCHOLARSHIPS AND FELLOWSHIPS | 146,570 | – |
| UTILITIES | 60,454 | 8,480 |
| SUPPLIES AND MATERIALS | 463,624 | 161,694 |
| PURCHASED SERVICES | 707,678 | 142,741 |
| DEPRECIATION/AMORTIZATION | 310,960 | 49,238 |
| OTHER | 135,975 | 20,048 |
| **TOTAL OPERATING EXPENSES** | **4,667,965** | **865,801** |
| **OPERATING INCOME (LOSS)** | **(451,267)** | **9,785** |
| **NONOPERATING REVENUES (EXPENSES)** | | |
| STATE APPROPRIATIONS | 255,156 | – |
| GIFTS | 115,636 | 342 |
| INVESTMENT INCOME (NET OF INVESTMENT EXPENSE OF $11,741) | 227,404 | 4,385 |
| INTEREST ON CAPITAL ASSET-RELATED DEBT | (79,259) | (23,004) |
| PELL GRANT REVENUE | 48,471 | – |
| PROPERTY TAX REVENUE | – | 18,132 |
| OTHER NONOPERATING REVENUES (EXPENSES) | 9,042 | 630 |
| **NET NONOPERATING REVENUES** | **576,450** | **485** |
| **INCOME BEFORE OTHER REVENUES** | **125,183** | **10,270** |
| CAPITAL APPROPRIATIONS | 20,812 | – |
| CAPITAL GRANTS, GIFTS AND OTHER | 21,986 | 2 |
| GIFTS TO PERMANENT ENDOWMENTS | 67,359 | 167 |
| **TOTAL OTHER REVENUES** | **110,157** | **169** |
| **INCREASE IN NET POSITION** | **235,340** | **10,439** |
| **NET POSITION** | | |
| NET POSITION – BEGINNING OF YEAR, AS RESTATED (NOTE 1) | 5,811,123 | 313,795 |
| **NET POSITION – END OF YEAR** | **$ 6,046,463** | **$ 324,234** |

[1] See Note 18

See accompanying notes to basic financial statements.

Dollars in thousands

# STATEMENT OF CASH FLOWS

| | UNIVERSITY OF WASHINGTON<br>Year Ended June 30, 2015 |
|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | |
| STUDENT TUITION AND FEES | $ 882,465 |
| PATIENT SERVICES | 1,328,801 |
| GRANTS AND CONTRACTS | 1,291,442 |
| PAYMENTS TO SUPPLIERS | (465,995) |
| PAYMENTS FOR UTILITIES | (60,009) |
| PURCHASED SERVICES | (707,938) |
| OTHER OPERATING DISBURSEMENTS | (132,406) |
| PAYMENTS TO EMPLOYEES | (2,186,431) |
| PAYMENTS FOR BENEFITS | (588,216) |
| PAYMENTS FOR SCHOLARSHIPS AND FELLOWSHIPS | (146,570) |
| LOANS ISSUED TO STUDENTS | (24,858) |
| COLLECTION OF LOANS TO STUDENTS | 23,530 |
| OTHER MEDICAL CENTER RECEIPTS | 45,157 |
| AUXILIARY ENTERPRISE RECEIPTS | 305,523 |
| SALES AND SERVICES OF EDUCATIONAL DEPARTMENTS | 220,004 |
| RECEIPTS FROM OUTSIDE AFFILIATED AGENCIES | 714,996 |
| DISBURSEMENTS TO OUTSIDE AFFILIATED AGENCIES | (712,292) |
| OTHER RECEIPTS | 96,441 |
| **NET CASH USED BY OPERATING ACTIVITIES** | **(116,356)** |
| **CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES** | |
| STATE APPROPRIATIONS | 255,613 |
| GIFTS AND GRANTS FOR OTHER THAN CAPITAL PURPOSES | 48,471 |
| PRIVATE GIFTS | 91,574 |
| PERMANENT ENDOWMENT RECEIPTS | 67,359 |
| DIRECT LENDING RECEIPTS | 239,000 |
| DIRECT LENDING DISBURSEMENTS | (240,607) |
| TRANSFERS TO COMPONENT UNITS | (100,945) |
| OTHER | 52,514 |
| **NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES** | **412,979** |
| **CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES** | |
| PROCEEDS FROM CAPITAL DEBT | 450,469 |
| STATE CAPITAL APPROPRIATIONS | 20,928 |
| CAPITAL GRANTS AND GIFTS RECEIVED | 21,651 |
| ACQUISITION AND CONSTRUCTION OF CAPITAL ASSETS | (432,885) |
| PRINCIPAL PAYMENTS ON CAPITAL-RELATED DEBT AND LEASES | (386,874) |
| INTEREST PAYMENTS ON CAPITAL-RELATED DEBT AND LEASES | (98,911) |
| OTHER | 5,427 |
| **NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES** | **(420,195)** |

| CASH FLOWS FROM INVESTING ACTIVITIES | Year Ended June 30, 2015 |
|---|---|
| PROCEEDS FROM SALES OF INVESTMENTS | 6,931,799 |
| DISBURSEMENTS FOR PURCHASES OF INVESTMENTS | (6,874,325) |
| INVESTMENT INCOME | 69,875 |
| **NET CASH PROVIDED BY INVESTING ACTIVITIES** | **127,349** |
| | |
| **NET INCREASE IN CASH AND CASH EQUIVALENTS** | **3,777** |
| CASH AND CASH EQUIVALENTS-BEGINNING OF THE YEAR | 79,128 |
| **CASH AND CASH EQUIVALENTS-END OF THE YEAR** | **$ 82,905** |

| RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES | |
|---|---|
| OPERATING LOSS | $ (451,267) |
| ADJUSTMENTS TO RECONCILE OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES: | |
| DEPRECIATION/AMORTIZATION EXPENSE | 310,960 |
| CHANGES IN ASSETS AND LIABILITIES: | |
| RECEIVABLES | (13,716) |
| OTHER ASSETS | (39,572) |
| PENSION-RELATED DEFERRED INFLOWS AND OUTFLOWS OF RESOURCES | 264,460 |
| NET PENSION LIABILITY | (289,763) |
| ACCOUNTS PAYABLE AND ACCRUED LIABILITIES | 24,763 |
| UNEARNED REVENUE | (10,813) |
| OTHER LONG-TERM LIABILITIES | 89,920 |
| U.S. GOVERNMENTAL GRANTS REFUNDABLE | (442) |
| LOANS TO STUDENTS | (886) |
| **NET CASH USED BY OPERATING ACTIVITIES** | **$ (116,356)** |

| NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES | |
|---|---|
| STOCK GIFTS | $ 24,062 |
| INCREASE IN INTEREST IN SEATTLE CANCER CARE ALLIANCE | 6,319 |
| NET UNREALIZED GAINS | 79,724 |
| **TOTAL NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES** | **$ 110,105** |

See accompanying notes to basic financial statements.
Dollars in thousands

# NOTES TO FINANCIAL STATEMENTS

## NOTE 1:

## Summary of Significant Accounting Policies

### FINANCIAL REPORTING ENTITY

The University of Washington (University), an agency of the state of Washington, is governed by a 10-member Board of Regents appointed by the governor and confirmed by the state senate.

The financial statements include the individual schools, colleges and departments of the University, the University of Washington Medical Center (UWMC), Portage Bay Insurance (a wholly-owned subsidiary of the University) and certain affiliated operations determined to be a part of the University's financial reporting entity. Affiliated organizations are evaluated for inclusion in the reporting entity as component units based on the significance of their relationship with the University.

Harborview Medical Center (HMC), a component unit of King County, Washington, is a related party to the University, but is not reflected as part of the financial reporting entity (Note 13).

Component units are legally separate organizations for which the University is financially accountable. These entities may be reported in the financial statements of the primary government in one of two ways: the component units' amounts may be blended with the amounts reported by the primary government, or they may be shown in a separate column, depending on the application of the criteria of Governmental Accounting Standards Board (GASB) Statement No. 61, "The Financial Reporting Entity: Omnibus." All component units of the University meet the criteria for blending except Northwest Hospital & Medical Center and Valley Medical Center. They are reported discretely, since they have separate boards of directors and they do not provide services exclusively to the University.

### BLENDED COMPONENT UNITS

The following entities are presented as blended component units because they provide service exclusively or almost exclusively to the University. Financial information for these affiliated organizations is available from their respective administrative offices.

**The Association of University Physicians dba UW Physicians (UWP)**

UWP was established as a tax-exempt entity for the exclusive benefit of the University of Washington School of Medicine (UWSOM). UWP employs UWSOM faculty and bills and collects for their clinical services as an agent for UWSOM. UWP had operating revenues of $204,079,000 in 2015.

**UW Medicine Neighborhood Clinics (Neighborhood Clinics)**

Neighborhood Clinics was established as a tax-exempt entity for the benefit of UWSOM, UWP and its affiliated medical centers, HMC and UWMC, exclusively for charitable, scientific and educational purposes. Neighborhood Clinics was organized to coordinate and develop patient care in a community clinical setting. They enhance the academic environment of UWSOM by providing additional sites of primary care practice and training for faculty, residents and students. Neighborhood Clinics had operating revenues of $16,008,000 in 2015.

**Real estate financing entities**

The entities listed below are nonprofit corporations that were formed to acquire, construct or renovate certain real properties for the benefit of the University in fulfilling its educational, medical or scientific research missions. These entities issue tax-exempt and taxable bonds to finance these activities.

- Washington Biomedical Research Properties I
- Washington Biomedical Research Properties II
- Washington Biomedical Research Facilities 3

These entities collectively have net capital assets of $278,928,000, and long-term debt of $281,550,000, in 2015. These amounts are reflected in the University's financial statements.

### DISCRETELY PRESENTED COMPONENT UNITS

**Northwest Hospital**

UW Medicine and Northwest Hospital & Medical Center (NWH), a 281-bed full-service acute care hospital, entered into an affiliation agreement effective January 1, 2010. The University is the sole corporate member of Northwest Hospital. The audited financial statements of Northwest Hospital are available by contacting Northwest Hospital & Medical Center at 1550 N. 115th Street, Seattle, Washington 98133-9733, Mailstop X-112.

**Valley Medical Center**
UW Medicine and Public Hospital District No. 1 of King County, a Washington public hospital district dba Valley Medical Center, entered into a strategic alliance, effective July 1, 2011. Valley Medical Center owns and operates a 321-bed full-service acute care hospital and 45 clinics located throughout southeast King County. The audited financial statements of Valley Medical Center are available by contacting Valley Medical Center at 400 S. 43rd Street, Renton, Washington 98055 or online at the following address: www.valleymed.org/about-us/financial-information/.

### JOINT VENTURES

The University, together with Seattle Children's Hospital and Fred Hutchinson Cancer Research Center established the Seattle Cancer Care Alliance (SCCA). The SCCA integrates the cancer research, teaching and clinical cancer programs of all three institutions to provide state-of-the-art cancer care. Each member of the SCCA has a one-third interest. The University accounts for its interest in SCCA under the equity method and has recorded $107,704,000 in Other Assets, together with $6,319,000 in Investment Income, for its share of the joint venture in 2015.

The University and Seattle Children's Hospital established Children's University Medical Group (CUMG) to assist the organizations in carrying out their pediatric patient care, charitable, educational, and scientific missions. CUMG employs UWSOM faculty physicians, and bills and collects for their services as an agent for UWSOM. The University records revenue from CUMG based on the income distribution plan effective December 31, 2008. The University's patient services receivable (Note 5) includes amounts due from CUMG of $18,852,000 in 2015.

### CHANGES IN REPORTING ENTITY

In fiscal year 2015, the University paid the remaining outstanding principal balance on the TSB Properties Lease Revenue Bonds, 2006, and title to the property was passed to the University. The entity that issued the leased-backed bonds, TSB Properties, was dissolved and is no longer a blended component unit of the University.

### BASIS OF ACCOUNTING

The financial statements of the University have been prepared in accordance with GASB Statement No. 34, "Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments," as amended by GASB Statement No. 35, "Basic Financial Statements — and Management's Discussion and Analysis — for Public Colleges and Universities." The University is reporting as a special-purpose government engaged in business-type activities (BTA). In accordance with BTA reporting, the University presents management's discussion and analysis, statements of net position, statements of revenues, expenses and changes in net position, statement of cash flows and notes to the financial statements. The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

Under the accrual basis of accounting, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All intra-agency transactions have been eliminated. The University reports capital assets net of accumulated depreciation/amortization (as applicable), and reports depreciation/amortization expense in the Statements of Revenues, Expenses and Changes in Net Position.

On July 1, 2014, the University adopted GASB Statement No. 68, "Accounting and Financial Reporting for Pensions." This Statement requires governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, which is measured as the total pension liability less the amount of the pension plan's fiduciary net position. The total pension liability is determined by discounting projected benefit payments based on the benefit terms and legal agreements existing at the pension plan's fiscal year end. Projected benefit payments are required to be discounted using a single rate that reflects the expected rate of return on investments, to the extent that plan assets are available to pay benefits. When plan assets are insufficient to pay benefits, the discount rate used is a blended rate comprised of the expected rate of return over the period when projected plan assets exist to pay benefits, and then a tax-exempt, high-quality municipal bond rate for the periods when projected plan assets are not available. This Statement requires that most changes in the net pension liability be included in pension expense in the period of the change. Prior to adopting this Statement, the University reported pension expense based on cash contributions paid to the pension plan administrator. In addition to the reporting changes described above, implementation of this Statement resulted in the restatement of fiscal year 2015 beginning unrestricted net position, reducing it by $831,426,000. The University's Statement of Net Position, Statement of Revenues, Expenses and Changes in Net Position, and the Statement of Cash Flows present only one fiscal year, since the change in accounting treatment required by Statement No. 68 is not able to be applied to the prior fiscal year due to the constraints of available information.

With the adoption of GASB Statement No. 68, net position was restated at July 1, 2014. Below is a reconciliation of total net position as previously reported at June 30, 2014, to the restated net position.

| *(Dollars in thousands)* | |
|---|---|
| NET POSITION AT JUNE 30, 2014, AS PREVIOUSLY REPORTED | $ 6,642,549 |
| ADOPTION OF GASB STATEMENT NO. 68 | (831,426) |
| **NET POSITION AT JULY 1, 2014, AS RESTATED** | **$ 5,811,123** |

On July 1, 2014, the University adopted GASB Statement No. 69, "Government Combinations and Disposals of Government Operations." This Statement requires disclosures to be made about government combinations and disposals of government operations, in order to enable financial statement users to evaluate the nature and financial effects of those transactions. There was no impact to the financial statements of the University as a result of implementing this Statement.

On July 1, 2014, the University adopted GASB Statement No. 71, "Pension Transition for Contributions Made Subsequent to the Measurement Date," an amendment of GASB Statement No. 68, "Accounting and Financial Reporting for Pensions." The purpose of this Statement is to address application of the transition provisions of GASB Statement No. 68, and clarify guidance regarding contributions made by a state or local government employer, or nonemployer contributing entity, to a defined benefit pension plan after the measurement date of the government's beginning net pension liability. Implementation of this Statement reduced the restatement of beginning unrestricted net position resulting from GASB Statement No. 68 by $80,926,000.

### ACCOUNTING STANDARDS IMPACTING THE FUTURE

In February 2015, the GASB issued Statement No. 72, "Fair Value Measurement and Application", which will be effective for the fiscal year ending June 30, 2016. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments, and disclosures related to all fair value measurements. This Statement establishes a three-level hierarchy of inputs to valuation techniques used to measure fair value, and requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. The University is currently analyzing the impact of this Statement.

In June 2015, the GASB issued Statement No. 73, "Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68". Amendments to Statement No. 68 will be effective for the fiscal year ending June 30, 2016 and the guidance for plans not within the scope of Statement No. 68 will be effective for the fiscal year ending June 30, 2017. This Statement is intended to improve financial reporting of governments whose employees are provided with pensions that are not within the scope of Statement No. 68, improve the usefulness of information associated with governments that hold assets accumulated for purposes of providing defined benefit pensions not within the scope of Statement No. 68, and to clarify the application of certain provisions of Statements No. 67 & 68. The University is currently analyzing the impact of this Statement.

In June 2015, the GASB issued Statement No. 74, "Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans", which is effective for the fiscal year ending June 30, 2017. The objective of this Statement is to improve the usefulness of information about other postemployment benefits (OPEB) such as death benefits, life insurance, disability, and long-term care in the financial reports of governments that provide them. This Statement replaces Statement No. 43, "Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans, as amended." The University is currently analyzing the applicability of this Statement.

In June 2015, the GASB issued Statement No. 75, "Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions", which is effective for the fiscal year ending June 30, 2018. This Statement establishes standards of accounting and financial reporting for defined benefit OPEB and defined contribution OPEB that are provided to the employees of state and local governmental employers through OPEB plans that are administered through trusts or equivalent arrangements. This Statement also establishes standards of accounting and financial reporting for OPEB plans that are not administered through trusts or equivalent arrangements. The University is currently analyzing the impact of this Statement.

In June 2015, the GASB issued Statement No. 76, "The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments", which is effective for the fiscal year ending June 30, 2016. The objective of this Statement is to identify the hierarchy of generally accepted accounting principles (GAAP). This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP, and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. The University is currently analyzing the impact of this Statement.

In August 2015, the GASB issued Statement No. 77, "Tax Abatement Disclosures", which is effective for the fiscal year ending June 30, 2017. This Statement defines a tax abatement as resulting from an agreement between a government and an individual or entity in which the government promises to forgo tax revenues, and the individual or entity promises to subsequently take a specific action that contributes to economic development or otherwise benefits the government or its citizens. This Statement requires governments that enter into tax abatement agreements to disclose information about the agreements. The University is currently analyzing the impact of this Statement.

### USE OF ESTIMATES

The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles involves management estimates that affect the reported amounts of assets, liabilities, deferrals, revenues and expenses during the reporting period. Actual results could differ from those estimates; however, in each case, the University believes that allowances, reserves and estimates of expected liabilities are adequate.

The University estimates the pollution remediation liability (Note 9) by reviewing the current status of known polluted sites and developing estimates of cleanup costs. These estimates are subject to change due to improvements in technology, inflation, changes in the scope of work, and the pursuit of reimbursement from other responsible parties.

Allowances (Notes 4 and 5) are estimates based on the historical experience of the University and current economic circumstances with respect to the collectability of accounts and loans receivable.

The University's share of pension plan assets, liabilities, deferrals and expenses related to the plans administered by the Washington Department of Retirement Systems, and the liability and expense related to the University of Washington Supplemental Retirement Plan (Note 15), reported in the University's financial statements are based on actuarial valuations prepared by an external actuary. The results of an actuarial valuation are estimates based on historical data, actuarial assumptions, and the demographics of the employee population.

The self-insurance reserve (Note 16) is estimated through an externally prepared actuarial calculation using individual case-basis valuations and statistical analyses. Considerable variability is inherent in such estimates.

### OTHER ACCOUNTING POLICIES

**Investments.** Investments are generally carried at fair value. The fair value of all debt and equity securities with a readily determinable fair value is based on quotations from major securities exchanges. Alternative investments, which are not readily marketable, are carried at the estimated fair values provided by the investment managers. The University reviews and evaluates the values provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these securities existed.

Investments under long-term strategies are considered noncurrent. Short-term investments consist primarily of cash equivalents and fixed income vehicles which management has identified as available to meet the day-to-day obligations of the University.

**Inventories.** Inventories are carried at the lower of cost or market value and reflected on the Statement of Net Position in Other Current Assets. Consumable inventories, consisting of expendable materials and supplies, are generally valued using the weighted-average method. Merchandise inventories are generally valued using the first-in, first-out method.

**Capital Assets.** Land, buildings, equipment, library books and intangibles are stated at cost or, if acquired by gift, at fair market value at the date of the gift. Additions, replacements, major repairs and renovations are capitalized. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets, generally 15 to 50 years for building components, 20 to 50 years for infrastructure and land improvements, 5 to 7 years for equipment, 15 years for library books, and 3 to 15 years for intangibles.

Interest incurred on capital asset-related debt was $86,931,000 during 2015. The University capitalized $7,672,000 of this cost during 2015.

**Unearned Revenues.** Unearned revenues occur when funds have been collected in advance of when the associated goods or services have been provided, such as advance ticket sales, summer quarter tuition and unspent cash advances on certain grants.

**Cost-Sharing Pension Plans.** The net pension asset or liability is measured as the University's proportionate share of the collective total pension liability, less the fiduciary net position, of the cost-sharing pension plans in which the University participates. The total pension liability is determined based upon discounting projected benefit payments based on the benefit terms and legal agreements existing at the pension plan's fiscal year end. Projected benefit payments are required to be discounted using a single rate that reflects the expected rate of return on investments, to the extent that plan assets are available to pay benefits. When plan assets are insufficient to pay benefits, the discount rate used is a blended rate comprised of the expected rate of return over the period when projected plan assets exist to pay benefits, and then a tax-exempt, high-quality municipal bond rate for the periods when projected plan assets are not available. The University's proportionate share is determined based on the relationship of University contributions to total contributions to the plan by all participating employers. Pension expense is recognized for benefits earned during the period, interest on the unfunded liability and changes in benefit terms. Differences between expected and actual experience, and changes in assumptions about future economic or demographic factors, are reported as deferred inflows of resources or deferred outflows of resources, and are recognized over the average expected remaining service period for employees eligible for pension benefits. Differences between expected and actual investment returns are reported as deferred inflows of resources or deferred outflows of resources, and are recognized over five years. Contributions made to the plan subsequent to the measurement date and prior to the University's fiscal year end are reported as a deferred outflow of resources, and recognized in the subsequent fiscal year. The measurement date for the cost-sharing plans in which the University participates is June 30 of the prior fiscal year.

**Split-Interest Agreements.** Under most agreements, donors/beneficiaries receive income for their lifetime or for a stated term, with the University receiving the remaining principal. The University records an asset related to these agreements at fair market value at year-end. The University also records a liability related to the split-interest agreements equal to the present value of expected future distributions; the discount rates applied range from 3.7% to 8.0%.

**Compensated Absences.** University employees accrue annual leave at rates based on length of service, and for sick leave at the rate of one day per month. Sick leave balances, which are unlimited, can be converted to monetary compensation annually at 25% of the employees' normal compensation rate for any balance that exceeds 480 hours, or for any balance upon retirement or death. Annual leave accrued at June 30, 2015 was $93,328,000, and is included in Accounts Payable and Accrued Liabilities. Sick leave accrued as of June 30, 2015 was $37,984,000, and is included in Long-Term Liabilities (Note 9).

**Scholarship Allowances.** Tuition and Fees are reported net of scholarship allowances that are applied to students' accounts from external funds that have already been recognized as revenue by the University. Student aid paid directly to students is reported as scholarships and fellowships expense.

**Net Patient Services Revenue.** Patient services revenue is recorded at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Revenue related to charity care provided to patients is excluded from net patient services revenue.

Third-party payor agreements with Medicare and Medicaid provide for payments at amounts different from established rates and are part of contractual adjustments to net patient services revenue. Medicare reimbursements are based on a tentative rate, with final settlement determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. The estimated final settlements for open years are based on preliminary cost findings after giving consideration to interim payments that have been received on behalf of patients covered under these programs.

For more information about UWMC operations and financial results, see their audited financial statements which are contained in the latest Bondholders Report at http://f2.washington.edu/treasury/sites/default/UW_BondholdersReport_15.pdf.

**Charity Care.** Based on established rates, the charges for patient services forgone as a result of charity care during the year ended June 30, 2015 were $31,915,000.

The cost of charity care is estimated based on the ratio of the cost of providing care to the value of the charges forgone. Applying this ratio results in an estimated cost of charity care and uncompensated care of $11,530,000 in fiscal year 2015.

**State Appropriations.** The state of Washington appropriates funds to the University on both annual and biennial bases. These revenues are reported as nonoperating revenues in the Statements of Revenues, Expenses and Changes in Net Position.

**Operating Activities.** The University's policy for reporting operating activities in the Statements of Revenues, Expenses and Changes in Net Position is to include activities that generally result from exchange transactions. Examples of exchange transactions are payments received for tuition, patient services or grants under which services are performed, as well as payments made for the delivery of goods or services. Certain other significant revenue streams used for operations, such as state appropriations, Pell grants, gifts and investment income are recorded as nonoperating revenues, as prescribed by GASB Statement No. 35.

**Net Position.** The University's net position is classified as follows:

*Net investment in capital assets:* The University's investments in capital assets, less accumulated depreciation/amortization, net of outstanding debt obligations related to capital assets;

*Restricted net position – nonexpendable:* Net position subject to externally-imposed requirements that it be maintained permanently by the University, including permanent endowment funds and annuity and life income trusts;

*Restricted net position – expendable:* Net position that the University is obligated to spend in accordance with restrictions imposed by external parties, generally for scholarships, research and departmental uses;

*Unrestricted net position:* Net position not subject to externally-imposed restrictions and which may be designated for specific purposes by management or the Board of Regents.

**Tax Exemption.** The University, as an agency of the state of Washington, is not subject to federal income tax pursuant to Section 115 of the Internal Revenue Code, except for tax on unrelated business income and certain federal excise taxes.

**NOTE 2:**

## Cash and Cash Equivalents

Cash includes cash on hand, petty cash and bank deposits. Most cash, except for cash held at the University and cash held in foreign banks, is covered by the Federal Deposit Insurance Corporation (FDIC), or if greater than FDIC limits, by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

At June 30, 2015, bank balances of $108,423,000 were either insured by the FDIC or collateralized under the PDPC.

**NOTE 3:**

## Deposit with State of Washington

State law requires the University to deposit certain funds with the state treasurer, who holds and invests the funds. These deposits include amounts held for the University's permanent land grant funds, and the University of Washington building fee collected from students. The fair value of these funds approximates the carrying value.

**NOTE 4:**

## Student Loans Receivable

Net student loans of $73,384,000 at June 30, 2015 consist of $55,537,000 from federal programs and $17,847,000 from University programs. Interest income from student loans for the year ended June 30, 2015 was $1,690,000. These unsecured loans are made primarily to students who reside in the state of Washington.

**NOTE 5:**

## Accounts Receivable

The major components of accounts receivable as of June 30, 2015 were:

| *(Dollars in thousands)* | **2015** |
|---|---|
| NET PATIENT SERVICES | $ 325,813 |
| GRANTS AND CONTRACTS | 179,621 |
| SALES AND SERVICES | 30,753 |
| TUITION | 12,094 |
| DUE FROM OTHER AGENCIES | 47,851 |
| ROYALTIES | 4,893 |
| INVESTMENTS | 31,392 |
| STATE APPROPRIATIONS | 5,930 |
| OTHER | 25,008 |
| **SUBTOTAL** | **663,355** |
| LESS: ALLOWANCE FOR DOUBTFUL ACCOUNTS | (66,902) |
| **TOTAL** | **$ 596,453** |

**NOTE 6:**

## Investments

### INVESTMENTS - GENERAL

The Board of Regents of the University of Washington is responsible for the management of the University's investments. The Board of Regents establishes investment policy, which is carried out by the Chief Investment Officer. The University of Washington Investment Committee, comprised of board members and investment professionals, advises on matters relating to the management of the University's investment portfolios. The composition of the carrying amounts of investments by type at June 30, 2015 is listed in Table 1.

**TABLE 1 – UNIVERSITY INVESTMENTS** *(Dollars in thousands)*

| | Carrying Value |
|---|---|
| **Investment Type** | **2015** |
| FIXED INCOME – CASH EQUIVALENTS | $ 403,978 |
| FIXED INCOME | 1,726,481 |
| EQUITY | 1,733,102 |
| NON-MARKETABLE ALTERNATIVES* | 353,053 |
| ABSOLUTE RETURN* | 561,999 |
| REAL ASSETS* | 189,447 |
| MISCELLANEOUS | 8,602 |
| **TOTAL INVESTMENTS** | **$ 4,976,662** |

* Investment type includes private and other illiquid investments held in the Consolidated Endowment Fund

### INVESTMENT POOLS

The University combines most short-term cash balances into the Invested Funds Pool. At June 30, 2015, the Invested Funds Pool totaled $1,526,380,000. The Invested Funds Pool also owns units in the Consolidated Endowment Fund (CEF) valued at $806,198,000 on June 30, 2015. By University policy, departments with qualifying funds in the Invested Funds Pool receive distributions based on their average balances and on the type of balance. Campus depositors received 2% in fiscal year 2015. Endowment operating and gift accounts received 3% in fiscal year 2015, with the distributions directed to the University. The difference between the actual earnings of the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The majority of the endowed funds are invested in the CEF, a pooled fund. Individual endowments purchase units in the pool on the basis of a per-unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held. RCW 24.55 of the Washington State Code and the Uniform Prudent Management of Institutional Funds Act allow for total return expenditure under comprehensive prudent standards.

Under the CEF spending policy approved by the Board of Regents, quarterly distributions to programs are based on an annual percentage rate of 4%, applied to the five-year rolling average of the CEF's market valuation. Additionally, the policy allows for an administrative fee of 1% supporting campus-wide fundraising and stewardship activities (0.80%) and offsetting the internal cost of managing endowment assets (0.20%). This policy was effective with the December 2010 quarterly distributions, with the five-year averaging period implemented incrementally.

The University records its permanent endowments at the lower of original gift value or current market value in the Restricted Nonexpendable Net Position category. Of the endowments that are recorded at current market value, the net deficiency from the original gift value is $2,986,000 at June 30, 2015.

Funds in irrevocable trusts managed by trustees other than the University are not reported in the financial statements. The fair value of these funds was $111,442,000 at June 30, 2015. Income received from these trusts, which is included in Investment Income, was $6,162,000 for the year ended June 30, 2015.

Net appreciation (depreciation) in the fair value of investments includes both realized and unrealized gains and losses on investments. The University realized net gains of $71,485,000 in 2015 from the sale of investments. The calculation of realized gains and losses is independent of the net appreciation of the fair value of investments. Realized gains and losses on investments that have been held in more than one fiscal year and are sold in the current year include the net appreciation of these investments reported in the prior year(s). The net appreciation in the fair value of investments during the year ended June 30, 2015 was $151,209,000.

### FUNDING COMMITMENTS

The University enters into contracts with investment managers to fund alternative investments. As of June 30, 2015, the University had outstanding commitments to fund alternative investments of $329,901,000. These commitments are expected to be called over a multi-year time frame. The University believes it has adequate liquidity and funding sources to meet these obligations.

### DERIVATIVES

The University's investment policies allow investing in various derivative instruments, including futures, swaps and forwards, to manage exposures within or across the portfolio and to improve the portfolio's risk/return profile. Futures are financial contracts obligating the buyer to purchase an asset at a predetermined future date and price. Total return swaps involve commitments to pay interest in exchange for a market-linked return, both based on notional amounts. Derivative instruments are recorded on the contract date and are carried at fair value using listed price quotations or amounts that approximate fair value. The fair value and notional amount of investment derivative instruments outstanding at June 30, 2015, categorized by type, are as follows:

**TABLE 2 – INVESTMENT DERIVATIVES** *(Dollars in thousands)*

| Notional Amount as of June 30 | | Fair Value as of June 30 | | Change in Fair Value | |
|---|---|---|---|---|---|
| DESCRIPTION | 2015 | ASSET CLASSIFICATION | 2015 | INCOME CLASSIFICATION | 2015 |
| FUTURES CONTRACTS | $100,747 | INVESTMENTS | $100,286 | INVESTMENT INCOME | ($461) |

Credit exposure represents exposure to counterparties relating to financial instruments, where gains exceed collateral held by the University or losses are less than the collateral posted by the University. There was no credit exposure as of June 30, 2015. No derivative instruments have been reclassified from a hedging instrument to an investment instrument.

Details on foreign currency derivatives are disclosed under Foreign Exchange Risk.

### INTEREST RATE RISK

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of fixed income securities. The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed-income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform, while controlling the interest rate risk in the portfolio. Effective duration is a commonly used measure of interest rate risk. The longer the duration, the more sensitive the portfolio is to changes in interest rates. The weighted average effective duration of the University's fixed income portfolio was 1.81 years at June 30, 2015.

### CREDIT RISK

Fixed income securities are subject to credit risk, which is the risk that the issuer or other counterparty to a financial instrument will not fulfill its obligations or that negative perceptions of the issuer's ability to make these payments will cause prices to decline. Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University Investment Policies limit fixed income exposure to investment grade assets. The Investment Policy for the Invested Funds' cash pool requires each manager to maintain an average quality rating of "AA" as issued by a nationally recognized rating organization. The Invested Funds' liquidity pool requires each manager to maintain an average quality rating of "A" and to hold 25% of their portfolios in government and government agency issues. The Investment Policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investment to investment grade credits.

Duration and credit risk figures at June 30, 2015 exclude $36,027,000 of fixed income securities held outside the CEF and the Invested Funds Pool. These amounts make up 1.69% of the University's fixed income investments (including cash equivalents), and are not included in the duration figures detailed in Table 3.

The composition of fixed income securities at June 30, 2015, along with credit quality and effective duration measures, is summarized as follows:

**TABLE 3 – FIXED INCOME: CREDIT QUALITY AND EFFECTIVE DURATION** *(Dollars in thousands)*

**2015**

| Investments | U.S. Government | Investment Grade* | Non-Investment Grade | Not Rated | Total | Duration (in years) |
|---|---|---|---|---|---|---|
| U.S. TREASURIES | $ 842,525 | $ – | $ – | $ – | $ 842,525 | 1.43 |
| U.S. GOVERNMENT AGENCY | 644,721 | – | – | – | 644,721 | 2.46 |
| MORTGAGE BACKED | – | 107,070 | 75,060 | 22,415 | 204,545 | 2.01 |
| ASSET BACKED | – | 195,968 | 6,998 | 24,111 | 227,077 | 1.73 |
| CORPORATE AND OTHER | – | 175,364 | – | 200 | 175,564 | 1.14 |
| **TOTAL** | **$1,487,246** | **$ 478,402** | **$ 82,058** | **$ 46,726** | **$ 2,094,432** | **1.81** |

* Investment Grade securities are those that are rated BBB and higher by Standard and Poor's or Baa and higher by Moody's

### FOREIGN EXCHANGE RISK

Foreign exchange risk is the risk that investments denominated in foreign currencies may lose value due to adverse fluctuations in the value of the U.S. dollar relative to foreign currencies. The University's investment policies permit investments in international equity and other asset classes, which can include foreign currency exposure. The University also enters into foreign currency forward contracts, futures contracts, and options to manage the foreign currency exposure. The University held non-U.S. denominated securities at June 30, 2015 of $1,195,070,000.

**TABLE 4 – INVESTMENTS DENOMINATED IN FOREIGN CURRENCY**

| *(Dollars in thousands)* | June 30, 2015 |
|---|---|
| CHINESE RENMINBI (RMB) | $ 211,184 |
| EURO (EUR) | 174,487 |
| INDIAN RUPEE (INR) | 112,679 |
| JAPANESE YEN (JPY) | 110,617 |
| HONG KONG DOLLAR (HKD) | 60,046 |
| SOUTH KOREAN WON (KRW) | 56,835 |
| BRITISH POUND (GBP) | 54,880 |
| BRAZILIAN REAL (BRL) | 54,225 |
| SWISS FRANC (CHF) | 39,061 |
| RUSSIAN RUBLE (RUB) | 36,218 |
| CANADIAN DOLLAR (CAD) | 35,385 |
| PHILIPPINE PESO (PHP) | 29,100 |
| TAIWANESE DOLLAR (TWD) | 27,055 |
| MEXICAN PESO (MXN) | 23,898 |
| REMAINING CURRENCIES | 169,400 |
| **TOTAL** | **$ 1,195,070** |

**NOTE 7:**

## Metropolitan Tract

The University of Washington Metropolitan Tract ("the Metropolitan Tract"), located in downtown Seattle, comprises approximately 11 acres of developed property, including office space, retail space, residential apartments, parking, and a luxury hotel. This land was the original site of the University from 1861 until 1895 when the University moved to its present location on Lake Washington. Since the early 1900s, the Metropolitan Tract has been leased by the University to entities responsible for developing and operating the property.

The balance as of June 30, 2015 represents operating assets net of liabilities, and land, buildings and improvements stated at appraised value as of November 1, 1954. The balance also includes subsequent capital additions and improvements at cost, less retirements and accumulated depreciation of $166,124,000, and is net of the outstanding balance of the associated long-term debt.

In March 2015, $8,500,000 of Metropolitan Tract commercial paper was refinanced and replaced by the issuance of University General Revenue and Refunding Bonds, 2015 A&B, as described in the refunding activity section of Note 11. The loan amount as of June 30, 2015 to the Metropolitan Tract under this agreement was $8,535,000. In addition, $33,400,000 of bond proceeds were loaned to the Metropolitan Tract as part of the Cobb Building lease termination. The loan amount as of June 30, 2015 under this agreement was $33,564,000. Both loans are unsecured, but expected to be repaid through revenues generated by the Metropolitan Tract properties.

### OFFICE PROPERTIES

On July 18, 1953, the University leased a significant portion of the office, retail, and parking facilities to Unico Properties LLC (formerly known as Unico Properties, Inc.) ("Unico"). In 2004, the Unico Lease was amended to exclude the Cobb Building, and a new lease for that building was signed with Unico.

The Unico Lease expired on October 31, 2014, and ownership of all leasehold assets transferred to the University. The University and Unico entered into a Transition Agreement to address "end of lease" issues that were not contemplated in the original Unico Lease. In addition, the following events occurred simultaneously with the Unico Lease expiration:

- The University terminated the ground lease with Unico for the Cobb Building and paid a termination price of $33,400,000
- Ownership of the Palomar Garage property transferred to the University as agreed to in the Unico Lease
- In accordance with the Predevelopment Agreement, the University entered into an Interim Agreement for the Rainier Square development site that provides Wright Runstad with significant control over the management and operation of the Rainier Square Building in exchange for a fixed rent schedule for up to seven years
- In connection with the Interim Agreement for the Rainer Square, the University entered into a property management agreement with Wright Runstad for the Rainier Tower Building
- The University hired Unico Properties LLC to oversee leasing for all of the office buildings and property management for all of the office buildings except the Rainer Tower

On May 15, 2014, the University entered into an agreement with Wright Runstad to undertake activities relating to the redevelopment of the site currently occupied by the Rainier Square ("Predevelopment Agreement"). In connection with this agreement, which commenced on November 1, 2014 and expires upon the retention of certain development milestones, the University would enter into a property management agreement for the Rainier Tower and an Interim Agreement for operation of the Rainier Square. Upon satisfaction of conditions included in the Pre-Development Agreement, the University plans to ground lease the site to Wright Runstad for a term of 80 years.

### HOTEL

On January 18, 1980, the Board of Regents entered into a lease ("the Hotel Lease") for the Olympic Hotel property, which expires in 2040. The hotel was operated as the Four Seasons Olympic Hotel until July 31, 2003. On August 1, 2003, the remaining lease term was assigned to LHCS Hotel Holding (2002), LLC. The hotel was renamed the Fairmont Olympic Hotel and managed by Fairmont Hotels and Resorts, Inc.

On September 18, 2007, Legacy REIT, a publicly traded Canadian real estate investment trust and parent company of LHCS Hotel Holding (2002), LLC, was purchased by Cadbridge Investors, LP, a limited partnership majority owned by Cadim (a division of the Caisse de depot et placement du Quebec). The tenant under the Hotel Lease remained the same, and the management of the hotel by Fairmont Hotels and Resorts, Inc. did not change. On June 1, 2015, the University consented to the assignment of the Hotel Lease from LHCS Hotel Holding (2002) LLC to IC/RCDP Seattle Hotel, an entity owned by affiliates of Rockwood IX REIT, Inc. and an affiliate of DiNapoli Capital Partners, LLC.

**NOTE 8:**

## Capital Assets

Capital asset activity for the period ended June 30, 2015 is summarized as follows:

| *(Dollars in thousands)* | Balance at June 30, 2014 | Additions/ Transfers | Retirements | Balance at June 30, 2015 |
|---|---|---|---|---|
| LAND | $ 126,795 | $ 1,953 | $ – | $ 128,748 |
| INFRASTRUCTURE | 194,002 | 11,068 | – | 205,070 |
| BUILDINGS | 5,244,985 | 70,936 | 2,575 | 5,313,346 |
| FURNITURE, FIXTURES AND EQUIPMENT | 1,223,811 | 104,985 | 84,785 | 1,244,011 |
| LIBRARY MATERIALS | 325,663 | 13,521 | 1,767 | 337,417 |
| CAPITALIZED COLLECTIONS | 7,093 | 65 | – | 7,158 |
| INTANGIBLE ASSETS | 105,319 | 25,484 | 6,946 | 123,857 |
| CONSTRUCTION IN PROGRESS | 121,696 | 224,043 | 1,931 | 343,808 |
| INTANGIBLES IN PROCESS | 25,412 | 17,615 | 7,775 | 35,252 |
| TOTAL COST | 7,374,776 | 469,670 | 105,779 | 7,738,667 |
| LESS ACCUMULATED DEPRECIATION/ AMORTIZATION: | | | | |
| INFRASTRUCTURE | 95,351 | 4,921 | – | 100,272 |
| BUILDINGS | 1,946,659 | 175,159 | 2,106 | 2,119,712 |
| FURNITURE, FIXTURES AND EQUIPMENT | 982,794 | 101,464 | 71,228 | 1,013,030 |
| LIBRARY MATERIALS | 239,087 | 12,546 | 1,317 | 250,316 |
| INTANGIBLE ASSETS | 66,089 | 16,870 | – | 82,959 |
| TOTAL ACCUMULATED DEPRECIATION/AMORTIZATION | 3,329,980 | 310,960 | 74,651 | 3,566,289 |
| **CAPITAL ASSETS, NET** | **$4,044,796** | **$ 158,710** | **$ 31,128** | **$4,172,378** |

**NOTE 9:**

## Long-Term Liabilities

### UNIVERSITY OF WASHINGTON

Long-term liability activity for the period ended June 30, 2015 is summarized as follows:

| *(Dollars in thousands)* | Balance at June 30, 2014 | Additions/ Transfers | Reductions | Balance at June 30, 2015 | Current Portion 2015 |
|---|---|---|---|---|---|
| BONDS PAYABLE: | | | | | |
| GENERAL OBLIGATION BONDS PAYABLE (NOTE 11) | $ 165,044 | $ 260 | $ 15,740 | $ 149,564 | $ 18,290 |
| REVENUE BONDS PAYABLE (NOTE 11) | 1,764,855 | 291,750 | 347,540 | 1,709,065 | 41,055 |
| UNAMORTIZED PREMIUM ON BONDS | 101,456 | 39,709 | 15,978 | 125,187 | 13,416 |
| TOTAL BONDS PAYABLE | 2,031,355 | 331,719 | 379,258 | 1,983,816 | 72,761 |
| NOTES PAYABLE AND CAPITAL LEASES: | | | | | |
| NOTES PAYABLE & OTHER – CAPITAL ASSET RELATED (NOTE 11) | 24,008 | 7,205 | 2,975 | 28,238 | 5,020 |
| NOTES PAYABLE & OTHER – NONCAPITAL ASSET RELATED (NOTE 11) | 1,822 | – | 65 | 1,757 | 1,546 |
| CAPITAL LEASE OBLIGATIONS (NOTE 10) | 20,457 | – | 4,641 | 15,816 | 3,479 |
| TOTAL NOTES PAYABLE AND CAPITAL LEASES | 46,287 | 7,205 | 7,681 | 45,811 | 10,045 |
| OTHER LONG-TERM LIABILITIES: | | | | | |
| OBLIGATIONS UNDER SPLIT-INTEREST AGREEMENTS | 36,684 | 5,614 | – | 42,298 | – |
| POLLUTION REMEDIATION LIABILITY (NOTE 1) | 22,000 | – | – | 22,000 | 4,000 |
| DUE TO RELATED PARTY (NOTE 13) | 16,366 | 11,760 | 5,500 | 22,626 | 8,500 |
| SICK LEAVE (NOTE 1) | 36,174 | 6,852 | 5,042 | 37,984 | 4,974 |
| SELF-INSURANCE (NOTE 16) | 67,450 | 29,495 | 14,744 | 82,201 | 20,459 |
| COMMERCIAL PAPER | – | 111,545 | – | 111,545 | – |
| UWSRP NET PENSION OBLIGATION (NOTE 15) | 198,895 | 53,057 | 3,766 | 248,186 | 3,398 |
| OTHER NONCURRENT LIABILITIES | – | 12,192 | – | 12,192 | – |
| TOTAL OTHER LIABILITIES | 377,569 | 230,515 | 29,052 | 579,032 | 41,331 |
| **TOTAL LONG-TERM LIABILITIES** | **$ 2,455,211** | **$ 569,439** | **$ 415,991** | **$2,608,659** | **$ 124,137** |

### DISCRETE COMPONENT UNITS

Long-term liability activity for the period ended June 30, 2015 is summarized as follows:

| *(Dollars in thousands)* | Balance at June 30, 2014 | Additions/ Transfers | Reductions | Balance at June 30, 2015 | Current Portion 2015 |
|---|---|---|---|---|---|
| **VALLEY MEDICAL CENTER** | | | | | |
| LIMITED TAX GENERAL OBLIGATION BONDS | $ 243,503 | $ – | $ 6,271 | $ 237,232 | $ 6,535 |
| REVENUE BONDS | 18,858 | – | 1,376 | 17,482 | 1,650 |
| BUILD AMERICA BONDS | 61,155 | – | – | 61,155 | – |
| NOTES PAYABLE & OTHER | 1,407 | – | 513 | 894 | 291 |
| **TOTAL LONG-TERM LIABILITIES** | **$ 324,923** | **$ –** | **$ 8,160** | **$ 316,763** | **$ 8,476** |
| **NORTHWEST HOSPITAL** | | | | | |
| REVENUE BONDS | $ 73,400 | $ – | $ 73,400 | $ – | $ – |
| NOTES PAYABLE & CAPITAL LEASES | 13,645 | – | 1,175 | 12,470 | 525 |
| **TOTAL LONG-TERM LIABILITIES** | **$ 87,045** | **$ –** | **$ 74,575** | **$ 12,470** | **$ 525** |

**NOTE 10:**

## Leases

Future minimum lease payments under capital leases, and the present value of the net minimum lease payments, as of June 30, 2015, are as follows:

### CAPITAL LEASES

| **Year** *(Dollars in thousands)* | Future Payments |
|---|---|
| 2016 | $ 3,839 |
| 2017 | 3,432 |
| 2018 | 2,113 |
| 2019 | 1,627 |
| 2020 | 1,494 |
| THEREAFTER | 4,601 |
| TOTAL MINIMUM LEASE PAYMENTS | 17,106 |
| LESS: AMOUNT REPRESENTING INTEREST COSTS | 1,290 |
| **PRESENT VALUE OF MINIMUM PAYMENTS** | **$ 15,816** |

Equipment under capital leases were as follows:

| *(Dollars in thousands)* | Balance at June 30, 2014 | Additions | Retirements | Balance at June 30, 2015 |
|---|---|---|---|---|
| EQUIPMENT | $ 32,879 | $ – | $ 10,292 | $ 22,587 |
| LESS ACCUMULATED DEPRECIATION | 15,904 | 3,514 | 8,331 | 11,087 |
| **LEASED CAPITAL ASSETS, NET** | **$ 16,975** | **$ (3,514)** | **$ 1,961** | **$ 11,500** |

### OPERATING LEASES

The University has certain lease agreements in effect that are considered operating leases, which are primarily for leased building space. During the year ended June 30, 2015, the University recorded rent expense of $44,736,000 for these leases. Future lease payments under these leases as of June 30, 2015 are as follows:

| **Year** *(Dollars in Thousands)* | |
|---|---|
| 2016 | $ 49,313 |
| 2017 | 45,886 |
| 2018 | 42,293 |
| 2019 | 32,568 |
| 2020 | 28,134 |
| 2021 - 2025 | 101,240 |
| 2026 - 2030 | 30,961 |
| 2031 - 2035 | 22,228 |
| THEREAFTER | 49,304 |
| **TOTAL MINIMUM LEASE PAYMENTS** | **$ 401,927** |

**NOTE 11:**

## Bonds and Notes Payable

The bonds and notes payable at June 30, 2015 consist of state of Washington General Obligation and Refunding Bonds, University Revenue Bonds, and Notes Payable. These obligations have fixed interest rates ranging from 0.45% to 6.52%. Debt service requirements at June 30, 2015 were as follows:

**BONDS AND NOTES PAYABLE** *(Dollars in thousands)*

| | STATE OF WASHINGTON GENERAL OBLIGATION BONDS | | UNIVERSITY OF WASHINGTON REVENUE BONDS | | NOTES PAYABLE AND OTHER | |
|---|---|---|---|---|---|---|
| **Year** | **Principal** | **Interest** | **Principal** | **Interest** | **Principal** | **Interest** |
| 2016 | $ 18,290 | $ 7,208 | $ 41,055 | $ 79,896 | $ 6,566 | $ 963 |
| 2017 | 17,619 | 6,318 | 42,370 | 78,761 | 5,380 | 825 |
| 2018 | 14,300 | 5,422 | 44,685 | 77,180 | 4,193 | 673 |
| 2019 | 14,345 | 4,673 | 46,125 | 75,253 | 3,146 | 538 |
| 2020 | 10,825 | 4,044 | 47,215 | 73,228 | 3,104 | 410 |
| 2021 - 2025 | 58,550 | 11,375 | 256,270 | 330,524 | 6,707 | 613 |
| 2026 - 2030 | 15,635 | 989 | 283,415 | 264,185 | 475 | 14 |
| 2031 - 2035 | – | – | 282,915 | 194,134 | 232 | – |
| 2036 - 2040 | – | – | 366,230 | 113,945 | 192 | – |
| 2041 - THEREAFTER | – | – | 298,785 | 22,488 | – | – |
| **TOTAL PAYMENTS** | **$ 149,564** | **$ 40,029** | **$1,709,065** | **$1,309,594** | **$ 29,995** | **$ 4,036** |

State law requires that the University reimburse the state for debt service payments relating to its portion of the state of Washington General Obligation and Refunding Bonds from Medical Center patient revenues, tuition, timber sales and other revenues.

### REFUNDING ACTIVITY

On August 21, 2014, the Washington Biomedical Research Properties II refunded Lease Revenue Bonds totaling $118,915,000 with new bond issuances totaling $115,660,000 and premium of $13,263,000. The refunded bonds had coupon rates ranging from 4.40% to 5.50% with an average interest rate of 5.03%; the new bonds have an average interest rate of 4.48%. The refunding decreased the total debt service payments to be made over the next 12.2 years by $15,026,000 and resulted in a total economic gain of $12,572,000. The average life of the Lease Revenue Refunding Bonds, 2014 is 11.95 years with final maturity on June 1, 2038.

On March 4, 2015, the University issued $218,270,000 in General Revenue & Refunding Bonds, 2015 A&B, at a premium of $26,315,000. A portion of the proceeds (new par of $176,090,000 plus premium of $26,396,000) was used to refund existing debt of $190,195,000. The refunded bonds had coupon rates ranging from 4.00% to 5.00% with an average interest rate of 4.98%; the new bonds have an average coupon of 4.22% with an average interest rate of 4.40%. The refunding decreased the total debt service payments to be made over the next 14.92 years by $74,997,000 and resulted in a total economic gain of $38,083,000. The remainder of the proceeds, issued at a slight discount, was used to pay off $42,500,000 in commercial paper. The average life of the 2015 A&B General Revenue bonds is 14.82 years with final maturity on December 1, 2044.

### COMMERCIAL PAPER PROGRAM

In July 2006, the Board of Regents authorized a commercial paper program with a maximum borrowing limit of $250,000,000, payable from University general revenues. This short-term borrowing program is primarily used to fund capital expenditures. As of June 30, 2015, there was $161,545,000, in outstanding commercial paper. The University reported $111,545,000 of commercial paper in long-term debt as of June 30, 2015 and refunded this amount on September 9, 2015 with General Revenue Bonds, 2015 C&D.

During fiscal year 2015, the University issued an additional $145,545,000 and retired $42,500,000 of commercial paper debt.

### SUBSEQUENT DEBT ACTIVITY

On September 9, 2015, the University issued $195,510,000 in General Revenue Bonds, 2015 C&D, at a premium of $13,279,000. The proceeds were used to fund various projects such as renovation of Denny Hall, construction of Animal Care and Research Facilities, South West Campus Central Utility Plant, and other projects. In addition, proceeds will be used to pay off $111,545,000 in commercial paper. The 2015 C&D bonds have coupon rates ranging from 1.40% to 5.00% with an average coupon rate of 4.03%. The average life of the 2015 C&D General Revenue bonds is 15.60 years with final maturity on December 1, 2045.

On September 24, 2015, the University through Washington Biomedical Research Properties 3.2 sold $132,070,000 in Lease Revenue Bonds, Series 2015, at a premium of $10,926,000. The proceeds were used to fund the design, construction and equipping of a new biomedical research facility and pay the costs of issuance. The 2015 bonds have coupon rates ranging from 1.485% to 5.00% with an average coupon rate of 4.42%. The average life of the 2015 Lease Revenue Bonds is 15.87 years with final maturity on January 1, 2048.

On October 8, 2015, the state of Washington refunded General Obligation Bonds totaling $34,285,000 (UW portion) with new bond issuances totaling $30,145,000 and premium of $4,775,000. The refunded bonds had an average interest rate and coupon rate of 5.0%; the new bonds have an average interest rate and coupon rate of 5.0%. The refunding decreased the total debt service payments to be made over the next 10 years by $5,621,000 and resulted in a total economic gain of $5,230,000.

### DEFEASED BONDS

The University defeased certain bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. The trust account assets and the liability for the defeased bonds are not included in the University's financial statements. As of June 30, 2015, $252,973,000 of bonds outstanding are considered defeased.

**NOTE 12:**

## Operating Expenses by Function

Operating expenses by functional classification for the year ended June 30, 2015 are summarized as follows:

| **OPERATING EXPENSES** *(Dollars in thousands)* | **2015** |
|---|---|
| INSTRUCTION | $ 1,113,959 |
| RESEARCH | 729,608 |
| PUBLIC SERVICE | 35,428 |
| ACADEMIC SUPPORT | 336,747 |
| STUDENT SERVICES | 43,101 |
| INSTITUTIONAL SUPPORT | 215,105 |
| OPERATION & MAINTENANCE OF PLANT | 241,719 |
| SCHOLARSHIPS & FELLOWSHIPS | 146,570 |
| AUXILIARY ENTERPRISES | 291,628 |
| MEDICAL-RELATED | 1,203,140 |
| DEPRECIATION/AMORTIZATION | 310,960 |
| **TOTAL OPERATING EXPENSES** | **$ 4,667,965** |

### Instruction

Instruction includes expenses for all activities that are part of an institution's instruction program. Expenses for credit and noncredit courses; academic, vocational, and technical instruction; and tutorial instruction are included in this category. The University's professional and continuing education programs are also included.

### Research

The research category includes all expenses for activities specifically organized to produce research, which are funded by federal, state, and private institutions.

### Public Service

Public service includes activities conducted primarily to provide non-instructional services to individuals and groups other than the University and its students, such as community service programs, conferences, institutes and general advisory services.

The activities of the University's public radio stations, Center for Educational Leadership and clinical trials are included in this category.

### Academic Support

Academic support includes expenses incurred to provide support services for the institution's primary missions: instruction, research, and public service. The activities of the University's academic administration, libraries, museums and galleries, and information technology support for academic activities are included in this category.

### Student Services

The student services category includes the Offices of Admissions and the University Registrar. The activities of the Center for Undergraduate Advising, Diversity, and Student Success, and the operations of the Rubenstein Pharmacy in the student health center are also included in this category.

**Institutional Support**

The institutional support category includes central activities that manage long-range planning for the institution, such as planning and programming operations, legal services, fiscal operations, space management, procurement and activities concerned with community and alumni relations. The University's central administration departments and information technology support for non-academic activities are included in this category.

**Operation and Maintenance of Plant**

The operation and maintenance of plant category includes the administration, operation, maintenance, preservation, and protection of the institution's physical plant.

**Scholarships and Fellowships**

This category includes expenses for scholarships and fellowships and other financial aid not funded from existing University resources. Financial aid funded from existing University resources are considered scholarship allowances, which are reflected as an offset to tuition revenues. Expenditure of amounts received from the Washington State Need grant, Washington Higher Education grant, and Pell grants are reflected in this manner.

**Auxiliary Enterprises**

Auxiliary enterprises furnish goods or services to students, faculty, staff or the general public. These units charge a fee directly related to the cost of the goods or services. A distinguishing characteristic of an auxiliary enterprise is that it operates as a self-supporting activity. The activities of the University's Intercollegiate Athletics, Commuter Services and Housing and Food Services departments are included in this category.

**Medical-related**

The medical-related category includes all expenses associated with patient-care operations, including nursing and other professional services, general services, administrative services, and fiscal services. The activities of UWMC, UWP, and Neighborhood Clinics are included in this category (Note 1).

**Depreciation/Amortization**

Depreciation and amortization reflect a periodic expensing of the cost of capitalized assets such as buildings, equipment, software or other intangible assets, spread over their estimated useful lives.

**NOTE 13:**

## Related Parties

Harborview Medical Center (HMC), a hospital and Level I adult and pediatric trauma center located in Seattle, is a component unit of King County, Washington. It has been managed by the University under a management contract between King County and the University since 1967. The current management contract was set to expire on June 30, 2015, but to facilitate ongoing negotiations of a new agreement, the expiration date has been extended by the parties to the earlier of December 31, 2015 or the date that a new agreement is effective.

Under the contract, the HMC Board of Trustees determines major institutional policies and retains control of programs and fiscal matters, while King County retains ultimate control over capital programs and capital budgets. The University is responsible for the operations of HMC, including the provision of medical, dental and management services. All of the individuals employed at HMC, including physicians, are employees of the University. HMC expenses, including payroll, are reimbursed to the University from HMC fund sources.

HMC revenues and expenses are not recognized in the University's financial statements. The University's financial statements do, however, include accounts receivable from HMC of $25,923,000 as of June 30, 2015, as well as HMC investments of $3,467,000, current accrued liabilities of $19,363,000, and long-term liabilities of $22,626,000.

Beginning in fiscal year 2014, UW Medicine information technology began operating as a self-sustaining activity of the University (ITS department). The ITS department began recording enterprise-wide information technology capital assets that are purchased for use by UW Medicine entities. The Due To Related Party reflected in long-term liabilities (Note 9) of $22,626,000 at June 30, 2015 represents HMC's funding of the enterprise-wide information technology which will be included in the recharge rates of the ITS department over the useful life of the asset.

The University of Washington Foundation (UWF) is a nonprofit organization that performs fundraising activities on behalf of the University. The UWF is not included in the University's financial statements as a component unit because gifts and grants that are made to the UWF are immediately transferred to the University. In 2015, the UWF transferred $82,502,000, to the University in gifts and grants received on its behalf; these are included in the financial statements of the University. The remaining amounts retained by the UWF are not significant to the University's financial statements.

The University of Washington Alumni Association is a tax-exempt entity that was established to connect and celebrate alumni and to support the University's mission. The Alumni Association received $2,818,000 from the University in support of its operations in fiscal year 2015.

During fiscal year 2015, UWMC provided $3,444,000 to NWH for strategic support of operations. These amounts are presented in the Statements of Revenues, Expenses and Changes in Net Position for the University as Other Nonoperating Expense and for NWH as Other Nonoperating Revenue.

During fiscal year 2015, NWH entered into a long-term financing agreement with the University to obtain funds for the defeasance and advance refunding of Series 2007 Revenue Bonds. Under the terms of this agreement, NWH is required to maintain annual debt service coverage equal to at least 1.25 and days cash on hand equal to at least 50 days. As of June 30, 2015, $71,306,000 is payable to the University as a result of this financing agreement. The portion which is due in fiscal year 2016 is reported by NWH as Other Current Liabilities, and by the University as Other Current Assets, on the Statements of Net Position as of June 30, 2015. The remaining long-term portion is reported on the Statements of Net Position by NWH as Due to Primary Government and by the University as Due from Discrete Component Units.

In addition, as of June 30, 2015, NWH has a payable to the University of $29,402,000 for services purchased from the University during the current and prior fiscal years. Payments to the University will occur each fiscal year beginning in 2016, with the first payment of $5,000,000 made in August 2015. The portion of the payable paid subsequent to year end is reported by NWH as Other Current Liabilities, and by the University as Other Current Assets, on the Statements of Net Position as of June 30, 2015. The remaining long-term portion is reported on the Statements of Net Position by NWH as Due to Primary Government and by the University as Due from Discrete Component Units.

**NOTE 14:**

## Other Post Employment Benefits (OPEB)

Healthcare and life insurance programs for employees of the state of Washington are administered by the Washington State Health Care Authority (HCA). The HCA calculates the premium amounts each year that are sufficient to fund the statewide health and life insurance programs on a pay-as-you-go basis. These costs are passed through to individual state agencies based upon active employee headcount; the agencies pay the premiums for active employees to the HCA. The agencies may also charge employees for certain higher cost options elected by the employee.

State of Washington retirees may elect coverage through state health and life insurance plans, for which they pay less than the full cost of the benefits, based on their age and other demographic factors. The healthcare premiums for active employees, which are paid by the agency during employees' working careers, subsidize the "underpayments" of retirees.

An additional factor in the OPEB obligation is a payment that is required by the state legislature to reduce the premiums for retirees covered by Medicare (an "explicit" subsidy). This amount was $150 dollars per retiree eligible for parts A and B of Medicare for calendar year 2015. This is also passed through to state agencies through active employee rates charged to the agency.

There is no formal state or University plan that underlies the subsidy of retiree health and life insurance.

### ACTUARIAL STUDY

Actuarial studies, performed every two years by the Washington Office of the State Actuary, calculated that the total OPEB obligation of the state of Washington at January 1, 2015 and 2013 was $5.3 billion and $3.7 billion, respectively. The annual required contribution was $498 million and $342 million for the state of Washington for 2015 and 2013, respectively. The actuary calculated the OPEB obligation based on individual state employee data, including age, retirement eligibility and length of service. The probability of an employee of a given age and length of service retiring and receiving OPEB benefits is based on statewide historical data.

The actuary's allocation of the cumulative statewide liability related to the University and HMC (an unconsolidated related party), was estimated at approximately $997 million and $671 million for 2015 and 2013, respectively. These amounts are not included in the University's financial statements.

The University paid $248 million for healthcare expenses in fiscal year 2015, which included its pay-as-you-go portion of the OPEB liability, calculated by the actuary at $7.9 million in fiscal year 2015.

The State Actuary's report is available at: osa.leg.wa.gov/Actuarial_Services/OPEB/OPEB.htm

**NOTE 15:**

## Pension Plans

The University offers four contributory pension plans: the Washington State Public Employees' Retirement System (PERS) plan, the Washington State Teachers' Retirement System (TRS) plan, and the Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) plan, cost sharing multiple-employer defined benefit pension plans administered by the State of Washington Department of Retirement Systems, and the University of Washington Retirement Plan (UWRP), a defined contribution plan. The University of Washington Supplemental Retirement Plan, a defined benefit pension plan which operates in tandem with the UWRP, is closed to new participants.

### PLAN DESCRIPTIONS

**Public Employees' Retirement System** (PERS) was established in 1947 and its retirement benefit provisions are contained in chapters 41.34 and 41.40 of the Revised Code of Washington (RCW). PERS is a cost-sharing multiple-employer retirement system comprised of three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined benefit plans, and PERS Plan 3 is a defined benefit plan with a defined contribution component. PERS members include higher education employees not participating in other higher education retirement programs.

PERS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3 and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

**Teachers' Retirement System** (TRS) was established in 1938 and its retirement benefit provisions are contained in chapters 41.32 and 41.34 of the RCW. TRS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: TRS Plan 1 and TRS Plan 2 are defined benefit plans, and TRS Plan 3 is a defined benefit plan with a defined contribution component. TRS eligibility for membership requires service as a certificated public school employee working in an instructional, administrative or supervisory capacity.

TRS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3 and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

**Law Enforcement Officers' and Fire Fighters' Retirement System** (LEOFF) was established in 1970 and its retirement benefit provisions are contained in chapter 41.26 of the RCW. LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate pension plans for both membership and accounting purposes. The University participates in LEOFF Plan 2, which is a defined benefit plan. LEOFF membership includes full-time, fully compensated, local law enforcement commissioned officers, firefighters, and as of July 24, 2005, emergency medical technicians.

### FIDUCIARY NET POSITIONS

The pension plans' fiduciary net positions have been determined on the same basis used by the pension plans. Washington State Department of Retirement Systems (DRS) financial statements have been prepared in conformity with generally accepted accounting principles (GAAP). The retirement plans are accounted for in pension trust funds using the flow of economic resources measurement focus and the accrual basis of accounting. Plan member contributions are recognized as revenues in the period in which the contributions are earned. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

The Washington State Investment Board (WSIB) has been authorized by statute (chapter 43.33A of the RCW) as having the investment management responsibility for the pension funds. Investments are reported at fair value, and unrealized gains and losses are included as investment income in the Statement of Changes in Fiduciary Net Position presented in the DRS Comprehensive Annual Financial Report. Purchases and sales of investments are recorded on a trade-date basis.

DRS publishes an annual report for retirement plans which is available at: http://www.drs.wa.gov/administration/annual-report/

### ACTUARIAL ASSUMPTIONS

The total pension liability for each plan was determined by an actuarial valuation as of June 30, 2013, with the results rolled forward to June 30, 2014. The following actuarial assumptions have been applied to all prior periods included in the measurement:

| | |
|---|---|
| **INFLATION** | 3.0% TOTAL ECONOMIC INFLATION, 3.75% SALARY INFLATION |
| **SALARY INCREASE** | EXPECTED TO GROW BY PROMOTIONS AND LONGEVITY IN ADDITION TO SALARY INFLATION ASSUMPTION |
| **INVESTMENT RATE OF RETURN** | 7.50% |

Mortality rates were based on the RP-2000 Combined Healthy Table and Combined Disabled Table published by the Society of Actuaries. The Washington State Office of the State Actuary (OSA) applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100% Scale BB. Mortality rates are applied on a generational basis, meaning members are assumed to receive additional mortality improvements in each future year, throughout their lifetime.

The actuarial assumptions used in the June 30, 2013 valuation were based on the results of OSA's 2007-2012 Experience Study. Additional assumptions for subsequent events and law changes are current as of the 2013 actuarial valuation report.

### DISCOUNT RATE

The discount rate used to measure the total pension liabilities was 7.50% for all plans in which the University participates. To determine the discount rate, an asset sufficiency test was completed to test whether each pension plan's fiduciary net position was sufficient to make all projected future benefit payments of current plan members. Consistent with current law, the completed asset sufficiency tests for PERS and TRS included an assumed 7.70% long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. LEOFF 2 included an assumed 7.50% long-term discount rate to determine the associated funding liabilities.

Consistent with the long-term expected rate of return, a 7.50% future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue to be made at contractually required rates (including the component of PERS 2/3 and TRS 2/3 employer rates pertaining to the unfunded actuarial accrued liability for PERS 1 and TRS 1, respectively, as provided for in chapter 41.45 of the RCW).

Based on those assumptions, the fiduciary net position for each pension plan was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.50% on pension plan investments was applied to determine the total pension liability.

### SENSITIVITY OF THE NET PENSION LIABILITY (ASSET) TO CHANGES IN THE DISCOUNT RATE

The following table presents the University's net pension liability calculated using the discount rate of 7.50%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50%) or 1-percentage-point higher (8.50%) than the current rate.

**DISCOUNT RATE SENSITIVITY – NET PENSION LIABILITY (ASSET)** *(Dollars in thousands)*

| Plan | 1% Decrease | Current Discount Rate | 1% Increase |
|---|---|---|---|
| PERS 1 | $514,278 | $417,231 | $333,926 |
| PERS 2/3 | $843,524 | $202,225 | ($287,608) |
| TRS 1 | $ 3,707 | $ 2,881 | $ 2,172 |
| TRS 2/3 | $ 2,191 | $ 252 | ($1,189) |
| LEOFF 2 | $ 1,217 | ($2,844) | ($5,891) |

### LONG-TERM EXPECTED RATE OF RETURN

The long-term expected rate of return of 7.50% on pension plan investments was determined by the WSIB. The rate approximately equals the median of the simulated investment returns over a fifty-year time horizon, increased slightly to remove WSIB's implicit, small, short-term downward adjustment due to assumed mean reversion. WSIB's implicit short-term adjustment, while small and appropriate over a 10- to 15-year period, becomes amplified over a 50-year measurement period.

The long-term expected rate of return was determined by the WSIB using a building-block method in which a best-estimate of expected future rates of return (expected returns, net of pension plan investment expense, but including inflation) are developed for each major asset class by the WSIB. Those expected returns make up one component of WSIB's Capital Market Assumptions (CMAs).

The CMAs contain three pieces of information for each class of assets the WSIB currently invest in:

- Expected annual return
- Standard deviation of the annual return
- Correlations between the annual returns of each asset class with every other asset class

WSIB uses the CMAs and their target asset allocation to simulate future investment returns over various time horizons.

Best estimates of arithmetic real rates of return for each major asset class included in the target asset allocation for each pension plan, as of June 30, 2014, are summarized in the following table:

| Asset Class | Target Allocation | % Long-term Expected Real Rate of Return Arithmetic |
|---|---|---|
| FIXED INCOME | 20.00% | 0.80% |
| TANGIBLE ASSETS | 5.00% | 4.10% |
| REAL ESTATE | 15.00% | 5.30% |
| GLOBAL EQUITY | 37.00% | 6.05% |
| PRIVATE EQUITY | 23.00% | 9.05% |

The inflation component used to create the above table is 2.70%, and represents WSIB's most recent long-term estimate of broad economic inflation.

### EMPLOYER CONTRIBUTION RATES

Employer contribution rates are developed in accordance with chapter 41.45 of the RCW by the OSA, and include an administrative expense component that is currently set at 0.18%. The statute provides authority to the Pension Funding Council to adopt changes to economic assumptions and contribution rates.

### UNIVERSITY PROPORTIONATE SHARE

Collective pension amounts are determined as of a measurement date, which can be no earlier than an employer's prior fiscal year. The measurement date for the net pension liabilities recorded by the University as of June 30, 2015 was June 30, 2014. University contributions received and processed by DRS during the fiscal year ended June 30, 2014 have been used as the basis for determining the University's proportionate share of the collective pension amounts reported by DRS in their June 30, 2014 Schedules of Employer and Nonemployer Allocations for all plans in which the University participates.

| Plan | Proportionate Share for Year ended June 30, 2015 |
|---|---|
| PERS 1 | 8.28% |
| PERS 2/3 | 10.00% |
| TRS 1 | 0.10% |
| TRS 2/3 | 0.08% |
| LEOFF 2 | 0.21% |

### UNIVERSITY AGGREGATED BALANCES

The University's aggregated balances of net pension liabilities, net pension assets, and deferrals as of June 30, 2015 are presented in the table below.

**JUNE 30, 2015** *(Dollars in thousands)*

| | Net Pension Liability | Net Pension Asset | Deferred Outflows | Deferred Inflows |
|---|---|---|---|---|
| PERS 1 | $ 417,231 | $ – | $ 38,503 | $ 52,172 |
| PERS 2/3 | 202,225 | – | 45,896 | 214,360 |
| TRS 1 | 2,881 | – | 286 | 505 |
| TRS 2/3 | 252 | – | 618 | 578 |
| LEOFF 2 | – | 2,844 | 299 | 1,520 |
| **TOTAL** | **$ 622,589** | **$ 2,844** | **$ 85,602** | **$ 269,135** |

## PERS Plan 1

PERS Plan 1 is closed to new entrants.

### VESTING

PERS Plan 1 members were vested after the completion of five years of eligible service.

### BENEFITS PROVIDED

PERS Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service.

Members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### CONTRIBUTIONS

The PERS Plan 1 employer contribution rate for the fiscal year ended June 30, 2015 was 9.21%. The University's contributions to PERS Plan 1 for the year ended June 30, 2015 were $38,503,000.

### PROPORTIONATE SHARE OF PERS 1 PENSION EXPENSE AND DEFERRALS RELATED TO PENSIONS

The University's proportionate share of PERS Plan 1 pension expense for the fiscal year ended June 30, 2015 was $23,023,000, and is reported on the Statement of Revenues, Expenses and Changes in Net Position in benefits expense.

The University's deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 1 as of June 30, 2015 are presented in the following table:

| **Description** *(Dollars in thousands)* | **Deferred Outflows of Resources** | **Deferred Inflows of Resources** |
|---|---|---|
| DIFFERENCE BETWEEN PROJECTED AND ACTUAL EARNINGS ON PLAN INVESTMENTS, NET | $ – | $ 52,172 |
| UNIVERSITY CONTRIBUTIONS SUBSEQUENT TO THE MEASUREMENT DATE OF THE COLLECTIVE NET PENSION LIABILITY | 38,503 | – |
| **TOTAL** | $ 38,503 | $ 52,172 |

Deferred outflows of resources related to University contributions subsequent to the measurement date of $38,503,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred inflows of resources pertaining to PERS Plan 1 will be recognized in pension expense as follows:

| **Year** *(Dollars in thousands)* | |
|---|---|
| 2016 | $ (13,043) |
| 2017 | (13,043) |
| 2018 | (13,043) |
| 2019 | (13,043) |
| 2020 | – |
| THEREAFTER | – |
| **TOTAL** | **$ (52,172)** |

## PERS Plan 2/3

### VESTING

PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service, or after five years of service if 12 months of that service are earned after age 44.

### BENEFITS PROVIDED

PERS Plan 2/3 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's AFC times the member's years of service for Plan 2, and one percent of AFC times the member's years of service for Plan 3.

The AFC is the monthly average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at age 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age, for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 2, 2013:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost- of-living allowance (based on the Consumer Price Index) capped at three percent annually, and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### CONTRIBUTIONS

The PERS Plan 2/3 employer contribution rate for the fiscal year ended June 30, 2015 was 9.21%. The Plan 2/3 employer rate includes a component to address the PERS Plan 1 unfunded actuarial accrued liability. The University's contributions to PERS Plan 2/3 for the year ended June 30, 2015 were $45,486,000 as determined by rates established in accordance with RCW 41.45.

### PROPORTIONATE SHARE OF PERS 2/3 PENSION EXPENSE AND DEFERRALS RELATED TO PENSIONS

The University's proportionate share of PERS Plan 2/3 pension expense for the fiscal year ended June 30, 2015 was $32,567,000, and is reported on the Statement of Revenues, Expenses and Changes in Net Position in benefits expense.

The University's deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 as of June 30, 2015 are presented in the following table:

| **Description** *(Dollars in thousands)* | **Deferred Outflows of Resources** | **Deferred Inflows of Resources** |
|---|---|---|
| DIFFERENCE BETWEEN PROJECTED AND ACTUAL EARNINGS ON PLAN INVESTMENTS, NET | $ – | $ 214,360 |
| CHANGE IN UNIVERSITY'S PROPORTIONATE SHARE | 410 | – |
| UNIVERSITY CONTRIBUTIONS SUBSEQUENT TO THE MEASUREMENT DATE OF THE COLLECTIVE NET PENSION LIABILITY | 45,486 | – |
| **TOTAL** | **$ 45,896** | **$ 214,360** |

Deferred outflows of resources related to University contributions subsequent to the measurement date of $45,486,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 will be recognized in pension expense as follows:

| **Year** *(Dollars in thousands)* | |
|---|---|
| 2016 | $ (53,473) |
| 2017 | (53,473) |
| 2018 | (53,473) |
| 2019 | (53,531) |
| 2020 | – |
| THEREAFTER | – |
| **TOTAL** | **$ (213,950)** |

## TRS Plan 1

TRS Plan 1 is closed to new entrants.

### VESTING

TRS Plan 1 members were vested after the completion of five years of eligible service.

### BENEFITS PROVIDED

TRS Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's AFC, for each year of service credit, up to a maximum of 60 percent, divided by twelve.

The AFC is the average of the member's earnable compensation for the two consecutive highest-paid fiscal years. Members are eligible for retirement at any age after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. Other benefits include temporary and permanent disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### CONTRIBUTIONS

The TRS Plan 1 employer contribution rate for the fiscal year ended June 30, 2015 was 10.39%. The University's contributions to TRS Plan 1 for the year ended June 30, 2015 were $286,000.

### PROPORTIONATE SHARE OF TRS PLAN 1 PENSION EXPENSE AND DEFERRALS RELATED TO PENSIONS

The University's proportionate share of TRS Plan 1 pension expense for the fiscal year ended June 30, 2015 was $1,052,000, and is reported on the Statement of Revenues, Expenses and Changes in Net Position in benefits expense.

The University's deferred outflows of resources and deferred inflows of resources pertaining to TRS Plan 1 as of June 30, 2015 are presented in the following table:

| **Description** *(Dollars in thousands)* | **Deferred Outflows of Resources** | **Deferred Inflows of Resources** |
|---|---|---|
| DIFFERENCE BETWEEN PROJECTED AND ACTUAL EARNINGS ON PLAN INVESTMENTS, NET | $ – | $ 505 |
| UNIVERSITY CONTRIBUTIONS SUBSEQUENT TO THE MEASUREMENT DATE OF THE COLLECTIVE NET PENSION LIABILITY | 286 | – |
| **TOTAL** | **$ 286** | **$ 505** |

Deferred outflows of resources related to University contributions subsequent to the measurement date of $286,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred inflows of resources pertaining to TRS Plan 1 will be recognized in pension expense as follows:

| **Year** *(Dollars in thousands)* | |
|---|---|
| 2016 | $ (126) |
| 2017 | (126) |
| 2018 | (126) |
| 2019 | (127) |
| 2020 | – |
| THEREAFTER | – |
| **TOTAL** | **$ (505)** |

## TRS Plan 2/3

### VESTING

TRS Plan 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service, or after five years of service if 12 months of that service are earned after age 44.

### BENEFITS PROVIDED

TRS Plan 2/3 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's AFC times the member's years of service for Plan 2, and one percent of AFC for Plan 3.

The AFC is the monthly average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at age 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. TRS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age, for each year before age 65. TRS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 1, 2013:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

TRS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service. TRS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other TRS Plan 2/3 benefits include duty and non-duty disability payments, a cost- of-living allowance (based on the Consumer Price Index) capped at three percent annually, and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### CONTRIBUTIONS

The TRS Plan 2/3 employer contribution rate for the fiscal year ended June 30, 2015 was 10.39%. The Plan 2/3 employer rate includes a component to address the TRS Plan 1 unfunded actuarial accrued liability. The University's contributions to TRS Plan 2/3 for the year ended June 30, 2015 were $307,000.

### PROPORTIONATE SHARE OF TRS 2/3 PENSION EXPENSE AND DEFERRALS RELATED TO PENSIONS

The University's proportionate share of TRS Plan 2/3 pension expense for the fiscal year ended June 30, 2015 was $237,000, and is reported on the Statement of Revenues, Expenses and Changes in Net Position in benefits expense.

The University's deferred outflows of resources and deferred inflows of resources pertaining to TRS Plan 2/3 as of June 30, 2015 are presented in the following table:

| **Description** *(Dollars in thousands)* | **Deferred Outflows of Resources** | **Deferred Inflows of Resources** |
|---|---|---|
| DIFFERENCE BETWEEN PROJECTED AND ACTUAL EARNINGS ON PLAN INVESTMENTS, NET | $ – | $ 578 |
| CHANGE IN UNIVERSITY'S PROPORTIONATE SHARE | 311 | – |
| UNIVERSITY CONTRIBUTIONS SUBSEQUENT TO THE MEASUREMENT DATE OF THE COLLECTIVE NET PENSION LIABILITY | 307 | – |
| **TOTAL** | **$ 618** | **$ 578** |

Deferred outflows of resources related to University contributions subsequent to the measurement date of $307,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources pertaining to TRS Plan 2/3 will be recognized in pension expense as follows:

| **Year** *(Dollars in thousands)* | |
|---|---|
| 2016 | $ (77) |
| 2017 | (77) |
| 2018 | (77) |
| 2019 | (77) |
| 2020 | 41 |
| THEREAFTER | – |
| **TOTAL** | **$ (267)** |

## LEOFF Plan 2

### VESTING

LEOFF Plan 2 members are vested after completing five years of eligible service.

### BENEFITS PROVIDED

LEOFF Plan 2 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the final average salary (FAS) per year of service (the FAS is based on the highest consecutive 60 months). Members are eligible for retirement with a full benefit at age 53 with at least five years of service credit. Members who retire prior to the age of 53 receive reduced benefits. If the member has at least 20 years of service and is age 50, the reduction is three percent for each year prior to age 53. Otherwise, the benefits are actuarially reduced for each year prior to age 53. LEOFF plan 2 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the Consumer Price Index), capped at three percent annually, and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### CONTRIBUTIONS

The LEOFF Plan 2 employer contribution rate for the fiscal year ended June 30, 2015 was 8.59%. The University's contributions to LEOFF Plan 2 for the year ended June 30, 2015 were $299,000.

### PROPORTIONATE SHARE OF LEOFF 2 PENSION EXPENSE AND DEFERRALS RELATED TO PENSIONS

The University's proportionate share of LEOFF Plan 2 pension expense for the fiscal year ended June 30, 2015 was ($144,000), and is reported on the Statement of Revenues, Expenses and Changes in Net Position in benefits expense.

The University's deferred outflows of resources and deferred inflows of resources pertaining to LEOFF Plan 2 as of June 30, 2015 are presented in the following table:

| **Description** *(Dollars in thousands)* | **Deferred Outflows of Resources** | **Deferred Inflows of Resources** |
|---|---|---|
| DIFFERENCE BETWEEN PROJECTED AND ACTUAL EARNINGS ON PLAN INVESTMENTS, NET | $ – | $ 1,505 |
| CHANGE IN UNIVERSITY'S PROPORTIONATE SHARE | – | 15 |
| UNIVERSITY CONTRIBUTIONS SUBSEQUENT TO THE MEASUREMENT DATE OF THE COLLECTIVE NET PENSION LIABILITY | 299 | – |
| **TOTAL** | **$ 299** | **$ 1,520** |

Deferred outflows of resources related to University contributions subsequent to the measurement date of $299,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred inflows of resources pertaining to LEOFF Plan 2 will be recognized in pension expense as follows:

| **Year** *(Dollars in thousands)* | |
|---|---|
| 2016 | $ (379) |
| 2017 | (379) |
| 2018 | (379) |
| 2019 | (379) |
| 2020 | (3) |
| THEREAFTER | (1) |
| **TOTAL** | **$ (1,520)** |

## University of Washington Retirement Plan (403(B))

Faculty, librarians and professional staff are eligible to participate in the University of Washington Retirement Plan, a 403(b) defined-contribution plan administered by the University.

### 403(B) PLAN DESCRIPTION

Contributions to the plan are invested by participants in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations. Benefits from the plan are available upon separation or retirement at the member's option. RCW 28B.10.400 et. seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

The number of participants in the 403 (b) plan for the year ended June 30, 2015 was 15,415.

### 403(B) FUNDING POLICY

Employee contribution rates, based on age, are 5%, 7.5% or 10% of salary. The University matches the contributions of employees. Within parameters established by the legislature, contribution requirements may be established or amended by the University of Washington Board of Regents. Employee and employer contributions for the year ended June 30, 2015 were $105,266,000.

## University Of Washington Supplemental Retirement Plan (401(A))

The University of Washington Supplemental Retirement Plan (UWSRP), a 401(a) defined-benefit retirement plan, operates in tandem with the 403(b) plan to supplement the expected defined contribution retirement savings accumulated under the UWRP. The UWSRP was closed to new participants effective March 1, 2011.

The Unfunded Actuarial Accrued Liability (UAL) and Annual Required Contribution (ARC) as of July 1 of the respective years were:

| *(Dollars in thousands)* | **2015** | **2013** |
|---|---|---|
| UAL | $ 373,711 | $ 292,535 |
| | | |
| NORMAL COST | $ 14,250 | $ 9,529 |
| AMORTIZATION OF UAL, INCLUDING INTEREST | 38,807 | 29,021 |
| **ARC** | **$ 53,057** | **$ 38,550** |

| **Actuarial Assumptions** *(Dollars in thousands)* | **2015** | **2013** |
|---|---|---|
| PAYROLL COVERED BY PLAN | $ 1,050,000 | $ 1,047,000 |
| RATE OF RETURN ASSUMPTION | 4.00% | 4.25% |
| SALARY INCREASES FOR YEARS 1 AND 2 | 3.75% | 3.00% |
| SALARY INCREASE FOR THIRD YEAR | 3.75% | 3.00% |
| SALARY INCREASES THEREAFTER | 3.75% | 3.00% |

The UAL and ARC were established using the entry age normal cost method.

The following table reflects the activity in the UWSRP Net Pension Obligation for the years ended June 30, 2015 and 2014:

| *(Dollars in thousands)* | **2015** | **2014** |
|---|---|---|
| BALANCE AT BEGINNING OF FISCAL YEAR | $ 198,895 | $ 163,372 |
| ARC | 53,057 | 38,550 |
| PAYMENTS TO BENEFICIARIES | (3,766) | (3,027) |
| **BALANCE AT END OF FISCAL YEAR** | **$ 248,186** | **$ 198,895** |

### 401(A) PLAN DESCRIPTION

This plan provides for a supplemental payment component, which guarantees a minimum retirement benefit based upon a one-time calculation at each eligible participant's retirement date. The University makes direct payments to qualifying retirees when the retirement benefits provided by the 403(b) plan do not meet the benefit goals.

### 401(A) PLAN FUNDING

The University received an actuarial valuation of the UWSRP with a valuation date of July 1, 2015. The previous evaluations were performed in 2013 and 2011. The University has set aside $188,881,000 as of June 30, 2015, for this liability. These funds do not meet the GASB technical definition of “Plan Assets” since they have not been segregated and restricted in a trust or equivalent arrangement. The UAL shown in the table above, therefore, does not reflect a credit for these amounts.

### NOTE 16:

## Commitments and Contingencies

Authorized expenditures for construction projects unexpended as of June 30, 2015 was $157,034,000. These expenditures will be funded from local funds, debt proceeds and state appropriations.

The University receives and expends substantial amounts under federal and state grants, contracts and programs. This funding is used for research, student aid, Medical Center operations and other programs, and is subject to audit by governmental granting agencies. Certain grant and contract costs billed to the federal government are subject to audit under OMB Circular A-133, “Audits of States, Local Governments, and Non-Profit Organizations.” The University is also involved in various other claims and legal actions arising in the ordinary course of business. University management believes that any liabilities arising from these matters will not have a material effect on the University’s financial statements.

The University is exposed to risk of loss related to tort liability, injuries to employees and loss of property. The University purchases insurance protection for workers’ compensation as well as marine, aviation and certain other risks. The University also purchases insurance protection for loss of property at self-sustaining units, bond-financed buildings and where otherwise required by contract; otherwise, the risk of property loss is retained, unfunded. For medical professional, general, employment practices and automobile liability, the University maintains a program of self-insurance reserves and excess insurance coverage. The self-insurance reserve represents the estimated ultimate cost of settling claims resulting from events that have occurred on or before the Statement of Net Position date. The reserve includes the undiscounted amounts that will be required for future payments of claims that have been reported, and claims related to events that have occurred but have not yet been reported.

The self-insurance reserve is estimated through an actuarial calculation and included in Long-Term Liabilities. Changes in the self-insurance reserve for the year ended June 30, 2015 are noted below:

| *(Dollars in thousands)* | **2015** |
|---|---|
| RESERVE AT BEGINNING OF FISCAL YEAR | $ 67,450 |
| INCURRED CLAIMS AND CHANGES IN ESTIMATES | 29,495 |
| CLAIM PAYMENTS | (14,744) |
| **RESERVE AT END OF FISCAL YEAR** | **$ 82,201** |

**NOTE 17:**

## Blended Component Units

Condensed combining statements for the University and its blended component units are shown below:

| *(Dollars in thousands)* **Statements of Net Position – June 30, 2015** | **Combined Entities** | **Eliminations** | **University of Washington** | **Total Blended Component Units** | **Medical Entities** | **Real Estate Entities** |
|---|---|---|---|---|---|---|
| ASSETS | | | | | | |
| CURRENT ASSETS: | | | | | | |
| TOTAL CURRENT ASSETS | $ 1,402,322 | $ (22,327) | $ 1,355,339 | $ 69,310 | $ 66,437 | $ 2,873 |
| NONCURRENT ASSETS: | | | | | | |
| TOTAL OTHER ASSETS | 4,786,897 | – | 4,675,492 | 111,405 | 86,557 | 24,848 |
| CAPITAL ASSETS, NET | 4,172,378 | – | 3,878,199 | 294,179 | 15,251 | 278,928 |
| TOTAL ASSETS | 10,361,597 | (22,327) | 9,909,030 | 474,894 | 168,245 | 306,649 |
| DEFERRED OUTFLOWS OF RESOURCES | 111,415 | – | 111,415 | – | – | – |
| **TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES** | **$10,473,012** | **$ (22,327)** | **$10,020,445** | **$ 474,894** | **$ 168,245** | **$ 306,649** |
| LIABILITIES | | | | | | |
| TOTAL CURRENT LIABILITIES | $ 998,318 | $ (31,313) | $ 932,905 | $ 96,726 | $ 66,701 | $ 30,025 |
| TOTAL NONCURRENT LIABILITIES | 3,159,096 | – | 2,864,897 | 294,199 | – | 294,199 |
| TOTAL LIABILITIES | 4,157,414 | (31,313) | 3,797,802 | 390,925 | 66,701 | 324,224 |
| DEFERRED INFLOWS OF RESOURCES | 269,135 | – | 269,135 | – | – | – |
| **TOTAL LIABILITIES AND DEFERRED INFLOWS OF RESOURCES** | 4,426,549 | (31,313) | 4,066,937 | 390,925 | 66,701 | 324,224 |
| NET POSITION | | | | | | |
| NET INVESTMENT IN CAPITAL ASSETS | 2,156,229 | – | 2,155,933 | 296 | 15,251 | (14,955) |
| RESTRICTED: | | | | | | |
| NONEXPENDABLE | 1,321,979 | – | 1,321,979 | – | – | – |
| EXPENDABLE | 1,699,135 | – | 1,699,135 | – | – | – |
| UNRESTRICTED | 869,120 | 8,986 | 776,461 | 83,673 | 86,293 | (2,620) |
| **TOTAL NET POSITION** | 6,046,463 | 8,986 | 5,953,508 | 83,969 | 101,544 | (17,575) |
| **TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION** | **$10,473,012** | **$ (22,327)** | **$10,020,445** | **$ 474,894** | **$ 168,245** | **$ 306,649** |

| *(Dollars in thousands)* **Statements of Revenues, Expenses and Changes in Net Position – Year ended June 30, 2015** | **Combined Entities** | **Eliminations** | **University of Washington** | **Total Blended Component Units** | **Medical Entities** | **Real Estate Entities** |
|---|---|---|---|---|---|---|
| **REVENUES** | | | | | | |
| OPERATING REVENUES: | | | | | | |
| STUDENT TUITION AND FEES | $ 914,419 | $ – | $ 914,419 | $ – | $ – | $ – |
| NET PATIENT SERVICE REVENUES | 1,362,279 | (8,913) | 1,151,404 | 219,788 | 219,788 | – |
| GRANT REVENUE | 1,280,658 | – | 1,280,658 | – | – | – |
| OTHER OPERATING REVENUE | 659,342 | (25,677) | 647,790 | 37,229 | 299 | 36,930 |
| **TOTAL OPERATING REVENUE** | **4,216,698** | **(34,590)** | **3,994,271** | **257,017** | **220,087** | **36,930** |
| **EXPENSES** | | | | | | |
| OPERATING EXPENSES: | | | | | | |
| OTHER OPERATING EXPENSES | 4,357,005 | (33,911) | 4,126,060 | 264,856 | 251,450 | 13,406 |
| DEPRECIATION / AMORTIZATION | 310,960 | – | 293,441 | 17,519 | 1,666 | 15,853 |
| **TOTAL OPERATING EXPENSES** | **4,667,965** | **(33,911)** | **4,419,501** | **282,375** | **253,116** | **29,259** |
| **OPERATING INCOME (LOSS)** | **(451,267)** | **(679)** | **(425,230)** | **(25,358)** | **(33,029)** | **7,671** |
| **NONOPERATING REVENUES (EXPENSES)** | | | | | | |
| STATE APPROPRIATIONS | 255,156 | – | 255,156 | – | – | – |
| GIFTS | 115,636 | – | 115,636 | – | – | – |
| INVESTMENT INCOME | 227,404 | – | 231,471 | (4,067) | (4,067) | – |
| OTHER NONOPERATING REVENUES (EXPENSES) | (21,746) | 394 | (34,144) | 12,004 | 31,674 | (19,670) |
| **NET NONOPERATING REVENUES (EXPENSES)** | **576,450** | **394** | **568,119** | **7,937** | **27,607** | **(19,670)** |
| **INCOME (LOSS) BEFORE OTHER REVENUES** | **125,183** | **(285)** | **142,889** | **(17,421)** | **(5,422)** | **(11,999)** |
| CAPITAL APPROPRIATIONS, GRANTS, GIFTS AND OTHER | 42,798 | – | 42,798 | – | – | – |
| GIFTS TO PERMANENT ENDOWMENTS | 67,359 | – | 67,359 | – | – | – |
| **TOTAL OTHER REVENUES** | **110,157** | **–** | **110,157** | **–** | **–** | **–** |
| **INCREASE (DECREASE) IN NET POSITION** | **235,340** | **(285)** | **253,046** | **(17,421)** | **(5,422)** | **(11,999)** |
| **NET POSITION** | | | | | | |
| **NET POSITION – BEGINNING OF YEAR** | 5,811,123 | 9,271 | 5,700,462 | 101,390 | 106,966 | (5,576) |
| **NET POSITION – END OF YEAR** | **$ 6,046,463** | **$ 8,986** | **$ 5,953,508** | **$ 83,969** | **$ 101,544** | **$ (17,575)** |

| *(Dollars in thousands)* **Statements of Cash Flows – Year ended June 30, 2015** | **Combined Entities** | **Eliminations** | **University of Washington** | **Total Blended Component Units** | **Medical Entities** | **Real Estate Entities** |
|---|---|---|---|---|---|---|
| **NET CASH PROVIDED (USED) BY:** | | | | | | |
| OPERATING ACTIVITIES | $ (116,356) | $ (9,728) | $ (93,223) | $ (13,405) | $ (18,746) | $ 5,341 |
| NONCAPITAL FINANCING ACTIVITIES | 412,979 | – | 389,898 | 23,081 | 23,081 | – |
| CAPITAL AND RELATED FINANCING ACTIVITIES | (420,195) | – | (412,579) | (7,616) | (1,612) | (6,004) |
| INVESTING ACTIVITIES | 127,349 | – | 129,076 | (1,727) | (1,727) | – |
| **NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS** | **3,777** | **(9,728)** | **13,172** | **333** | **996** | **(663)** |
| CASH AND CASH EQUIVALENTS – BEGINNING OF THE YEAR | 79,128 | – | 60,401 | 18,727 | 17,038 | 1,689 |
| **CASH AND CASH EQUIVALENTS – END OF THE YEAR** | **$ 82,905** | **$ (9,728)** | **$ 73,573** | **$ 19,060** | **$ 18,034** | **$ 1,026** |

## NOTE 18:

# Discrete Component Units

Condensed combining statements for the University's discrete component units are shown below:

| *(Dollars in thousands)*<br>**Statements of Net Position** | **June 30, 2015**<br>**Total Discrete Component Units** | **Northwest Hospital** | **Valley Medical Center** |
|---|---|---|---|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | | |
| CURRENT ASSETS: | | | |
| TOTAL CURRENT ASSETS | $ 238,178 | $ 78,426 | $ 159,752 |
| NONCURRENT ASSETS: | | | |
| TOTAL OTHER ASSETS | 176,921 | 48,895 | 128,026 |
| CAPITAL ASSETS, NET | 467,701 | 117,735 | 349,966 |
| TOTAL ASSETS AND DEFERRED OUTFLOWS | 6,435 | 6,435 | – |
| **TOTAL ASSETS AND DEFERRED OUTFLOWS** | **$ 889,235** | **$ 251,491** | **$ 637,744** |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | |
| TOTAL CURRENT LIABILITIES | $ 141,904 | $ 52,083 | $ 89,821 |
| TOTAL NONCURRENT LIABILITIES | 413,472 | 105,185 | 308,287 |
| TOTAL DEFERRED INFLOWS OF RESOURCES | 9,625 | – | 9,625 |
| **TOTAL LIABILITIES AND DEFERRED INFLOWS OF RESOURCES** | **565,001** | **157,268** | **407,733** |
| NET POSITION | | | |
| NET INVESTMENT IN CAPITAL ASSETS | 67,033 | 33,864 | 33,169 |
| RESTRICTED: | | | |
| NONEXPENDABLE | 1,943 | 1,943 | – |
| EXPENDABLE | 8,471 | 459 | 8,012 |
| UNRESTRICTED | 246,787 | 57,957 | 188,830 |
| **TOTAL NET POSITION** | 324,234 | 94,223 | 230,011 |
| **TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION** | **$ 889,235** | **$ 251,491** | **$ 637,744** |

| *(Dollars in thousands)*<br>**Statements of Revenues, Expenses and Changes in Net Position** | **Year Ended June 30, 2015**<br>**Total Discrete Component Units** | **Northwest Hospital** | **Valley Medical Center** |
|---|---|---|---|
| REVENUES | | | |
| OPERATING REVENUES: | | | |
| NET PATIENT SERVICE REVENUES | $ 822,421 | $ 341,405 | $ 481,016 |
| OTHER OPERATING REVENUE | 53,165 | 15,649 | 37,516 |
| **TOTAL OPERATING REVENUE** | **875,586** | **357,054** | **518,532** |
| EXPENSES | | | |
| OPERATING EXPENSES: | | | |
| OTHER OPERATING EXPENSES | 816,563 | 352,124 | 464,439 |
| DEPRECIATION / AMORTIZATION | 49,238 | 18,027 | 31,211 |
| **TOTAL OPERATING EXPENSES** | **865,801** | **370,151** | **495,650** |
| **OPERATING INCOME (LOSS)** | **9,785** | **(13,097)** | **22,882** |
| NONOPERATING REVENUES (EXPENSES) | | | |
| PROPERTY TAX REVENUE | 18,132 | – | 18,132 |
| INVESTMENT INCOME | 4,385 | 981 | 3,404 |
| OTHER NONOPERATING EXPENSES | (22,032) | 6,769 | (28,801) |
| **NET NONOPERATING REVENUES (EXPENSES)** | **485** | **7,750** | **(7,265)** |
| **INCOME (LOSS) BEFORE OTHER REVENUES** | **10,270** | **(5,347)** | **15,617** |
| CAPITAL GRANTS, GIFTS AND OTHER | 169 | 169 | – |
| **INCREASE (DECREASE) IN NET POSITION** | **10,439** | **(5,178)** | **15,617** |
| NET POSITION | | | |
| NET POSITION – BEGINNING OF YEAR | 313,795 | 99,401 | 214,394 |
| **NET POSITION – END OF YEAR** | **$ 324,234** | **$ 94,223** | **$ 230,011** |

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# SCHEDULES OF REQUIRED SUPPLEMENTARY INFORMATION

### Schedule of Proportionate Share of the Net Pension Liability

**PERS 1**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| UNIVERSITY'S PROPORTION OF THE NET PENSION LIABILITY | | 8.28% |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY | $ | 417,231 |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 25,376 |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 1644.20% |
| PLAN FIDUCIARY NET POSITION AS A PERCENTAGE OF THE TOTAL PENSION LIABILITY | | 61.19% |

### Schedule of Contributions

**PERS 1**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 2,311 |
| CONTRIBUTIONS IN RELATION TO THE CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 2,313 |
| CONTRIBUTION DEFICIENCY (EXCESS) | $ | (2) |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 25,376 |
| CONTRIBUTIONS AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 9.11% |

### Schedule of Proportionate Share of the Net Pension Liability

**PERS 2/3**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| UNIVERSITY'S PROPORTION OF THE NET PENSION LIABILITY | | 10.00% |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY | $ | 202,225 |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 856,839 |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY AS A PERCENTAGE OF ITS COVERED-EMPLOYEE PAYROLL | | 23.60% |
| PLAN FIDUCIARY NET POSITION AS A PERCENTAGE OF THE TOTAL PENSION LIABILITY | | 93.29% |

### Schedule of Contributions

**PERS 2/3**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 78,164 |
| CONTRIBUTIONS IN RELATION TO THE CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 78,160 |
| CONTRIBUTION DEFICIENCY (EXCESS) | $ | 4 |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 856,839 |
| CONTRIBUTIONS AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 9.12% |

### Schedule of Proportionate Share of the Net Pension Liability

**TRS 1**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| UNIVERSITY'S PROPORTION OF THE NET PENSION LIABILITY | | 0.10% |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY | $ | 2,881 |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 514 |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY AS A PERCENTAGE OF ITS COVERED-EMPLOYEE PAYROLL | | 560.51% |
| PLAN FIDUCIARY NET POSITION AS A PERCENTAGE OF THE TOTAL PENSION LIABILITY | | 68.77% |

### Schedule of Contributions

**TRS 1**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 51 |
| CONTRIBUTIONS IN RELATION TO THE CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 51 |
| CONTRIBUTION DEFICIENCY (EXCESS) | $ | – |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 514 |
| CONTRIBUTIONS AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 9.92% |

### Schedule of Proportionate Share of the Net Pension Liability

**TRS 2/3**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| UNIVERSITY'S PROPORTION OF THE NET PENSION LIABILITY | | 0.08% |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY | $ | 252 |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 3,391 |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 7.43% |
| PLAN FIDUCIARY NET POSITION AS A PERCENTAGE OF THE TOTAL PENSION LIABILITY | | 96.81% |

### Schedule of Contributions

**TRS 2/3**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 341 |
| CONTRIBUTIONS IN RELATION TO THE CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 343 |
| CONTRIBUTION DEFICIENCY (EXCESS) | $ | (2) |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 3,391 |
| CONTRIBUTIONS AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 10.06% |

### Schedule of Proportionate Share of the Net Pension Liability (Asset)

**LEOFF 2**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| UNIVERSITY'S PROPORTION OF THE NET PENSION LIABILITY (ASSET) | | 0.21% |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY (ASSET) | $ | (2,844) |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 3,581 |
| UNIVERSITY'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY (ASSET) AS A PERCENTAGE OF ITS COVERED-EMPLOYEE PAYROLL | | (79.42%) |
| PLAN FIDUCIARY NET POSITION AS A PERCENTAGE OF THE TOTAL PENSION LIABILITY | | 116.75% |

### Schedule of Contributions

**LEOFF 2**

| *(Dollars in thousands)* | | **2015** |
|---|---|---|
| CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 308 |
| CONTRIBUTIONS IN RELATION TO THE CONTRACTUALLY REQUIRED CONTRIBUTION | $ | 308 |
| CONTRIBUTION DEFICIENCY (EXCESS) | $ | – |
| UNIVERSITY'S COVERED-EMPLOYEE PAYROLL | $ | 3,581 |
| CONTRIBUTIONS AS A PERCENTAGE OF COVERED-EMPLOYEE PAYROLL | | 8.60% |

## NOTES TO REQUIRED SUPPLEMENTARY INFORMATION FOR THE YEAR ENDED JUNE 30, 2015

**Changes of benefit terms.**
Amounts reported in 2015 reflect no change in benefit terms.

**Changes of assumptions.**
Amounts reported in 2015 reflect no changes in assumptions.

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For more information, contact Financial Accounting at 206.221.7845 or accountg@uw.edu

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UNIVERSITY *of*
WASHINGTON

# SUPPLEMENTAL BONDHOLDER INFORMATION

## STUDENTS & ENROLLMENT

| | AUTUMN QUARTER | | | | |
|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 |
| **UNDERGRADUATE** | | | | | |
| Freshmen | | | | | |
| Applied | 27,469 | 29,723 | 33,857 | 35,382 | 41,257 |
| Accepted | 16,527 | 18,152 | 19,560 | 20,510 | 23,183 |
| Percent Accepted to Applied | 60% | 61% | 58% | 58% | 56% |
| Enrolled | 6,546 | 6,931 | 7,233 | 7,429 | 7,819 |
| Percent Enrolled to Accepted | 40% | 38% | 37% | 36% | 34% |
| Transfers | | | | | |
| Applied | 8,277 | 8,415 | 8,809 | 9,480 | 9,819 |
| Accepted | 4,250 | 4,448 | 4,705 | 4,826 | 4,747 |
| Pecent Accepted to Applied | 51% | 53% | 53% | 51% | 3,123 |
| Enrolled | 3,046 | 3,084 | 3,252 | 3,308 | 3,123 |
| Percent Enrolled to Accepted | 72% | 69% | 69% | 69% | 66% |
| Total Undergraduate FTE | | | | | |
| Bothell | 2,934 | 3,327 | 3,794 | 4,101 | 4,402 |
| Seattle | 28,118 | 28,011 | 28,597 | 29,359 | 29,888 |
| Tacoma | 2,775 | 3,064 | 3,346 | 3,565 | 3,685 |
| Total All Campuses | 33,827 | 34,402 | 35,737 | 37,025 | 37,975 |
| Totals Undergraduate Headcount | | | | | |
| Bothell | 3,254 | 3,648 | 4,106 | 4,406 | 4,698 |
| Seattle | 29,822 | 29,771 | 30,148 | 31,099 | 31,525 |
| Tacoma | 3,116 | 3,366 | 3,641 | 3,826 | 3,940 |
| Total All Campuses | 36,192 | 36,785 | 37,895 | 39,331 | 40,163 |
| Additional Enrollment Statistics | | | | | |
| Percent Non-resident Students (1) | 32% | 30% | 30% | 31% | 32% |
| Percent Retention (Freshman to Sophomore) | 92% | 91% | 91% | 92% | 92% |
| Mean GPA | 3.70 | 3.69 | 3.69 | 3.69 | 3.70 |
| Median GPA | 3.77 | 3.76 | 3.77 | 3.76 | 3.78 |
| Percent of class reporting GPA data | 100% | 100% | 100% | 100% | 100% |
| Mean Combined SAT scores | 1193 | 1198 | 1200 | 1200 | 1210 |
| Median Combined SAT scores | 1210 | 1210 | 1220 | 1210 | 1230 |
| Percent of class reporting SAT data | 86% | 86% | 87% | 84% | 81% |
| Median Combined SAT scores | 1210 | 1210 | 1220 | 1210 | 1230 |
| Percent of class reporting SAT data | 86% | 86% | 87% | 84% | 81% |
| **GRADUATE** | | | | | |
| Applied | 24,692 | 26,350 | 27,381 | 29,851 | 32,248 |
| Accepted | 7,493 | 8,106 | 8,980 | 9,106 | 9,693 |
| Percent Accepted to Applied | 30% | 31% | 33% | 31% | 30% |
| Enrolled | 3,720 | 3,643 | 4,383 | 4,389 | 4,717 |
| Percent Enrolled to Accepted | 50% | 45% | 49% | 48% | 49% |
| Graduate FTE | 12,820 | 13,048 | 13,557 | 13,751 | 14,154 |
| Graduate Headcount | 12,574 | 12,782 | 13,177 | 13,333 | 13,595 |

(1) Includes Graduate and Undergraduate Students.

Unless otherwise noted all figures include Seattle, Tacoma, and Bothell campuses.

## STUDENTS & ENROLLMENT CONTINUED

| | AUTUMN QUARTER | | | | |
|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 |
| **PROFESSIONAL** | | | | | |
| **Law** | | | | | |
| Applied | 2,656 | 2,930 | 2,624 | 2,946 | 2,877 |
| Accepted | 586 | 638 | 686 | 776 | 775 |
| Enrolled | 182 | 176 | 143 | 163 | 170 |
| Law Headcount | 520 | 527 | 508 | 493 | 474 |
| **Pharmacy** | | | | | |
| Applied | 354 | 411 | 413 | 390 | 399 |
| Accepted | 108 | 123 | 131 | 121 | 131 |
| Enrolled | 94 | 99 | 96 | 90 | 92 |
| Pharmacy Headcount | 350 | 361 | 372 | 374 | 378 |
| **Dentistry** | | | | | |
| Applied | 996 | 1,085 | 1,058 | 1,046 | 1,022 |
| Accepted | 80 | 83 | 82 | 85 | 94 |
| Enrolled | 63 | 62 | 63 | 63 | 63 |
| Dental Headcount | 258 | 260 | 262 | 262 | 260 |
| **Medicine** | | | | | |
| Applied | 4,962 | 5,101 | 6,015 | 6,129 | 8,090 |
| Accepted | 285 | 272 | 296 | 287 | 291 |
| Enrolled | 219 | 220 | 235 | 240 | 245 |
| Medicine Headcount | 851 | 851 | 858 | 877 | 897 |
| Total Professional FTE | 3,932 | 3,949 | 4,086 | 4,081 | 3,834 |
| Total Professional Headcount | 1,979 | 1,999 | 2,000 | 2,006 | 2,009 |
| **Tuition and Fees (full academic year)** | | | | | |
| Undergraduate Resident (1) | $ 10,574 | $ 12,383 | $ 12,397 | $ 12,394 | $ 11,839 (2) |
| Undergraduate Non-Resident | $ 28,058 | $ 29,938 | $ 31,971 | $ 33,513 | $ 34,143 |
| Graduate Resident | $ 13,438 | $ 14,698 | $ 15,666 | $ 16,683 | $ 16,665 |
| Graduate Non-Resident | $ 26,308 | $ 27,318 | $ 28,119 | $ 28,926 | $ 28,909 |
| Business Masters Resident | $ 26,338 | $ 27,608 | $ 28,950 | $ 30,339 | $ 31,200 |
| Business Masters Non-Resident | $ 38,408 | $ 40,158 | $ 42,126 | $ 44,175 | $ 45,450 |
| Law Resident | $ 26,608 | $ 29,948 | $ 31,983 | $ 31,980 | $ 31,962 |
| Law Non-Resident | $ 40,678 | $ 42,918 | $ 45,024 | $ 45,021 | $ 44,124 |
| Pharmacy Resident | $ 20,778 | $ 24,018 | $ 26,325 | $ 26,496 | $ 28,362 |
| Pharmacy Non-Resident | $ 37,878 | $ 43,688 | $ 47,964 | $ 49,215 | $ 50,286 |
| Medical Resident | $ 25,548 | $ 28,268 | $ 30,186 | $ 32,220 | $ 33,759 |
| Medical Non-Resident | $ 54,528 | $ 57,198 | $ 59,175 | $ 61,206 | $ 64,194 |
| Dentistry Resident | $ 27,388 | $ 32,948 | $ 36,150 | $ 39,654 | $ 43,494 |
| Dentistry Non-Resident | $ 50,298 | $ 53,018 | $ 56,667 | $ 60,555 | $ 66,483 |
| **University FTE** | | | | | |
| Undergraduate | 33,827 | 34,402 | 35,737 | 37,025 | 37,975 |
| Graduate | 12,820 | 13,048 | 13,557 | 13,751 | 14,154 |
| Professional | 3,932 | 3,949 | 4,086 | 4,081 | 3,834 |
| Total University FTE | 50,579 | 51,399 | 53,380 | 54,857 | 55,963 |
| **University Headcount** | | | | | |
| Undergraduate | 36,192 | 36,785 | 37,895 | 39,331 | 40,163 |
| Graduate | 12,574 | 12,782 | 13,177 | 13,333 | 13,595 |
| Professional | 1,979 | 1,999 | 2,000 | 2,006 | 2,009 |
| Total University Headcount | 50,745 | 51,566 | 53,072 | 54,670 | 55,767 |

(1) Includes Undergraduates and Graduate Students.
(2) Reflects the impact of legislative action.

Unless otherwise noted all figures include Seattle, Tacoma, and Bothell campuses.

## FACULTY & OTHER DATA

| | AUTUMN QUARTER | | | | |
|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 |
| **FACULTY DATA** | | | | | |
| Number of faculty [1] | 4,280 | 4,356 | 4,497 | 4,561 | 4,703 |
| Tenure rate (%) | 39% | 39% | 37% | 37% | 36% |
| Percent holding terminal degree (Ph.D., MD, DDS) | 93% | 93% | 92% | 93% | 93% |
| **HOUSING AND DINING** | | | | | |
| Room and Board [2] | $ 7,785 | $ 8,091 | $ 9,360 | $ 10,055 | $ 10,576 |
| Autumn Opening Occupancy | 5,677 | 5,294 | 6,403 | 6,607 | 7,010 |
| Occupancy [3] | 116% | 114% | 111% | 114% | 112% |

(1) Faculty headcount reflects core faculty comprised of professorial, instructional, and research categories. Headcount associated with temporary faculty categories is excluded.

(2) Room and board pricing is for the full academic year. Starting Autumn 2013, room portion of annual room and board pricing is the weighted average of all Residence Hall double rooms in inventory, and dining amount is for a representative meal plan.

(3) Numbers reflect as-built capacity and 10th day occupancy (occupancy that exceeds 100% is the result of housing three students in a room designed for two).

# MEDICAL CENTERS [1]

| | FISCAL YEARS ($000) | | | | |
|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | 2014 | 2015 |
| **UWMC, NORTHWEST AND VALLEY FINANCIAL INFORMATION [2]** | | | | | |
| **UWMC** | | | | | |
| Operating Revenue | $ 847,861 | $ 877,548 | $ 920,705 | $ 967,651 | $ 1,083,584 |
| Net Income | $ 59,891 | $ 36,026 | $ 5,798 | $ 14,096 | $ 26,745 |
| **Northwest** | | | | | |
| Operating Revenue | $ 275,839 | $ 300,089 | $ 327,807 | $ 324,342 | $ 357,054 |
| Net Income | $ (8,390) | $ (2,700) | $ 9,284 | $ (4,755) | $ (5,283) |
| **Valley [3]** | | | | | |
| Operating Revenue | $ N/A | $ 436,407 | $ 451,012 | $ 474,195 | $ 518,532 |
| Net Income | $ N/A | $ (5,899) | $ (16,385) [4] | $ 6,149 | $ 15,617 |
| **Combined** | | | | | |
| Operating Revenue | $1,123,700 | $1,614,044 | $1,699,524 | $1,766,188 | $ 1,958,783 |
| Net Income | $ 51,501 | $ 27,427 | $ 2,047 | $ 15,490 | $ 37,676 |
| **UWMC, NORTHWEST AND VALLEY PATIENT ACTIVITY STATISTICS** | | | | | |
| **UWMC** | | | | | |
| Admissions | 18,919 | 17,915 | 17,728 | 18,033 | 18,092 |
| Outpatient Visits | 306,825 | 300,487 | 284,870 | 291,375 | 302,038 |
| Emergency Visits | 24,119 | 23,487 | 22,977 | 25,338 | 26,465 |
| **Northwest** | | | | | |
| Admissions | 9,576 | 9,127 | 9,974 | 9,211 | 9,934 |
| Outpatient Visits | 161,297 | 193,992 | 195,978 | 193,387 | 195,031 |
| Emergency Visits | 35,146 | 33,832 | 33,942 | 34,276 | 36,159 |
| **Valley [3]** | | | | | |
| Admissions | N/A | 16,842 | 17,477 | 16,693 | 17,174 |
| Outpatient Visits | N/A | 344,947 | 362,274 | 403,169 | 471,780 |
| Emergency Visits | N/A | 75,586 | 74,202 | 73,763 | 81,250 |
| **Combined** | | | | | |
| Admissions | 28,495 | 43,884 | 45,179 | 43,937 | 45,200 |
| Outpatient Visits | 468,122 | 839,426 | 843,122 | 887,931 | 968,849 |
| Emergency Visits | 59,265 | 132,905 | 131,121 | 133,377 | 143,874 |
| **MEDICARE/MEDICAID PAYMENT** | | | | | |
| **Percent of Total Clinical Revenue [5]** | N/A | 36% | 37% | 38% | 40% |

(1) Medical Centers include University of Washington Medical Center (UWMC), Northwest Hospital and Medical Center (Northwest) and Valley Medical Center (Valley).
(2) Only UWMC revenues are included in General Revenues for the University.
(3) Valley affiliated with the University in 2011.
(4) Updated to reflect reclassification in a subsequent audit.
(5) Percent of total clinical revenue. Medicare and Medicaid payments as a percentage of total clinical revenue. Includes Northwest and Valley. Data not available for 2011.

# ENDOWMENT AND OTHER RESOURCES

| PORTFOLIO | FISCAL YEARS FY 2011 | FY 2012 | FY 2013 | FY 2014 | FY 2015 |
|---|---|---|---|---|---|
| **Endowment Market Value ($000)** | | | | | |
| True | 1,354,585 | 1,339,251 | 1,493,747 | 1,708,921 | 1,778,207 |
| Term | 35,231 | 33,513 | 36,202 | 56,776 | 41,135 |
| Quasi | 785,477 | 738,570 | 816,744 | 1,067,056 | 1,256,884 |
| **Total** | **2,175,293** | **2,111,334** | **2,346,693** | **2,832,753** | **3,076,226** |
| **Portfolio Breakdown** | | | | | |
| **Equity** | **79.0%** | **81.0%** | **84.0%** | **86.0%** | **84.0%** |
| Domestic | 13.0% | 17.0% | 19.0% | 19.0% | 18.0% |
| International | 29.0% | 28.0% | 32.0% | 36.0% | 37.0% |
| Venture Capital | 5.0% | 6.0% | 5.0% | 4.0% | 4.0% |
| Private Equity | 12.0% | 13.0% | 11.0% | 7.0% | 7.0% |
| Absolute Return | 20.0% | 17.0% | 17.0% | 20.0% | 18.0% |
| **Real Assets** | **7.0%** | **8.0%** | **7.0%** | **7.0%** | **6.0%** |
| **Fixed Income** | **5.0%** | **9.0%** | **8.0%** | **7.0%** | **10.0%** |
| Domestic | 5.0% | 9.0% | 8.0% | 7.0% | 10.0% |
| International | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| **Cash** | **9.0%** | **2.0%** | **1.0%** | **0.0%** | **0.0%** |
| **Total** | **100.0%** | **100.0%** | **100.0%** | **100.0%** | **100.0%** |
| RETURN & SPENDING | | | | | |
| **Annualized Rates of Return (1)** | | | | | |
| One | 16.0% | -0.9% | 13.5% | 15.8% | 6.8% |
| Three | -0.1% | 9.0% | 9.3% | 9.2% | 11.9% |
| Five | 4.7% | 0.2% | 2.3% | 11.2% | 10.0% |
| **Endowment Return & Spending (2)** | | | | | |
| Annual Return on Endowment ($000) | 301,068 | (17,822) | 284,736 | 379,837 | 201,493 |
| Amount of Annual Return Spent ($000) | 95,391 | 106,381 | 109,365 | 117,222 | 105,274 |
| Actual Annual Spending Rate | 5.21% | 4.94% | 5.18% | 5.00% | 4.65% |
| EXTERNALLY MANAGED FUNDS | | | | | |
| Annuity and Life Income Funds | 69,878 | 66,514 | 70,863 | 86,212 | 83,043 |
| Externally Managed Endowments | 51,806 | 49,099 | 49,755 | 111,831 | 111,442 |

## INVESTMENT POLICY CHANGE

Subsequent to June 30, 2015 the UW Board of Regents approved the creation of the University of Washington Investment Management Company (UWINCO), an internal investment management company. This results in the advisory committee becoming an advisory board (UWINCO Board).

(1) Net of manager fees.
(2) Under the spending policy distributions to endowed programs are 4% of the average market value of the CEF for the previous five years. There is an additional 1% administrative fee bringing the total annual distribution to 5%.

# OPERATING FUNDS

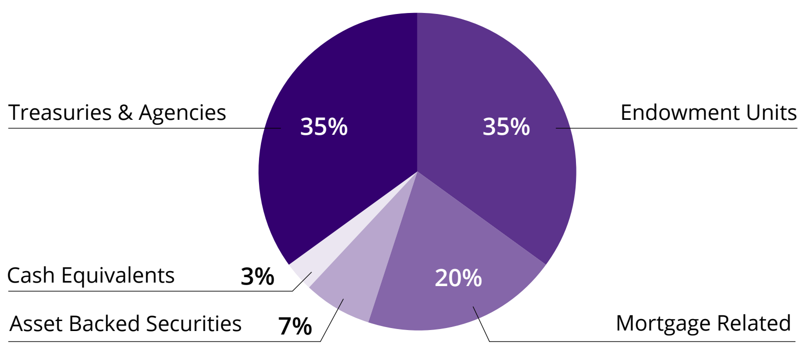
### ALLOCATION BY POOL

For the quarter ending June 30, 2015
(in millions)

| | Fund Allocation | | | Range | Duration in Years: Actual | Duration in Years: Maximum |
|---|---|---|---|---|---|---|
| Cash Pool | $ | 679 | 28% | 10% – 40% | 0.7 | 3 |
| Liquidity Pool | $ | 847 | 34% | 25% – 60% | 2.6 | 5 |
| Diversified Investment Pool (1) | $ | 806 | 33% | 15% – 45% | n/a | n/a |
| **Invested Funds excluding Capital Assets Pool** | **$** | **2,333** | **95%** | n/a | n/a | n/a |
| Capital Assets Pool (2) | $ | 127 | 5% | 0% – 15% | n/a | n/a |
| **Total Operating Funds** | **$** | **2,460** | **100%** | n/a | n/a | n/a |

### OPERATING FUNDS – MIX OF INVESTMENTS

(Excluding the Capital Assets Pool)
For the quarter ending June 30, 2015




(1) Diversified Investment Pool consists of units in the University's endowment, which are included in the endowment's market value.
(2) Capital Assets Pool is used to pay for University capital projects, and therefore consists of University capital assets.

Note: Numbers may not sum due to rounding.

## FUTURE DEBT SERVICE

*as of 6/30/15*

| | FISCAL YEAR ($000) | | | | | |
|---|---|---|---|---|---|---|
| | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 - 2048 |
| TOTAL GENERAL REVENUE DEBT SERVICE | | | | | | |
| **State General Obligation Bonds** | 25,498 | 23,938 | 19,722 | 19,018 | 14,869 | 86,549 |
| **State Certificates of Participation** | 3,413 | 3,421 | 3,189 | 3,045 | 2,875 | 4,839 |
| **Revenue Bonds** | | | | | | |
| General Revenue Bonds (1) | 120,951 | 121,131 | 121,865 | 121,378 | 120,443 | 2,412,892 |
| Lease Revenue Bonds (2) | 26,888 | 26,796 | 26,720 | 25,635 | 24,752 | 342,013 |
| Subtotal | 147,839 | 147,927 | 148,585 | 147,014 | 145,195 | 2,754,905 |
| **Interest on Commercial Paper (3)** | 23 | – | – | – | – | – |
| **Equipment Leases & Other** | 11,369 | 9,637 | 6,980 | 5,312 | 5,007 | 12,834 |
| **Total General Revenue Debt Service** | 188,142 | 184,924 | 178,476 | 174,389 | 167,946 | 2,859,127 |
| AFFILIATED ENTITIES | | | | | | |
| **Northwest Hospital Revenue Bonds** | – | – | – | – | – | – |
| **Valley Medical Center Revenue Bonds (4)** | 25,477 | 25,477 | 25,470 | 26,462 | 23,743 | 454,961 |
| **Equipment & Other** | 1,094 | 4,668 | 709 | 709 | 709 | 8,564 |
| **Total Affiliated Entities** | 26,571 | 30,145 | 26,178 | 27,171 | 24,452 | 463,524 |
| **Total Debt Service All Obligations (5)** | 270,512 | 269,224 | 254,286 | 249,258 | 234,893 | 3,756,052 |

(1) General Revenue Bonds Series 2007, 2008, 2009, 2009B, 2010A&B, 2011, 2012A, B & C, 2013 and 2015A&B.
(2) Series 2010B WBRP, 2013 WEDFA, and 2014 WEDFA.
(3) Reflects interest to be paid on outstanding commercial paper through 1/19/2016.
(4) Does not include Limited Tax General Obligation Bonds payable by property tax revenues.

Note: Numbers may not sum due to rounding.

# OFFICIAL STATEMENT DISCLOSURES

| OS DISCLOSURE OBLIGATIONS | LOCATION IN BONDHOLDERS REPORT |
|---|---|
| The audited financial statements of the University for the prior fiscal year, prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board. | Tab 2 (UW Financial Report) |
| The amount of University revenue and other debt outstanding in that fiscal year. | Tab 2 (UW Financial Report - Note 9) |
| Student enrollment information for that fiscal year, of the type provided in the table entitled “Student and Enrollment” under the heading “UNIVERSITY OF WASHINGTON—Admissions, Student Enrollment and Faculty Information” and distribution of undergraduate enrollment among University campuses. | Tab 3 (Supplemental Bondholder Information) |
| Information regarding the number of faculty, tenure rate and percent holding terminal degrees for that fiscal year, of the type provided in the table entitled “FACULTY DATA” under the heading “UNIVERSITY OF WASHINGTON—Admissions, Student Enrollment and Faculty Information.” | Tab 3 (Supplemental Bondholder Information) |
| Information regarding room and board fees, autumn opening occupancy and occupancy for that fiscal year, of the type provided in the table entitled “HOUSING AND DINING DATA” under the heading “UNIVERSITY OF WASHINGTON—Admissions, Student Enrollment and Faculty Information.” | Tab 3 (Supplemental Bondholder Information) |
| General Revenues and General Revenue components for that fiscal year, of the type provided in the table entitled “GENERAL REVENUES” under the heading “UNIVERSITY OF WASHINGTON—General Revenues.” | Tab 4 (General Revenues) |
| Grant and contract revenues for that fiscal year, and amount or percentage of grant and contract revenues from federal sources. | Tab 2 (UW Financial Report - SRECNP) |
| Information regarding the amount or percentage of revenues from Medicare or Medicaid payments in that fiscal year. | Tab 3 (Supplemental Bondholder Information) |
| Expenditures of State capital and operating appropriations to the University for such fiscal year, of the type provided in the table entitled “Expenditures of State Appropriations to the University by Type” under the heading “UNIVERSITY OF WASHINGTON—Other University Financial Information—State Funding.” | Tab 2 (UW Financial Report - SRECNP) |
| UWMC, Northwest and Valley financial information and patient activity statistics for such fiscal year, generally of the type provided in the tables under the heading “UW Medicine.” | Tab 3 (Supplemental Bondholder Information) |
| Value of investments, including operating fund investments (currently referred to as “Invested Funds”) and the Consolidated Endowment Fund (“CEF”), for that fiscal year. | Tab 3 (Supplemental Bondholder Information) |
| A narrative description of any material changes to the University’s investment policy or CEF distribution policy during the preceding fiscal year. | Tab 3 (Supplemental Bondholder Information) |
| Gift revenue for that fiscal year. | Tab 2 (UW Financial Report - SRECNP) |
| University revenue by source for that fiscal year, of the type provided in the table “University Total Revenue by Source, for Fiscal Year 2014” under the heading “UNIVERSITY OF WASHINGTON—Other University Financial Information—University Total Revenue by Source, Fiscal Year 2014.” | Tab 2 (UW Financial Report - MD&A) |
| Total University expenditures and percentages of expenditures by category for that fiscal year, of the type presented under the heading “UNIVERSITY OF WASHINGTON—Other University Financial Information—University Expenditures.” | Tab 2 (UW Financial Report - MD&A) |
| University total net assets and unrestricted net assets, of the type presented under the heading “UNIVERSITY OF WASHINGTON—Other University Financial Information—University Net Assets.” | Tab 2 (UW Financial Report - SNA) |
| A description of any material changes to the University’s obligations with respect to its pension plans, of the type presented under the heading “OTHER UNIVERSITY INFORMATION—Pension Plans.” | Tab 2 (UW Financial Report - Note 16) |
| A description of any material changes to the University’s obligations with respect to other post-employment benefits, of the type presented under the heading “OTHER UNIVERSITY INFORMATION—Other Post-Employment Retirement Benefits (“OPEB”).” | Tab 2 (UW Financial Report - Note 15) |
| Amount of the University’s self-insurance reserve, of the type presented under the heading “OTHER UNIVERSITY INFORMATION—Risk Management.” | Tab 2 (UW Financial Report - Note 17) |

# SUPPLEMENTAL FINANCIAL REPORTS

**UNIVERSITY OF WASHINGTON**

Supplementary Information

June 30, 2015

(With Independent Auditors’ Report Thereon)

KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

# Independent Auditors' Report on Supplementary Information

The Board of Regents
University of Washington:

We have audited the financial statements of the business-type activities of the University of Washington, an agency of the state of Washington, as of and for the year ended June 30, 2015, and have issued our report thereon dated October 23, 2015, which contained an unmodified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. We have not performed any procedures with respect to the audited financial statements subsequent to October 23, 2015.

The supplementary information included on pages 2 through 4 is presented for the purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

This report is intended solely for the information and use of the Board of Regents and management of the University of Washington and rating agencies and bondholders who have previously received the financial statements of the University of Washington as of and for the year ended June 30, 2015, and our unmodified opinion thereon, for use in evaluating those financial statements, and is not intended to be, and should not be used for any other purpose.

KPMG LLP

November 25, 2015

**UNIVERSITY OF WASHINGTON**

Reconciliation of Total University Revenue to General Revenue

Year ended June 30, 2015

(Dollars in thousands)

| | | 2015 |
|---|---|---|
| General revenue: | | |
| Total revenue | $ | 4,982,564 |
| Less: | | |
| State appropriations | | 255,156 |
| Grant and contract direct costs | | 1,082,452 |
| Gifts | | 115,636 |
| Revenues of component units | | 211,174 |
| Student activities fees and U-Pass fees | | 44,080 |
| Student technology fees, student building fees, and student loan funds | | 76,297 |
| Trust and endowment income, net unrealized gains on noninvested funds investments, Metropolitan Tract net operating income, component unit investment income, and other restricted investment income | | 187,599 |
| Capital appropriations | | 20,812 |
| Capital grants, gifts and other | | 21,986 |
| Other nonoperating revenues | | 9,042 |
| Gifts to permanent endowments | | 67,359 |
| Total general revenue | $ | 2,890,971 |
| General revenue components: | | |
| Student tuition and fees (less student activities fees, U-Pass fees, technology fees, building fees, and loan funds) | $ | 804,391 |
| Grant and contract indirect costs | | 246,677 |
| Invested funds distribution and net invested funds unrealized gains and losses (note 2) | | 39,805 |
| Sales and services of educational departments | | 223,494 |
| Auxiliary systems and patient services | | 1,505,444 |
| Other operating revenues | | 71,160 |
| Total general revenue | $ | 2,890,971 |

See accompanying notes to supplementary information.

**UNIVERSITY OF WASHINGTON**

Reconciliation of Total University of Washington Unrestricted Net Position
to General Net Position

June 30, 2015

(Dollars in thousands)

| | | 2015 |
|---|---|---|
| Total University unrestricted net position per financial statements | $ | 869,120 |
| Less: | | |
| Student and activities fees | | 21,655 |
| Net position (deficit) of component units: | | |
| Association of University Physicians | | 84,987 |
| UW Neighborhood Clinics | | 10,276 |
| Real estate entities | | (2,620) |
| Total to be excluded | | 114,298 |
| General net position | $ | 754,822 |

See accompanying notes to supplementary information.

# UNIVERSITY OF WASHINGTON

Notes to Supplementary Information

June 30, 2015

## (1) Basis of Presentation

The General Revenue schedule presents the general income of the University of Washington (University) that is not restricted in its use by law, regulation, or contract. General Revenues, as defined in the bond agreements, are revenues pledged to bondholders under the University's General Revenue Bond platform. The supplementary information included herein reconciles total University revenue to General Revenue pledged to bondholders. For example, the following items are restricted and, therefore, excluded from General Revenues:

a) Appropriations to the University by the state of Washington (state) from the state's General Fund;

b) Revenues from gifts or grants restricted by the terms of the gift or grant either in writing or otherwise by the donor;

c) Fees imposed upon students as a condition of enrollment at the University, including but not limited to services and activities fees, building fees, and technology fees; and

d) Revenues and receipts attributable to the Metropolitan Tract Revenue, which are appropriated to the University by the state.

Unrestricted fund balances, to the extent that they were accumulated from money that was received as General Revenues, also are included and available to pay obligations secured by General Revenues. Any interest subsidy received from the federal government with respect to General Revenue Bonds is included and available to pay obligations secured by General Revenues.

## (2) Invested Funds Distributions and Net Invested Funds Unrealized Gains and Losses

These amounts represent the net interest, dividends, and realized gains or losses earned on the Invested Funds that are distributed to departments for operations, in addition to or offset by any unrealized gains and losses on the portfolio.

## (3) University Adoption of Governmental Accounting Standards Board (GASB) Statement No. 68

On July 1, 2014, the University adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. GASB Statement No. 68 requires governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, which is measured as the total pension liability less the amount of the pension plan's fiduciary net position. Implementation of GASB Statement No. 68 resulted in the restatement of fiscal year 2015 beginning unrestricted net position, reducing it by $831,426,000. GASB Statement No. 68 is not able to be applied to the prior fiscal year due to the constraints of available information.

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**
(A Department of University of Washington)

Financial Statements

June 30, 2015

(With Independent Auditors' Report Thereon)

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**
(A Department of University of Washington)

## Table of Contents

**KPMG LLP**
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

# Independent Auditors' Report

The Board of Regents
University of Washington:

We have audited the accompanying financial statements of the University of Washington Housing and Food Services, a Department of the University of Washington, which comprise the statement of net position as of June 30, 2015, and the related statements of revenue, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

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

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

## *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our 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 financial statements are free from material misstatement.

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

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

As discussed in note 1 to the financial statements, the financial statements of the University of Washington Housing and Food Services, an auxiliary enterprise within the University of Washington (the University), are intended to present the financial position, the changes in financial position and cash flows of only the respective portion of the business-type activities of the University that is attributable to the transactions of the University of Washington Housing and Food Services. They do not purport to, and do not, present fairly the financial position of the University as of June 30, 2015, the changes in its financial position or its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

KPMG

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington Housing and Food Services as of June 30, 2015, and the results of its operations and its cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.

***Other Matters***

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 9, and the schedules of required supplementary information on pages 34 and 35, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Emphasis of Matter***

As discussed in note 1 to the financial statements, on July 1, 2014, the University of Washington Housing and Food Services adopted new accounting guidance requiring governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, as well as recognizing most changes in the net pension liability within pension expense. Our opinion is not modified with respect to this matter.

KPMG LLP

Seattle, Washington
November 9, 2015

## Discussion and Analysis Prepared by Management

The following discussion and analysis provides an overview of the financial position and activities of the University of Washington Housing and Food Services (HFS) as of and for the years ended June 30, 2015 and 2014. This discussion has been prepared by HFS management and should be read in conjunction with the financial statements and accompanying notes, which follow this section.

## Overview of the Financial Statements

The financial statements of HFS include the statement of net position; the statement of revenue, expenses, and changes in net position; the statement of cash flows; and notes to financial statements. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities.

The statement of net position presents the financial condition of HFS at the end of the last fiscal year and reports all assets, deferred outflows of resources, liabilities, and deferred inflows of resources. A summarized comparison of HFS's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position is as follows as of June 30, 2015 and 2014:

### *Statement of Net Position*

| | 2015 | 2014 | Percentage change |
|---|---|---|---|
| Assets: | | | |
| Current assets | $ 72,063,586 | 61,174,943 | 17.8% |
| Noncurrent assets | 448,333,392 | 377,232,789 | 18.8 |
| Total assets | 520,396,978 | 438,407,732 | 18.7 |
| Deferred outflows | 1,265,667 | — | 100.0 |
| Total assets and deferred outflows | $ 521,662,645 | 438,407,732 | 19.0 |
| Liabilities: | | | |
| Current liabilities | $ 30,666,617 | 25,111,478 | 22.1 |
| Noncurrent liabilities | 480,221,949 | 400,924,272 | 19.8 |
| Total liabilities | 510,888,566 | 426,035,750 | 19.9 |
| Deferred inflows | 3,323,211 | — | 100.0 |
| Net position: | | | |
| Net investment in capital assets | (27,484,410) | (19,719,120) | 39.4 |
| Unrestricted | 34,935,278 | 32,091,102 | 8.9 |
| Total net position | 7,450,868 | 12,371,982 | (39.8) |
| Total liabilities and net position | $ 521,662,645 | 438,407,732 | 19.0% |

Current assets consist primarily of cash, accounts receivable, inventory, prepaid expenses, and receivables from other University departments. Current assets were $41.4 million more than current liabilities at June 30, 2015. Total current assets increased from $61.2 million at June 30, 2014 to a total of $72.1 million at June 30, 2015. The increase was caused by an increase in cash due to an overall increase in residence hall room rents, conference services, and related food services.

Noncurrent assets consist of capital assets of land, buildings, building improvements, equipment, construction in process, and prepayment of payroll modernization project. Noncurrent assets were $71.1 million more at June 30, 2015, than at June 30, 2014, mainly due to the construction of additional housing under the Housing Master Plan.

Current liabilities consist primarily of accounts payable, accrued interest, accrued expenses, unearned revenue, deposits, due to other University departments, and the current portion of debt payments. Current liabilities increased by 22.1% to a total of $30.7 million at June 30, 2015, from $25.1 million at June 30, 2014, due to increases in refundable and retained deposits, and short-term portion of Internal Lending Program (ILP) debt, all related to the overall increase associated with the new residential housing.

Noncurrent liabilities consist of the long-term portion of ILP debt and net pension liability. Total long-term debt increased by 17.9% to a total of $472.6 million at June 30, 2015, from $400.9 million at June 30, 2014, due primarily to additional debt incurred to finance the Comprehensive Housing Master Plan (the Master Plan). Net pension liability decreased from $10.8 million at June 30, 2014 to $7.7 million at June 30, 2015.

The change in net position or "equity" measures whether the overall financial condition has improved or deteriorated during the past year. Total net position decreased by 39.8% to a total of $7.5 million at June 30, 2015. Although the continued strong demand for campus housing resulted in a positive net operating income, HFS had higher debt interest payments, increased building depreciation and the implementation of Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions*, resulted in the recording of pension liabilities for the first time.

### *Statement of Revenue, Expenses, and Changes in Net Position*

The changes in total net position, as presented on the statement of net position, are detailed in the activity presented in the statement of revenue, expenses, and changes in net position. This statement presents HFS's results of operations. In accordance with GASB reporting principles, revenue and expenses are classified as operating, nonoperating, or other.

In general, operating revenue is revenue received for providing housing, food service, and related services to the students and conference guests. Operating revenue is also received in the form of educational sponsorship, and as vending commissions. Operating expenses are those expenses paid to provide the services and resources, mainly salaries and benefits, cost of food, building depreciation, and administrative overhead.

Nonoperating revenue is that received for which goods and services were not provided. Under GASB reporting principles, investment income and expenses are classified as nonoperating activities. Also included as nonoperating are energy rebates and utility refunds.

The following is a condensed view of the statement of revenue, expenses, and changes in net position for the fiscal years ended June 30, 2015 and 2014:

| | | 2015 | 2014 | Percentage change |
|---|---|---|---|---|
| Operating revenue | $ | 108,966,444 | 100,298,527 | 8.6% |
| Operating expenses | | (87,025,494) | (87,285,766) | (0.3) |
| Net operating income | | 21,940,950 | 13,012,761 | 68.6 |
| Net nonoperating expense | | (17,089,340) | (21,946,780) | (22.1) |
| Capital asset contribution | | — | (2,584,000) | 100.0 |
| Change in net position | | 4,851,610 | (11,518,019) | 142.1 |
| Net position, beginning of year | | 12,371,982 | 23,890,001 | (48.2) |
| Effect of accounting and reporting entity changes | | (9,772,724) | — | (100.0) |
| Net position, end of year | $ | 7,450,868 | 12,371,982 | (39.8)% |

**Revenue from all Sources**

The following table summarizes revenue from all sources for the years ended June 30, 2015 and 2014:

| | | 2015 | 2014 |
|---|---|---|---|
| Residence halls and single-student apartment rent | $ | 56,305,353 | 52,313,110 |
| Residence halls and retail food services | | 39,740,009 | 36,832,222 |
| Conferences and guest rent | | 4,947,456 | 3,600,051 |
| Leases | | 2,621,369 | 2,813,768 |
| Family housing rent | | 2,291,191 | 2,061,616 |
| Forfeitures and miscellaneous fees | | 1,058,495 | 789,700 |
| Educational sponsorship | | 857,000 | 806,611 |
| Vending machines | | 646,003 | 625,143 |
| Laundry | | 397,967 | 377,228 |
| Microfridge commission | | 7,531 | 6,693 |
| Energy rebates and utilities refunds | | 1,729,868 | 1,472,952 |
| Investment income | | 1,256,635 | 1,002,179 |
| Other | | 94,070 | 72,385 |
| Total revenue – all sources | $ | 111,952,947 | 102,773,658 |



(Continued)

The largest revenue source is residence hall and single-student room rent and food services, which comprised 85.8% of total revenue in 2015, versus 86.7% in 2014. Residence hall and single-student rent increased slightly by 7.6%, or $4.0 million and conference services also increased by 37.4% or $1.3 million over the prior year. Aside from a 3.6% rent increase, the new residential buildings brought in a net increase of 207 beds from prior year. Conference groups coming to the campus continued to grow.

Nonoperating revenue increased by 20.7% due to equal increases in investment income from increased cash and a one-time soil remediation reimbursement received this year from Exxon.

**Expenses and Expense Transfers**

The following table summarizes expenses and expense transfers for the years ended June 30, 2015 and 2014:

| | | 2015 | 2014 |
|---|---|---|---|
| Salaries and related benefits | $ | 25,704,043 | 24,274,588 |
| Depreciation | | 16,137,829 | 16,074,790 |
| Cost of food and merchandise | | 15,633,022 | 14,362,105 |
| Indirect expenses | | 6,416,787 | 6,407,093 |
| Utilities | | 6,474,086 | 6,587,079 |
| Noncapitalized equipment | | 5,061,325 | 8,500,845 |
| Contract services | | 4,617,115 | 4,004,652 |
| Supplies | | 2,938,944 | 2,921,768 |
| Repairs and maintenance | | 2,345,640 | 2,454,095 |
| Institutional overhead | | 1,351,618 | 1,349,043 |
| Interest expense on capital asset-related debt | | 19,276,208 | 16,761,966 |
| Loss on capital asset disposals and transfers | | 3,176 | 6,512,296 |
| Financing cost | | 796,459 | 1,147,649 |
| Capital asset contribution to other department | | — | 2,584,000 |
| Other | | 345,085 | 349,708 |
| Total expenses and expense transfers | $ | 107,101,337 | 114,291,677 |

Salaries and benefits expense increased by 5.9%, or $1.4 million, over the prior year due mainly to rate increases and to increased housing and food operation with Lander Hall and Local Point food service operation for a full year in fiscal year 2015.

Cost of food and merchandise increased by 8.8%, or $1.3 million, over the prior year due to an increase in residence hall and retail food services revenue of a comparable 7.9%. Cost of food was 39.3% of total food service revenue for fiscal year 2015 and 39.0% for fiscal year 2014.

Nonoperating expenses decreased by 17.8%, or $4.3 million over the prior year. Unlike last year, there was no significant disposal of capital assets this year, which attributed to a decrease of $6.5 million. The decrease was partially offset by a $2.5 million increase in debt service payments.

**Economic Factors and Significant Events**

***Housing Operation***

Autumn quarter 2015 will open at 120.0% occupancy of as-built capacity with approximately 50 students in temporary lounge space and 250 students on the waiting list. To meet excess student demand in 2015–16, 18 doubles and 82 triples were added to our housing inventory. UW Real Estate managed off-campus facilities are showing similar strength in demand.

Fiscal year 2014–15 was the first full year of operations of the new Lander Hall, which opened in winter 2014. Mercer Court opened at 100% occupancy in autumn 2014, a result of significant increase in 12-month single student demand. To meet excess 9-month demand, 100 new triples were added to west campus residence halls.

***Updates to the Housing Master Plan***

Phase 1, which consisted of four new buildings, was completed as of September 2012. Poplar residence hall and Cedar Apartments were opened on September 2011 and Alder and Elm residence halls opened in September 2012.

Phase 2, which consisted of two properties, was completed in January 2014. Mercer Court opened on schedule in autumn 2013 and Lander residence hall opened in January 2014.

In June 2012, the Board of Regents approved borrowing under the ILP for up to $142.3 million for Phase 3. Phase 3 includes the demolition of Terry Hall and the construction of two new residence halls, Maple and New Terry. New Terry Hall and Maple Hall will open to students in autumn 2015 and signify the completion of Phase 3 and the west campus development phase of the Housing Master Plan. Net bed space will have increased by approximately 2,450.

The planning process for Phase 4 of the Housing Master Plan began in summer 2014. This phase focuses on north campus and will include the demolition and replacement of Haggett Hall and McCarty Hall as well as the construction of three new halls surrounding Denny Field. The future of McMahon Hall is uncertain at this time – possibly being renovated, demolished or repurposed within the university. The plans for Phase 4 will be reviewed by the University President and the Office of the Provost (Provost) and will be presented to the Board of Regents in November 2015 for approval. Phase 4 financing and pro formas are currently being vetted through Treasury.

Anticipating approval for Phase 4a, McCarty Hall will be closed to students in fiscal year 2015–16 as it prepares to be decommissioned in early 2016. McCarty will remain open through the end of the 2015 summer conference season (September 2015).

Debt service is being paid to the ILP for all Phases 1 and 2 buildings. Debt service on Phase 3 for the New Terry and Maple Halls is scheduled to begin October 2015. The debt service ratio for fiscal year 2015 is 1.55.



(Continued)

Effective April 2015, the ILP interest rate was decreased from 5.5% to 4.75% for all existing and future ILP debt, resulting in an annual savings of $465,796 for fiscal year 2014–15 and approximately $1,959,00 for fiscal year 2015-16. In July 2015, Treasury announced that it would be refinancing all non-ILP debt with interest rates above 4.75% into the ILP program. The adjustment will be effective in November 2015 and savings are estimated at an additional $1,000,000 annually. Debt service for new Terry and Maple Halls is scheduled to begin in October 2015.

***Dining Operation***

Phase 2 of the Housing Master Plan introduced Local Point in Lander Hall and Husky Grind Café in Mercer Court. Local Point is the replacement dining option for 1101, which was demolished with Terry residence hall during winter and spring quarter of 2014. Local Point is located on the ground level of Lander and is easily accessible by all west campus residence halls.

Local Point was designed to accommodate the increased west campus student capacity as determined by the Housing master plan. Due to the ongoing construction of New Terry and Maple Halls, Local Point operated under capacity in 2014–15. When New Terry and Maple Halls open in autumn 2015, an additional 1,100 beds will be added to west campus and Local Point's meal factor.

The new Husky Grind Café at Mercer Court expands the offerings of the in-house roasted coffee brand, Husky Grind Coffee and brings the coffee brand exclusively to a total of four retail locations across campus. These locations include the District Market, Cultivate, and the Parnassus Café. Coffee sales and their related transaction counts have continued to grow quarter to quarter over the last two fiscal years at these locations.

The express markets produced net income of $1,327,000 during the 2014-15 fiscal year, $337,000 more than their budgeted target of $1,033,000. While the Nook and Ian's Domain continued to do well, it was the growing popularity of the District Market, which contributed $828,000 to this total. Continued profitability for the express markets is anticipated in 2015-16. Ian's Domain is located in McCarty Hall and will close after the 2015 summer conference season.

***Retail and Remote Dining Operation***

Retail and Remote locations far exceeded anticipated budgeted net operating income in 2014-15 by $275,000.

Autumn 2013 marked the beginning of the institutional-level Starbucks and Coca-Cola sponsorship agreements. All non-Husky Grind locations were converted to the Starbucks model including signage, equipment, product, and pricing. Other changes resulting from the Starbucks agreement include the closing of Padelford Espresso, serving Green Mountain coffee, and Freshens in the Husky Den. The first licensed store front has been constructed in the Husky Union Building (HUB) and will open in autumn.

***Systemwide Considerations***

Effective January 1, 2015, the University of Washington increased the minimum wage for hourly student and staff to $10.10 from $9.47. This was done to align the minimum wage with that of the wage set for federal contractors. The city of Seattle also implemented a new $15.00 per hour minimum wage, which is to be phased-in over the next two years. As a result, the University of Washington increased the minimum wage to $11.00 per hour effective April 1, 2015 with additional planned increase to $13.00 on January 1, 2016 and finally to $15.00 on January 1, 2017.

In an effort to bridge the increase in the cost of labor, the Provost has provided funding totaling $98,500 in 2014-15 and agreed to provide $538,177 in 2015-16. No additional funding is planned for future years.

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**
(A Department of University of Washington)

Statement of Net Position

June 30, 2015

**Assets and Deferred Outflow of Resources**

| | | |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents in the University of Washington Invested Funds Pool | $ | 63,483,695 |
| Accounts receivable, net | | 1,404,583 |
| Prepaid expense | | 281,312 |
| Inventory | | 887,725 |
| Due from other University departments | | 6,006,271 |
| Total current assets | | 72,063,586 |
| Noncurrent assets: | | |
| Prepaid expense (note 1) | | 2,037,193 |
| Capital assets, less accumulated depreciation (note 3) | | 446,296,199 |
| Total noncurrent assets | | 448,333,392 |
| Pension deferred outflow of resources (note 6) | | 1,265,667 |
| Total assets and deferred outflow of resources | $ | 521,662,645 |

**Liabilities, Deferred Inflow of Resources, and Net Position**

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | $ | 4,662,276 |
| Accrued interest | | 1,499,656 |
| Other accrued expenses | | 2,197,088 |
| Unearned revenue | | 5,598,957 |
| Deposits | | 4,065,730 |
| Due to other University departments | | 1,649,203 |
| Internal lending program payable, current portion (notes 2 and 5) | | 10,653,707 |
| Lease payable, current portion (notes 2 and 4) | | 340,000 |
| Total current liabilities | | 30,666,617 |
| Noncurrent liabilities: | | |
| Internal lending program payable, less current portion (notes 2 and 5) | | 470,130,353 |
| Net pension liability (note 6) | | 7,656,596 |
| Lease payable, less current portion (note 4) | | 2,435,000 |
| Total noncurrent liabilities | | 480,221,949 |
| Total liabilities | | 510,888,566 |
| Pension deferred inflow of resources (note 6) | | 3,323,211 |
| Net position: | | |
| Net investment in capital assets | | (27,484,410) |
| Unrestricted | | 34,935,278 |
| Total net position | | 7,450,868 |
| Total liabilities, deferred inflow of resources, and net position | $ | 521,662,645 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**
(A Department of University of Washington)

Statement of Revenue, Expenses, and Changes in Net Position

Year ended June 30, 2015

| | | |
|---|---|---|
| Operating revenue: | | |
| Residence halls and single-student apartment rent | $ | 56,305,353 |
| Residence halls and retail food services | | 39,740,009 |
| Conferences and guest rent | | 4,947,456 |
| Leases | | 2,621,369 |
| Family housing rent | | 2,291,191 |
| Forfeitures and miscellaneous fees | | 1,058,495 |
| Educational Sponsorship | | 857,000 |
| Vending machines | | 646,003 |
| Laundry | | 397,967 |
| Microfridge commission | | 7,531 |
| Other | | 94,070 |
| Total operating revenue | | 108,966,444 |
| Operating expenses: | | |
| Salaries and related benefits | | 25,704,043 |
| Depreciation | | 16,137,829 |
| Cost of food and merchandise | | 15,633,022 |
| Indirect expenses | | 6,416,787 |
| Utilities | | 6,474,086 |
| Noncapitalized equipment | | 5,061,325 |
| Contract services | | 4,617,115 |
| Supplies | | 2,938,944 |
| Repairs and maintenance | | 2,345,640 |
| Institutional overhead | | 1,351,618 |
| Other | | 345,085 |
| Total operating expenses | | 87,025,494 |
| Net operating income | | 21,940,950 |
| Nonoperating revenue (expense): | | |
| Energy rebates | | 1,315,276 |
| Investment income | | 1,256,635 |
| Utilities Refund | | 414,592 |
| Interest expense on capital asset-related debt | | (19,276,208) |
| Financing cost | | (796,459) |
| Loss on capital asset disposals and transfers | | (3,176) |
| Total nonoperating expense | | (17,089,340) |
| Change in net position | | 4,851,610 |
| Net position, beginning of year, as restated (note 1) | | 2,599,258 |
| Net position, end of year | $ | 7,450,868 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**
(A Department of University of Washington)

Statement of Cash Flows

Year ended June 30, 2015

| | |
|---|---|
| Cash flows from operating activities: | |
| Cash received from student housing fees | $ 56,996,958 |
| Cash received from residence hall food services | 39,813,608 |
| Cash received from conference services | 4,907,056 |
| Cash received from leases | 2,639,851 |
| Cash received from facility rentals | 2,202,637 |
| Cash received from vending commissions | 648,710 |
| Cash received from educational sponsorship | 857,000 |
| Cash received from others | 93,654 |
| Cash received for interfund and debit card activities | 119,580 |
| Cash paid to suppliers | (38,425,353) |
| Cash paid for employee salaries, wages, and benefits | (24,435,013) |
| Cash paid for indirect expenses | (7,716,572) |
| Net cash flows provided by operating activities | 37,702,116 |
| Cash flows from capital and related financing activities: | |
| Purchases of capital assets | (79,604,170) |
| Borrowing on internal lending program | 82,839,526 |
| Interest paid on capital debt | (22,597,474) |
| Principal payments on capital debt | (8,379,662) |
| Financing cost paid on capital debt | (796,459) |
| Net cash flows used in capital and related financing activities | (28,538,239) |
| Cash flow from investing activity: | |
| Interest received | 1,274,719 |
| Net change in cash and cash equivalents | 10,438,596 |
| Cash and cash equivalents, beginning of year | 53,045,099 |
| Cash and cash equivalents, end of year | $ 63,483,695 |



(Continued)

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**
(A Department of University of Washington)

Statement of Cash Flows

Year ended June 30, 2015

| | |
|---|---|
| Reconciliation of operating income to net cash flows from operating activities: | |
| Operating income | $ 21,940,950 |
| Adjustments to reconcile operating income to net cash flows provided by operating activities: | |
| Depreciation | 16,137,829 |
| Change in operating assets and liabilities: | |
| Accounts receivable | (133,211) |
| Prepaid expenses and other | (2,051,012) |
| Inventory | 90,363 |
| Due to/from other University departments | (368,618) |
| Accounts payable | 1,620,879 |
| Unearned revenue | 321,945 |
| Accrued expenses | 58,010 |
| Deposits | 143,565 |
| Pension deferred resources and liability | (58,584) |
| Net cash flows provided by operating activities | $ 37,702,116 |
| Supplemental disclosures for cash flow information: | |
| Capitalized interest | $ 3,373,960 |
| Amortization of deferred premium on refunded bonds | 66,480 |

See accompanying notes to financial statements.

## (1) Organization and Significant Accounting Policies

### *(a) Organization*

The University of Washington Housing and Food Services (HFS) operates food services, residence halls, and apartment complexes both on and off the University of Washington (the University) campus. The operations of HFS as an auxiliary enterprise support the University's mission by providing safe, convenient, and affordable housing as well as programs that promote personal development. In addition, HFS provides conference facilities and catering services to various organizations. The University provides certain administrative services to HFS.

### *(b) Basis of Accounting*

The financial statements have been prepared in accordance with generally accepted accounting principles. The statements are presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenue is recognized when earned, and expenses are recorded when an obligation has been incurred. All internal activities have been eliminated.

On July 1, 2014, HFS adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This Statement requires governments providing defined-benefit pensions to their employees to recognize their long-term obligation for pension benefits as a liability for the first time, along with the associated assets, which have been set aside to fund the plan. Since the University participates in several cost sharing pension plans, which are administered by the State of Washington Department of Retirement Systems (DRS), this Statement requires the University to recognize its proportionate share of the state-wide net pension liability for each of the plans in which it participates. HFS recorded their proportionate share of the net pension liability in its 2015 financial statements, which had a material impact to its financial statements. The Statement also eliminates the method of amortizing the liability balances over several years, and instead requires full recognition of the net liability upon implementation. In addition to the reporting changes described above, implementation of this Statement resulted in the restatement of fiscal year 2015 beginning unrestricted net position, reducing it by $9,772,724. See note 6 for further discussion on the adoption of this standard.

With the adoption of GASB Statement No. 68, net position was restated at July 1, 2014. Below is a reconciliation of total net position as previously reported at June 30, 2014, to the restated net position:

| | | |
|---|---|---|
| Net position at June 30, 2014, as previously reported | $ | 12,371,982 |
| Adoption of GASB No. 68 | | (9,772,724) |
| Net position at July 1, 2014, as restated | $ | 2,599,258 |

### *(c) Cash and Cash Equivalents in the University Invested Funds Pool*

All of the HFS's cash and cash equivalents are invested in the University's Invested Funds Pool. The following information is for the entire pool and are audited disclosures as a part of the University audit.

The Board of Regents of the University is responsible for the management of the University's investments. The Board establishes investment policy, which is carried out by the Chief Investment Officer. The University of Washington Investment Committee, comprising Board members and investment professionals, advises on matters relating to the management of the University's investment portfolios. The composition of the carrying amounts of investments by type at June 30, 2015 is listed below.

**University investments**

| **Investment type** | | **Carrying value** |
|---|---|---|
| | | (Dollars in thousands) |
| Cash equivalents | $ | 403,978 |
| Fixed income | | 1,726,481 |
| Equity | | 1,733,102 |
| Nonmarketable alternatives | | 353,053 |
| Absolute return | | 561,999 |
| Real assets | | 189,447 |
| Miscellaneous | | 8,603 |
| Total investments | $ | 4,976,663 |

*Investment Pools* – The University combines most short-term cash balances into the Invested Funds Pool. At June 30, 2015, the Invested Funds Pool totaled $1,526,380,000. The Invested Funds Pool also owns units in the Consolidated Endowment Fund valued at $806,198,000 on June 30, 2015. By University policy, departments with qualifying funds in the Invested Funds Pool receive distributions based on their average balances and on the type of balance. Campus depositors received 2% in fiscal year 2015. Endowment operating and gift accounts received 3% in fiscal year 2015. The difference between the actual earnings of the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The majority of the endowed funds are invested in a pooled fund called the Consolidated Endowment Fund (CEF). Individual endowments purchase units in the pool on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held. RCW 24.55 of the Washington State Code and the Uniform Prudent Management of Institutional Funds Act allow for total return expenditure under comprehensive prudent standards.

*Interest Rate Risk* – The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform, while controlling the interest rate risk in the portfolio. The weighted average effective duration of the University's fixed income portfolio was 1.81 years at June 30, 2015.

*Credit Risk* – Fixed income securities are subject to credit risk, which is the risk that the issuer or other counterparty to a financial instrument will not fulfill its obligations, or that negative perceptions of the issuer's ability to make these payments will cause prices to decline. Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University Investment Policies limit fixed income exposure to investment grade assets. The Investment Policy for the Invested Funds' cash pool requires each manager to maintain an average quality rating of "AA" as issued by a nationally recognized rating organization. The Invested Funds' liquidity pool requires each manager to maintain an average quality rating of "A" and to hold 25% of their portfolios in government and government agency issues. The Investment Policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investment-to-investment grade credits.

Duration and credit risk figures at June 30, 2015 exclude $36,027,000 of fixed income securities held outside the CEF and the Invested Funds Pool. These amounts make up 1.69%, of the University's fixed income investments (including cash equivalents) and are not included in the duration figures detailed in the following table.

The composition of the fixed income securities at June 30, 2015 along with credit quality and effective duration measures is summarized below:

**Fixed income credit quality and effective duration**

| Investments | U.S. government | Investment grade* | Noninvestment grade | Not rated | Total | Duration (in years) |
|---|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | | |
| 2015: | | | | | | |
| U.S. Treasuries | $ 842,525 | — | — | — | 842,525 | 1.43 |
| U.S. government agency | 644,721 | — | — | — | 644,721 | 2.46 |
| Mortgage backed | — | 107,070 | 75,060 | 22,415 | 204,545 | 2.01 |
| Asset backed | — | 195,968 | 6,998 | 24,111 | 227,077 | 1.73 |
| Corporate and other | — | 175,364 | — | 200 | 175,564 | 1.18 |
| Total | $ 1,487,246 | 478,402 | 82,058 | 46,726 | 2,094,432 | 1.81 |

* Investment grade securities are those that are rated BBB and higher by Standard and Poor's or Baa and higher by Moody's.

*Foreign Currency Risk* – The University's Investment Policies permit investments in international equity and other asset classes, which can include foreign currency exposure. The University held non-U.S. denominated securities at June 30, 2015 of $1,195,070,000.

**Investments denominated in foreign currency**

| | | (Dollars in thousands) |
|---|---|---|
| Chinese Renminbi (RMB) | $ | 211,184 |
| Euro (EUR) | | 174,487 |
| Indian Rupee (INR) | | 112,679 |
| Japanese Yen (JPY) | | 110,617 |
| Hong Kong Dollar (HKD) | | 60,046 |
| South Korean Won (KRW) | | 56,835 |
| British Pound (GBP) | | 54,880 |
| Brazilian Real (BRL) | | 54,225 |
| Swiss Franc (CHF) | | 39,061 |
| Russian Ruble (RUB) | | 36,218 |
| Canadian Dollar (CAD) | | 35,385 |
| Philippine Peso (PHP) | | 29,100 |
| Taiwanese Dollar (TWD) | | 27,055 |
| Mexican Peso (MXN) | | 23,898 |
| Remaining currencies | | 169,400 |
| Total | $ | 1,195,070 |

### *(d) Accounts Receivable*

HFS has established an allowance for doubtful accounts to allow for those receivables, which are estimated to be uncollectible. The allowance is based on historical collection rates. Student accounts are considered past due if they are unpaid for 30 days after the due date. Other customer accounts are considered past due if they are unpaid for 60 days after the due date. When an account is deemed uncollectible, it is generally written off against the allowance. The balance of the allowance account was $37,098 at June 30, 2015.

### *(e) Inventory*

Inventory, consisting primarily of food, is stated at the lower of cost (first-in, first-out method) or market.

### *(f) Prepaid Expense*

Prepaid expense, current, consists primarily of building insurance amortized over one year. Prepaid expense, noncurrent, represents implementation cost for the Human Resource and Payroll modernization project to be allocated to campus beginning July 1, 2016 that was prepaid by HFS to avail of the reduced cost versus incurring interest if paid over the long-term period.

***(g) Capital Assets***

Buildings, building improvements, and equipment are stated at cost. Additions, replacements, major repairs, and renovations are capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 50 years for building components, 20 to 50 years for infrastructure and land improvements, and 4 to 13 years for equipment. Expenditures for noncapitalized equipment and repairs that represent normal replacement of such equipment and routine maintenance of the buildings are expensed as incurred, as are furniture, fixtures, or equipment for newly constructed buildings individually that do not meet the criteria described below. Building and improvements are capitalized if they result in additional asset services (i.e., expanded facilities), result in more valuable asset services (i.e., upgraded facilities), or extend normal service life. Expenditures are not capitalized if they are incurred to maintain assets in good operating condition, and/or do not meet the criteria for capitalization stated above. Equipment with a cost of $2,000 and above is generally capitalized if it benefits more than one operating cycle.

HFS developed a Comprehensive Housing Master Plan to develop residence halls and single-student apartments in four phases. The development of these residence halls creates a richer on-campus community, alleviating the currently overcrowded conditions within student housing, and provide additional bed capacity (surge space) to support renovation of existing residence halls. This additional capacity permits HFS to renovate existing facilities while continuing to meet current housing demand. As of June 30, 2015, costs incurred related to the Housing Master Plan are approximately $434 million. These costs were recorded in construction in process and completed building costs at June 30, 2015. Total projected cost of the Housing Master Plan is $489.9 million, which will be funded by borrowing under the ILP (see note 5). The Board of Regents has approved borrowing under the ILP of up to $523.4 million for three of the four phases of the Housing Master Plan as of June 30, 2015.

Interest expense is capitalized during the time a project is under construction and begins upon the issuance of debt to finance the construction of a capital asset. Capitalized construction-related interest was $3.4 million during 2015.

***(h) Unearned Revenue***

Unearned revenue consists of prepaid food sales, room rent, and conference revenue.

***(i) Deposits***

Deposits consist of a required $500 per student housing damage deposit that is refundable when the student vacates (presuming no damage resulted during the student's tenure in the housing unit).

***(j) Net Position***

Net position consists of the following components:

*Net investment in capital assets* – This component consists of capital assets, net of accumulated depreciation, reduced by the net outstanding debt balances related to capital assets, net of unamortized debt expenses. The negative balance at June 30, 2015 is due to the inclusion of existing debt on the old Mercer, Lander, and Terry Halls, all of which were demolished as of fiscal year 2015, while additional debt was incurred for the demolition and redevelopment.

*Unrestricted* – This component consists of assets and liabilities that do not meet the definition of "net investment in capital assets."

***(k) Operating and Nonoperating Revenue and Expenses***

In general, operating revenue is revenue received for providing housing, dining, and related services to the customers of HFS, the majority of which consists of room and board services to students. Revenue is recognized as the food service is provided, the appropriate rental period occurs, or the conference takes place. Operating expenses are those expenses paid to provide the services and resources, mainly consisting of the cost of food, salaries and benefits, utilities, building maintenance, and administrative overhead expenses.

Nonoperating revenue is recognized for receipts under the energy rebate program applied from the Master Plan constructions. Nonoperating expense includes interest expense and financing cost incurred in borrowing for the construction of buildings under the Master Plan.

***(l) Institutional Overhead***

The University allocates certain general and administrative charges to those departments for which services are performed. This institutional overhead charge, which is based on a percent of division revenue, amounted to $1,351,618 during the year ended June 30, 2015.

***(m) Indirect Expenses***

Administrative expenses such as salaries and benefits, contract services, and supplies are reported as indirect expense. These allocations to HFS amounted to $6,416,787 for the year ended June 30, 2015.

***(n) Income Taxes***

As a part of the University, the operations of HFS are exempt from federal income taxes, except to the extent of unrelated business income. HFS did not incur unrelated business income tax during 2015, and accordingly, the financial statements do not include a provision for federal income taxes.



(Continued)

### *(o) Use of Estimates*

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

## (2) Noncurrent Liabilities

Noncurrent liability activity for the year ended June 30, 2015 is summarized as follows:

| | Balance at June 30, 2014 | Additions | Reductions | Balance at June 30, 2015 |
|---|---|---|---|---|
| Noncurrent liabilities: | | | | |
| ILP payable | $ 406,066,925 | 82,839,526 | (8,122,391) | 480,784,060 |
| Net pension liability | 10,768,232 | — | (3,111,636) | 7,656,596 |
| Lease payable | 3,100,000 | — | (325,000) | 2,775,000 |
| Total noncurrent liabilities | 419,935,157 | $ 82,839,526 | (11,559,027) | 491,215,656 |
| Current portion | (8,242,653) | | | (10,993,707) |
| Noncurrent portion | $ 411,692,504 | | | 480,221,949 |

## (3) Capital Assets

Capital asset activity for the year ended June 30, 2015 is summarized as follows:

| | Balance at June 30, 2014 | Additions | Reductions | Balance at June 30, 2015 |
|---|---|---|---|---|
| Capital assets, not being depreciated: | | | | |
| Land | $ 6,775,215 | — | — | 6,775,215 |
| Construction in progress | 24,872,830 | 84,690,995 | (484,423) | 109,079,402 |
| Total capital assets not being depreciated | 31,648,045 | 84,690,995 | (484,423) | 115,854,617 |
| Capital assets, being depreciated: | | | | |
| Building and building improvements | 419,916,767 | 484,423 | — | 420,401,190 |
| Equipment | 5,631,108 | 513,420 | (85,171) | 6,059,357 |
| Total capital assets being depreciated | 425,547,875 | 997,843 | (85,171) | 426,460,547 |



(Continued)

| | Balance at June 30, 2014 | Additions | Reductions | Balance at June 30, 2015 |
|---|---|---|---|---|
| Less accumulated depreciation: | | | | |
| Building and building improvements | $ 76,139,825 | 15,489,260 | — | 91,629,085 |
| Equipment | 3,823,306 | 648,569 | (81,995) | 4,389,880 |
| Total accumulated depreciation | 79,963,131 | 16,137,829 | (81,995) | 96,018,965 |
| Capital assets, net | $ 377,232,789 | 69,551,009 | (487,599) | 446,296,199 |

## (4) Leases

### *Lease Payments*

In June 2001, the state of Washington, in conjunction with the Washington Finance Officers Association (a nonprofit corporation), issued Certificates of Participation (CoPs) to certain investors. The proceeds from the CoPs were used for improvements to food services at the HUB. The University has agreed to make certain payments (considered lease payments) as required by the CoPs and HFS has agreed to reimburse the University for these payments.

At June 30, 2015, the total principal amount of obligation under this agreement was $2,775,000. It is expected to be repaid in installments of approximately $480,000 (including imputed interest of approximately 5%) per year through 2022. Following is a summary of minimum payments under this agreement (principal and interest) for the years ending June 30:

| | Principal | Interest | Total |
|---|---|---|---|
| 2016 | $ 340,000 | 143,284 | 483,284 |
| 2017 | 355,000 | 126,284 | 481,284 |
| 2018 | 375,000 | 108,534 | 483,534 |
| 2019 | 395,000 | 89,315 | 484,315 |
| 2020 | 415,000 | 68,775 | 483,775 |
| 2021–2022 | 895,000 | 71,138 | 966,138 |
| | $ 2,775,000 | 607,330 | 3,382,330 |

### *Lease Revenue*

The University and Community Development Properties (CDP), a nonprofit organization, entered into a lease agreement whereby CDP issued bonds to undertake a comprehensive redevelopment of the Commodore Duchess, Radford Court, and Nordheim Court properties, mainly for student housing. In July 2011 and 2012, the University took over the Commodore Duchess, Radford Court, and Nordheim Court properties (the Apartments) and refunded the CDP bonds with loan proceeds from the Internal Lending Program (ILP). In accordance with the ILP financing agreement, HFS will be obligated to pay debt service on this loan only in the event that funds from the Apartments are insufficient. The Apartments have been self-sustaining in past years. The Apartments are owned by the University and are managed by University of Washington Real Estate (UWRE) with an outside property manager. As of June 30, 2015, the outstanding debt under this agreement was $62,397,460.

The University receives an annual payment from the Apartments, which it designates to HFS. Revenue from these properties was $2,621,369 for the year ended June 30, 2015.

## (5) The Internal Lending Program

Effective July 1, 2008, the University Board of Regents adopted the amended "Debt Management Policy: Statement of Objectives and Policies" to provide for the implementation of an ILP.

The purpose of the ILP is to lower the University's overall cost of capital and provide internal borrowing units with a stable and predictable borrowing rate. The ILP will make loans to internal borrowers at a uniform internal lending rate. These loans will be funded through the issuance of University General Revenue bonds and notes. ILP program policies include a provision for a rate of stabilization reserve and a provision for rate adjustments, if necessary.

On April 22, 2008, the University issued General Revenue Refunding Bonds (2008 Bonds) to refund certain outstanding bonds of the University. A portion of the proceeds from the sale of the 2008 Bonds was used for the purpose of refunding HFS's 1996 junior lien revenue bonds with a premium. HFS is obligated to the ILP in the amount of $14,229,167 as of June 30, 2015. The final payment is due in the fiscal year ending 2022. The average interest rate is 3.94%. The balance of the premium was $369,980 as of June 30, 2015.

In December 2008, HFS drew funds from the ILP in a total amount of $6,348,067 for the purchase of a piece of property called the Cavalier Apartments for future housing development plans. The final payment is due in the fiscal year ending 2034. The interest rate was adjusted in April 2015 from 5.5% to 4.75%. The interest is reviewed annually and is subject to adjustment. HFS is obligated to the ILP in the amount of $5,434,064 as of June 30, 2015.

In October 2010, the University issued General Revenue & Refunding Bonds, 2010A & B. A portion of the proceeds was used to partially refund the 2002 Housing and Dining Revenue & Refunding Bonds with a premium. HFS is obligated to the ILP in the amount of $8,118,212 as of June 30, 2015. The final payment is due in the fiscal year ending 2032. The average interest rate is 5.43%. The balance of the premium was $95,359 as of June 30, 2015.

In March 2012, the University issued General Revenue & Refunding Bonds, 2012A. A portion of the proceeds was used to fully refund the 2002 and 2004 Housing and Dining Revenue & Refunding Bonds. The amount refunded was $15,595,000 with no gain or loss. HFS is obligated to the ILP in the amount of $11,209,943 as of June 30, 2015. The final payments are due in the fiscal years ending 2022 and 2029. The interest rates are 5.43% and 4.06%, respectively.

From May 2009 through June 2012, the Board of Regents approved borrowing for HFS under the ILP of up to $523.4 million for three of the four phases of the Housing Master Plan to build residence halls and single student apartments. The total draws to fund the project as of June 30, 2015 has amounted to approximately $452 million and HFS has made principal payments beginning October 2011 for Phases 1 and 2. Principal payments for Phase 3 will begin in September 2015. HFS is obligated to the ILP in the amount of $441,327,335 as of June 30, 2015. The final payments are due between the fiscal years ending 2042 and 2045. The interest rate was adjusted in April 2015 from 5.5% to 4.75%.

The ILP agreements require HFS to maintain certain financial performance ratios. If these requirements were violated, future financing for the ILP can be ceased or minimized. As of June 30, 2015, HFS met all these requirements.

The following is a summary of future payments (principal and interest) to be paid to the University to cover the debt service payments for the years ending June 30:

| | Principal | Interest | Total |
|---|---|---|---|
| 2016 | $ 10,653,707 | 21,840,151 | 32,493,858 |
| 2017 | 11,471,116 | 22,151,330 | 33,622,446 |
| 2018 | 12,021,945 | 21,597,439 | 33,619,384 |
| 2019 | 12,593,914 | 21,023,547 | 33,617,461 |
| 2020 | 13,203,243 | 20,412,370 | 33,615,613 |
| 2021–2025 | 65,721,126 | 92,356,535 | 158,077,661 |
| 2026–2030 | 74,250,534 | 76,001,278 | 150,251,812 |
| 2031–2035 | 88,655,310 | 56,534,507 | 145,189,817 |
| 2036–2040 | 109,106,297 | 33,310,898 | 142,417,195 |
| 2041–2045 | 82,641,529 | 7,269,257 | 89,910,786 |
| | 480,318,721 | $ 372,497,312 | 852,816,033 |
| Add unamortized premium | 465,339 | | |
| | $ 480,784,060 | | |

## (6) Pension Plan

### *(a) Public Employees’ Retirement System (PERS)*

PERS was established in 1947 and its retirement benefit provisions are contained in Chapters 41.34 and 41.40 of the Revised Code of Washington (RCW). PERS is a cost-sharing multiple-employer retirement system comprised of three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined-benefit plans, and PERS Plan 3 is a defined-benefit plan with a defined-contribution component. PERS members include higher education employees not participating in other higher education retirement programs.

PERS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined-benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined-contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined-benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

### *(b) The Pension Plans' Fiduciary Net Positions*

The pension plans' fiduciary net positions have been determined on the same basis used by the pension plans. Washington State Department of Retirement Systems (DRS) financial statements have been prepared in conformity with generally accepted accounting principles (GAAP). The retirement plans are accounted for in pension trust funds using the flow of economic resources measurement focus and the accrual basis of accounting. Plan member contributions are recognized as revenue in the period in which the contributions are earned. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

The Washington State Investment Board (WSIB) has been authorized by statute (Chapter 43.33A of the RCW) as having the investment management responsibility for the pension funds. Investments are reported at fair value, and unrealized gains and losses are included as investment income in the Statement of Changes in Fiduciary Net Position presented in the DRS Comprehensive Annual Financial Report. Purchases and sales of investments are recorded on a trade-date basis.

DRS publishes an annual report for retirement plans which is available at http://www.drs.wa.gov/administration/annual-report/

### *(c) Actuarial Assumptions*

The total pension liability for each plan was determined by an actuarial valuation as of June 30, 2013, with the results rolled forward to June 30, 2014. The following actuarial assumptions have been applied to all prior periods included in the measurement:

| | |
|---|---|
| Inflation | 3.0% total economic inflation, 3.75% salary inflation |
| Salary increase | Expected to grow by promotions and longevity in addition to the salary inflation assumption |
| Investment rate of return | 7.50% |

Mortality rates were based on the RP-2000 Combined Healthy Table and Combined Disabled Table published by the Society of Actuaries. The Washington State Office of the State Actuary (OSA) applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100% Scale BB. Mortality rates are applied on a generational basis, meaning members are assumed to receive additional mortality improvements in each future year, throughout their lifetime.

The actuarial assumptions used in the June 30, 2013 valuation were based on the results of OSA's 2007–2012 Experience Study. Additional assumptions for subsequent events and law changes are current as of the 2013 actuarial valuation report.

***(d) Discount Rate***

The discount rate used to measure the total pension liabilities was 7.50% for all plans in which the University participates. To determine the discount rate, an asset sufficiency test was completed to test whether each pension plan's fiduciary net position was sufficient to make all projected future benefit payments of current plan members. Consistent with current law, the completed asset sufficiency tests for PERS included an assumed 7.70% long-term discount rate to determine funding liabilities for calculating future contribution rate requirements.

Consistent with the long-term expected rate of return, a 7.50% future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue to be made at contractually required rates (including the component of PERS 2/3 employer rates pertaining to the unfunded actuarial accrued liability for PERS 1 as provided for in Chapter 41.45 of the RCW).

Based on those assumptions, the fiduciary net position for each pension plan was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.50% on pension plan investments was applied to determine the total pension liability.

***(e) Sensitivity of the Net Pension Liability to Changes in the Discount Rate***

The following table presents the net pension liability of HFS calculated using the discount rate of 7.50%, as well as what the employer's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50%) or 1-percentage-point higher (8.50%) than the current rate.

**Discount rate sensitivity**
**Net pension liability**
(Dollars in thousands)

| Plan | | 1% Decrease | Current discount rate | 1% Increase |
|---|---|---|---|---|
| PERS 1 | $ | 6,319 | 5,126 | 4,103 |
| PERS 2/3 | | 10,555 | 2,531 | (3,599) |

***(f) Long-Term Expected Rate of Return***

The long-term expected rate of return of 7.50% on pension plan investments was determined by the WSIB. The rate approximately equals the median of the simulated investment returns over a fifty-year time horizon, increased slightly to remove WSIB's implicit, small, short-term downward adjustment due to assumed mean reversion. WSIB's implicit short-term adjustment, while small and appropriate over a 10- to 15-year period, becomes amplified over a 50-year measurement period.

The long-term expected rate of return was determined by the WSIB using a building-block method in which a best-estimate of expected future rates of return (expected returns, net of pension plan investment expense, but including inflation) are developed for each major asset class by the WSIB. Those expected returns make up one component of WSIB's Capital Market Assumptions (CMAs).

The CMAs contain three pieces of information for each class of assets the WSIB currently invest in:

- Expected annual return
- Standard deviation of the annual return
- Correlations between the annual returns of each asset class with every other asset class

WSIB uses the CMAs and their target asset allocation to simulate future investment returns over various time horizons.

Best estimates of arithmetic real rates of return for each major asset class included in the target asset allocation for each pension plan, as of June 30, 2014, are summarized in the following table:

| Asset class | Target allocation | Long-term expected real rate of return |
|---|---|---|
| Fixed income | 20.00% | 0.80% |
| Tangible assets | 5.00 | 4.10 |
| Real estate | 15.00 | 5.30 |
| Global equity | 37.00 | 6.05 |
| Private equity | 23.00 | 9.05 |

The inflation component used to create the above table is 2.70%, and represents WSIB's most recent long-term estimate of broad economic inflation.

### *(g) Employer Contribution Rates*

Employer contribution rates are developed in accordance with Chapter 41.45 of the RCW by the OSA, and include an administrative expense component that is currently set at 0.18%. The statute provides authority to the Pension Funding Council to adopt changes to economic assumptions and contribution rates.

### *(h) HFS Proportionate Share*

Collective pension amounts are determined as of a measurement date, which can be no earlier than an employer's prior fiscal year. The measurement date for the net pension liabilities recorded by HFS as of June 30, 2015 was June 30, 2014. University contributions received and processed by DRS during the fiscal year ended June 30, 2014 have been used as the basis for determining the University's proportionate share of the collective pension amounts reported by DRS in their June 30, 2014 Schedules of Employer and Nonemployer Allocations for all plans in which the University participates.

HFS's proportionate share for the year ended June 30, 2015 was determined by the proportion of HFS's employer contributions to total employer contributions as of the measurement date:

| Plan | Proportionate share for year ended June 30, 2015 |
|---|---|
| PERS 1 | 0.10176 % |
| PERS 2/3 | 0.12518 % |

### *(i) HFS Aggregated Balances*

HFS' aggregated balances of net pension liabilities and deferrals as of June 30, 2015 are presented in the table below.

| | | Net pension liability | Deferred outflows | Deferred inflows |
|---|---|---|---|---|
| | | | (Dollars in thousands) | |
| June 30, 2015: | | | | |
| PERS 1 | $ | 5,126 | 505 | 641 |
| PERS 2/3 | | 2,531 | 761 | 2,682 |
| Total | $ | 7,657 | 1,266 | 3,323 |

### *(j) PERS Plan 1*

PERS Plan 1 is closed to new entrants.

**Vesting**

PERS Plan 1 members were vested after the completion of five years of eligible service.

**Benefits Provided**

PERS Plan 1 provides retirement, disability, and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service.



(Continued)

The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service.

Members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and nonduty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### Contributions

The PERS Plan 1 employer contribution rate for the fiscal year ended June 30, 2015 was 9.21%. HFS' contributions to PERS Plan 1 for the year ended June 30, 2015 was $505,000.

### Proportionate share of PERS Plan 1 Pension Expense and Deferrals Related to Pensions

HFS' proportionate share of PERS Plan 1 pension expense for the fiscal year ended June 30, 2015 was $598,000, and is reported on the Statement of Revenue, Expenses, and Changes in Net Position in benefits expense.

HFS' deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 1 as of June 30, 2015 are presented in the following table:

| Description | | Deferred outflows of resources | Deferred inflows of resources |
|---|---|---|---|
| | | (Dollars in thousands) | |
| Difference between projected and actual earnings on pension plan investments, net | $ | — | 641 |
| HFS' pension plan contributions subsequent to the measurement date of collective net pension liability | | 505 | — |
| Total | $ | 505 | 641 |

Deferred outflows of resources related to HFS' contributions subsequent to the measurement date, of $505,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred inflows of resources pertaining to PERS Plan 1 will be recognized in pension expense as follows:

| | | |
|---|---|---|
| Year ending (dollars in thousands): | | |
| 2016 | $ | (160) |
| 2017 | | (160) |
| 2018 | | (160) |
| 2019 | | (161) |
| 2020 | | — |
| Thereafter | | — |
| Total | $ | (641) |

### *(k) PERS Plan 2/3*

**Vesting**

PERS Plan 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined-benefit portion of their plan after ten years of service, or after five years of service if twelve months of that service are earned after age 44.

**Benefits Provided**

PERS Plan 2/3 provides retirement, disability, and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2, and one percent of AFC times the member's years of service for Plan 3.

The AFC is the monthly average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at age 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age, for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 2, 2013:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other PERS Plan 2/3 benefits include duty and nonduty disability payments, a cost-of-living allowance (based on the Consumer Price Index), capped at three percent annually, and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

**Contributions**

The PERS Plan 2/3 employer contribution rate for the fiscal year ended June 30, 2015 was 9.21%. The Plan 2/3 employer rate includes a component to address the PERS Plan 1 unfunded actuarial accrued liability. HFS' contributions to PERS Plan 2/3 for the year ended June 30, 2015 was $603,000 as determined by rates established in accordance with RCW 41.45.

**Proportionate Share of PERS Plan 2/3 Pension Expense and Deferrals Related to Pensions**

HFS' proportionate share of PERS Plan 2/3 pension expense for the fiscal year ended June 30, 2015 was $451,000, and is reported on the Statement of Revenue, Expenses, and Changes in Net Position in benefits expense.

HFS' deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 as of June 30, 2015 are presented in the following table:

| Description | | Deferred outflows of resources | Deferred inflows of resources |
|---|---|---|---|
| | | (amounts in thousands) | |
| Difference between projected and actual earnings on plan investments, net | $ | — | 2,682 |
| Change in HFS' proportion | | 158 | — |
| HFS's contributions to plans subsequent to the measurement date of collective net pension liability | | 603 | — |
| Total | $ | 761 | 2,682 |

Deferred outflows of resources related to University contributions subsequent to the measurement date of $603,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 will be recognized in pension expense as follows:

| | | |
|---|---|---|
| Year ending (amounts in thousands): | | |
| 2016 | $ | (625) |
| 2017 | | (625) |
| 2018 | | (625) |
| 2019 | | (649) |
| 2020 | | — |
| Thereafter | | — |
| Total | $ | (2,524) |

## (7) University of Washington Retirement Plan and University of Washington Supplemental Retirement Plan

The University offers the University of Washington Retirement Plan (UWRP), a defined contribution plan with supplemental payment to beneficiaries, when required. The ILP is allocated a cost for the participation of this plan. The cost is included in the benefits load rate set by the University in calculating its fringe benefit expense and is applied on a per employee basis and is not a significant dollar amount.

### *(a) University of Washington Retirement Plan (403(b))*

Faculty, librarians, and professional staff are eligible to participate in the University of Washington Retirement Plan, a 403(b) defined-contribution plan administered by the University.

*403(b) Plan Description* – Contributions to the plan are invested by participants in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations. Benefits from the plan are available upon separation or retirement at the member's option. RCW 28B.10.400 et. seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

The number of participants in the 403(b) plan for the year ended June 30, 2015 was 15,415.

*403(b) Plan Funding Policy* – Employee contribution rates, based on age, are 5%, 7.5%, or 10% of salary. The University matches the contributions of employees. Within parameters established by the legislature, $105.3 million contribution requirements may be established or amended by the University of Washington Board of Regents. Employee and employer contributions for the years ended June 30, 2015 were $105.3 million.

### *(b) University of Washington Supplemental Retirement Plan (401(a))*

The University of Washington Supplemental Retirement Plan (UWSRP), a 401(a) defined-benefit retirement plan, operates in tandem with the 403(b) plan and is closed to new participants.

The Unfunded Actuarial Accrued Liability (UAL) and Annual Required Contribution (ARC) as of July 1 of the respective years were:

| | | 2015 | 2013 |
|---|---|---|---|
| | | (Dollars in thousands) | |
| UAL | $ | 373,711 | 292,535 |
| Normal cost | $ | 14,250 | 9,529 |
| Amortization of UAL, including interest | | 38,807 | 29,021 |
| ARC | $ | 53,057 | 38,550 |

| | | 2015 | 2013 |
|---|---|---|---|
| | | (Dollars in thousands) | |
| Actuarial assumptions: | | | |
| Payroll covered by Plan | $ | 1,050,000 | 1,047,000 |
| Rate of return assumption | | 4.00% | 4.25% |
| Salary increases for years 1 and 2 | | 3.75% | 3.00% |
| Salary increase for third year | | 3.75% | 3.00% |
| Salary increases thereafter | | 3.75% | 3.00% |

The UAL and ARC were established using the entry age normal cost method.

The following table reflects the activity in the Net Pension Obligation for the years ended June 30, 2015 and 2014:

| | | 2015 | 2014 |
|---|---|---|---|
| | | (Dollars in thousands) | |
| Balance at beginning of fiscal year | $ | 198,895 | 163,372 |
| ARC | | 53,057 | 38,550 |
| Payments to beneficiaries | | (3,766) | (3,027) |
| Balance at end of fiscal year | $ | 248,186 | 198,895 |

*401(a) Plan Description* – This plan provides for a supplemental payment component, which guarantees a minimum retirement benefit based upon a one-time calculation at each eligible participant’s retirement date. The University makes direct payments to qualifying retirees when the retirement benefits provided by the 403(b) plan do not meet the benefit goals.

*401(a) Plan Funding Policy* – The University received an actuarial valuation of the UWSRP with a valuation date of July 1, 2015. The previous evaluation was performed in 2013. The University has set aside $188.9 million as of June 30, 2015 for this liability. These funds do not meet the GASB technical definition of "Plan Assets" since they have not been segregated and restricted in a trust, or equivalent arrangement. The UAL shown in the table above, therefore, does not reflect a credit for these amounts.

## (8) Other Postemployment Benefits (OPEB)

The University funds OPEB obligations at a university-wide level on a pay-as-you-go basis. Disclosure information, as required under GASB Statement No. 45 (GASB 45), *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, does not exist at the Department level, and as a result, the Actuarial Accrued Liability (AAL) is not available for auxiliary entities. The University is ultimately responsible for the obligation; therefore, the (ARC) is not recorded on the Department's financial statements.

## (9) Subsequent Event

A capital contribution in September 2015 resulted from the transfer of the Lander, Terry, and Maple building garages from Housing and Food Services to Commuter Services. This is the final part of a Memorandum of Understanding dated June 2009 as part of the Master Plan.

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**

(A Department of University of Washington)

Schedules of Required Supplementary Information (Unaudited)

June 30, 2015

The Schedules of Required Supplementary Information below reflect information for the University of Washington as a whole due to the constraints of available information for the University of Washington Housing and Food Services.

**Schedule of the University's Proportionate Share of the Net Pension Liability**
**PERS 1 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| University's proportion of the net pension liability (asset) | | 8.28243% |
| University's proportionate share of the net pension liability (asset) | $ | 417,231 |
| University's covered-employee payroll | | 25,376 |
| University's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll | | 1,644.20% |
| Plan fiduciary net position as a percentage of the total pension liability | | 61.19 |

**Schedule of the University's Contributions**
**PERS 1 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| Contractually required contribution | $ | 2,311 |
| Contributions in relation to the contractually required contribution | | 2,313 |
| Contribution deficiency (excess) | | (2) |
| University's covered-employee payroll | | 25,376 |
| Contributions as a percentage of covered-employee payroll | | 9.11% |

**Schedule of the University's Proportionate Share of the Net Pension Liability**
**Pers 2/3 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| University's proportion of the net pension liability (asset) | | 10.004398% |
| University's proportionate share of the net pension liability (asset) | $ | 202,225 |
| University's covered-employee payroll | | 856,839 |
| University's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll | | 23.60% |
| Plan fiduciary net position as a percentage of the total pension liability | | 93.29 |



(Continued)

**UNIVERSITY OF WASHINGTON**
**HOUSING AND FOOD SERVICES**

(A Department of University of Washington)

Schedules of Required Supplementary Information (Unaudited)

June 30, 2015

## Schedule of the University's Contributions PERS 2/3 Pension Plan

(Dollar amounts in thousands)

| | | |
|---|---|---|
| Contractually required contribution | $ | 78,164 |
| Contributions in relation to the contractually required contribution | | 78,160 |
| Contribution deficiency (excess) | | 4 |
| University's covered-employee payroll | | 856,839 |
| Contributions as a percentage of covered-employee payroll | | 9.12% |

**Notes to Schedules of Required Supplementary Information (Unaudited) for the Year Ended June 30, 2015**

*Changes of Benefit Terms:* Amounts reported in 2015 reflect no change in benefit terms.

*Changes of Assumptions:* Amounts reported in 2015 reflect no changes in assumptions.

**STUDENT SERVICES AND FACILITIES FEES – SEATTLE CAMPUS**

**ADMINISTERED BY THE DIVISION OF STUDENT LIFE OF THE UNIVERSITY OF WASHINGTON**

FINANCIAL REPORT

JUNE 30, 2015

## C O N T E N T S

petersonsullivan LLP
Certified Public Accountants
& Advisors

# INDEPENDENT AUDITORS' REPORT

To the Board of Regents
University of Washington
Seattle, Washington

We have audited the accompanying statements of cash receipts, cash disbursements, and changes in cash balances of Student Services and Facilities Fees – Seattle Campus administered by the Division of Student Life of the University of Washington for the years ended June 30, 2015 and 2014, and the related notes to the financial statements.

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

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the cash basis of accounting described in Note 1; this includes determining that the cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

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

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

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

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Seattle, WA 98101
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**Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the cash receipts, cash disbursements, and changes in cash balances of the Student Services and Facilities Fees – Seattle Campus administered by the Division of Student Life of the University of Washington for the years ended June 30, 2015 and 2014, on the cash basis of accounting described in Note 1.

**Basis of Accounting**

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. These statements are prepared on the cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States. Our opinion is not modified with respect to that matter.

Peterson Sullivan L.L.P.

October 27, 2015

**STUDENT SERVICES AND FACILITIES FEES – SEATTLE CAMPUS**
**ADMINISTERED BY**
**THE DIVISION OF STUDENT LIFE**
**OF THE UNIVERSITY OF WASHINGTON**

STATEMENTS OF CASH RECEIPTS, CASH DISBURSEMENTS,
AND CHANGES IN CASH BALANCES

For the Years Ended June 30, 2015 and 2014

| | 2015 | 2014 |
|---|---|---|
| Cash Receipts | | |
| Student services and facilities fees - Seattle campus | $ 28,793,470 | $ 28,552,055 |
| Interest income | 443,550 | 382,317 |
| Total cash receipts | 29,237,020 | 28,934,372 |
| Debt Service | | |
| Principal - ILP - IMA Bonds | (1,559,167) | (1,490,417) |
| Principal - ILP - Student Facilities Renovation | (1,806,248) | (1,636,526) |
| Interest - ILP - IMA Bonds | (1,859,979) | (1,933,000) |
| Interest - ILP - Student Facilities Renovation | (6,040,509) | (6,279,331) |
| Total debt service payments | (11,265,903) | (11,339,274) |
| Cash receipts available after debt service | 17,971,117 | 17,595,098 |
| Other Cash Disbursements | | |
| Hall Health Center | 6,487,060 | 6,475,060 |
| Recreational Sports Operations | 2,183,171 | 2,041,053 |
| Student Parent Resource Center | 1,503,500 | 1,413,369 |
| Associated Students of the University of Washington | 917,602 | 822,474 |
| Student Activities and Union Facilities | 879,795 | 725,595 |
| Ethnic Cultural Center and Theatre Complex | 833,200 | 651,763 |
| Student Counseling Center | 546,246 | 493,549 |
| Graduate and Professional Student Senate | 405,060 | 381,909 |
| Campus Sustainability Fund | 370,000 | 333,605 |
| Student Publications | 306,930 | 266,435 |
| Q-Center | 269,622 | 247,276 |
| Student Legal Services | 183,984 | 171,884 |
| Classroom Support Services | 131,904 | 100,000 |
| D-Center | 37,500 | 37,673 |
| Peer Health Education Group | 37,048 | 23,273 |
| Services and Activities Committee Operations | 33,464 | 28,034 |
| Total other cash disbursements | 15,126,086 | 14,212,952 |
| Cash receipts in excess of other cash disbursements | 2,845,031 | 3,382,146 |
| Transfers: | | |
| Transfer to Student Publications | (615,000) | |
| Other transfers | | (692,176) |
| Return of unspent funds | 387,812 | |
| Total Transfers | (227,188) | (692,176) |
| **Change in cash balances** | **2,617,843** | **2,689,970** |
| Cash Balance, beginning of year | 20,754,604 | 18,064,634 |
| Cash Balance, end of year | $ 23,372,447 | $ 20,754,604 |

See Notes to Financial Statements

## NOTES TO FINANCIAL STATEMENTS

### Note 1. Organization and Significant Accounting Policies

**Organization**

The Division of Student Life ("Student Life") is a unit within the University of Washington ("the University") and is responsible for a variety of programs, services, facilities, and operations supporting the student experience on campus, including housing, food services, recreational sports programs, student government, the Husky Union Building, student conduct, counseling, health & wellness, disability resources, career services, student publications, fraternity and sorority life, the Q-center, ceremonies, and the University's police department. Student Life administers the allocation and expenditure of certain fees collected from students on the Seattle campus called "Student Services and Facilities Fees." Student Services and Facilities Fees are a portion of the total fees collected from students. Student Services and Facilities Fees include Services and Activities Fees, Intramural Bond Fees, and Student Facilities Renovation Fees.

The Student Services and Facilities Fees are first used to pay debt service on current and future bonds, and debt obtained from the University's Internal Lending Program ("ILP"), and are then used to support programs recommended by the Services and Activities Fee Committee ("SAF Committee") and approved by the Board of Regents of the University ("the Board of Regents"). The Services and Activities Fees are student levied, student distributed fees to support and enhance the out-of-class experience of students at the University. The Services and Activities Fees provide ongoing operational and capital funding for programs which protect and enrich the cultural, emotional, intellectual, physical, and social well-being of the student. Each academic quarter, Student Services and Facilities Fees are charged to full-time and part-time students registered at the University.

As a part of the University, Student Services and Facilities Fee activity is exempt from income taxes and no tax return is filed. Student Services and Facilities Fee activity receives administrative support from the University without charge.

These financial statements only present a selected portion of the activities of the University. As such, they are not intended and do not present either the financial position, results of operations, or changes in net position of the University.

**Change in Reporting Entity**

In the year ended June 30, 2014, the reporting entity structure for Student Services and Facilities Fees was changed to include the SAF Committee Expenditure Fund in the cash balances presented in the Statements of Cash Receipts, Cash Disbursements, and Changes in Cash Balances. The SAF Committee Expenditure Fund was a capital allocation reserve fund comprised of student services and activities fees set aside for subsequent allocation to capital projects as recommended by the SAF Committee and approved by the Board of Regents. This budget unit was included in the reporting entity to more closely reflect student services and facilities fees which remain under the oversight and control of the SAF Committee. During the year ended June 30, 2015, the SAF Committee voted to close the SAF Committee Expenditure Fund.

**Financial Statement Presentation**

These financial statements are prepared on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States. Accordingly, revenue is recognized when cash is received and expenses are recognized when cash is disbursed.

**Cash Receipts**

All cash receipts are deposited with the University. Funds held by the University are funds invested in pooled investments with the University. The University combines most short-term available cash balances from various departments into the invested funds pool, which is primarily comprised of U.S. government and agency securities, mortgage rated investments, and asset backed securities, as well as units in the Consolidated Endowment Fund ("CEF"), which is a diversified investment fund. The underlying investments in CEF include emerging market equity securities, developed market equity securities, and fixed income securities.

The University annually allocates investment earnings to the departments with qualifying funds in the invested funds pool based on relative amount invested at a rate determined and approved by the University. For the years ended June 30, 2015 and 2014, the rate determined by the University was 2.0%. Principal amounts invested in the invested funds pool are guaranteed by the University.

**Transfers**

In June 2014, the SAF Committee signed a memorandum of understanding with Student Publications to allocate $615,000 from the SAF General Fund in order to fund a majority of Student Publications' historical operating deficit. Accordingly, during the year ended June 30, 2015, $615,000 was transferred to Student Publications. The amount is to be repaid over a period of time to be determined by Student Publications' ability to repay the debt (not to exceed thirty years). During the year ended June 30, 2015, no repayments were made.

During the year ended June 30, 2015, the SAF Committee required the Student Parent Resource Center to return $330,000 of unspent Services and Activities Fees and grant funds to the SAF General Fund. Additionally, approximately $58,000 in unspent innovation funds from various units were returned to the SAF General Fund during fiscal year 2015.

**Note 2. Uncollected Fees and Future Disbursements**

As these financial statements are presented on the cash basis of accounting, receivables and payables are not recognized.

Student Life had Student Services and Facilities Fees that were uncollected (and are, therefore, receivable) of approximately $1,127,172 and $986,358 at June 30, 2015 and 2014, respectively.

In June 2015, the Board of Regents accepted proposed disbursements for the year ending June 30, 2016, totaling $16,313,000.

## Note 3. Internal Lending Program – IMA Bonds

Student Services and Facilities Fees are used to make semi-annual debt service payments on the Series 2005 Revenue Bonds issued by the University. In 2015, these bonds were refinanced with General Revenue Bonds issued by the University and the debt was transferred to the University's internal debt portfolio managed by the ILP. The ILP requires varying annual principal and interest payments, with the final payment due in June 2030. The principal amount of the debt outstanding was $35,640,416 at June 30, 2015, with interest at 4.75%. The ILP funds its payments through the revenues of Student Services and Facilities Fees (specifically the IMA bond fees).

The following is a summary of future payments (principal and interest) to be paid to cover the debt service payments for the years ending June 30:

| | Principal | Interest | Total |
|---|---|---|---|
| 2016 | 1,638,333 | 1,782,021 | 3,420,354 |
| 2017 | 1,718,333 | 1,700,104 | 3,418,437 |
| 2018 | 1,807,500 | 1,614,188 | 3,421,688 |
| 2019 | 1,897,500 | 1,523,813 | 3,421,313 |
| 2020 | 1,992,083 | 1,428,938 | 3,421,021 |
| 2021 - 2025 | 11,558,750 | 5,547,292 | 17,106,042 |
| 2026 - 2030 | 15,027,917 | 2,367,124 | 17,395,041 |
| | $ 35,640,416 | $ 15,963,480 | $ 51,603,896 |

## Note 4. Internal Lending Program – Student Facilities Renovation

In July 2009, the Board of Regents approved the renovation of the Husky Union Building, the Hall Health Center, and the Ethnic Cultural Center. A majority of the money to fund the renovation was borrowed from the University's Internal Lending Program (a program sponsored by the University to consolidate borrowing activities by University departments).

On behalf of the SAF Committee, Student Life has borrowings available from the University Internal Lending Program of $126,000,000, $8,000,000, and $16,000,000 for the Husky Union Building, the Hall Health Center, and the Ethnic Cultural Center, respectively. At June 30, 2015, the outstanding balances on these borrowings were $92,783,886, $6,732,554, and $13,939,072 for the Husky Union Building, the Hall Health Center, and the Ethnic Cultural Center, respectively, all bearing interest at 4.75%. The interest rate is reviewed each year and is subject to adjustment by the Board of Regents, and as such, in April 2015, was adjusted from 5.5% to 4.75%. Loan payments began in October 2011 for the Hall Health Center with a 30-year amortization and term. Loan payments began in October 2012 for the Husky Union Building and the Ethnic Cultural Center, also with 30-year amortizations and terms. The renovation activity is not included in these financial statements.

Borrowings are being repaid by the Student Facilities Renovation Fees, which are included in the student services and facilities fees cash receipts at both June 30, 2015 and 2014.

The following is a summary of future payments (principal and interest) to be paid to the University to cover the debt service payments for the years ending June 30:

| | Principal | Interest | Total |
|---|---|---|---|
| 2016 | 2,095,289 | 5,343,911 | 7,439,200 |
| 2017 | 2,197,011 | 5,242,189 | 7,439,200 |
| 2018 | 2,303,671 | 5,135,529 | 7,439,200 |
| 2019 | 2,415,509 | 5,023,691 | 7,439,200 |
| 2020 | 2,532,777 | 4,906,423 | 7,439,200 |
| 2021 - 2025 | 14,632,124 | 22,563,877 | 37,196,001 |
| 2026 - 2030 | 18,545,933 | 18,650,067 | 37,196,000 |
| 2031 - 2035 | 23,506,612 | 13,689,389 | 37,196,001 |
| 2036 - 2040 | 29,794,175 | 7,401,825 | 37,196,000 |
| 2041 - 2043 | 15,432,411 | 856,570 | 16,288,981 |
| | $ 113,455,512 | $ 88,813,471 | $ 202,268,983 |

The ratio of cash receipts to all debt service payments (bonds and Internal Lending Program debt) for the years ended June 30 were as follows:

| | |
|---|---|
| 2014 | 2.6 to 1 |
| 2015 | 2.6 to 1 |

**Note 5. Subsequent Events**

Student Services and Facilities Fees has evaluated subsequent events through the date these financial statements were available to be issued, which was October 27, 2015.

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

Financial Statements

June 30, 2015

(With Independent Auditors' Report Thereon)

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

## Table of Contents

KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

# Independent Auditors' Report

The Board of Regents
University of Washington:

We have audited the accompanying financial statements of the University of Washington Commuter Services (Unit or CS), which comprise the statement of net position as of June 30, 2015, and the related statement of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements.

## Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

## Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 financial statements are free from material misstatement.

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

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

As discussed in note 1 to the financial statements, the financial statements of the Unit, an auxiliary enterprise within the University of Washington (the University), are intended to present the financial position, the changes in financial position, and cash flows of only the respective portion of the business-type activities of the University that is attributable to the transactions of the Unit. They do not purport to, and do not, present fairly the financial position of the University as of June 30, 2015, the changes in its financial position or its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

KPMG

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington Commuter Services as of June 30, 2015, and the changes in its net position and its cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.

## Other Matter

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 8, and the schedules of required supplementary information on pages 29 through 30, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### *Emphasis of Matter*

As discussed in note 1 to the financial statements, on July 1, 2014, the Unit adopted new accounting guidance requiring governments providing defined-benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, as well as recognizing most changes in the net pension liability within pension expense. Our opinion is not modified with respect to this matter.

KPMG LLP

Seattle, Washington
November 10, 2015

## Discussion and Analysis Prepared by Management

The following discussion and analysis provides an overview of the financial position and activities of the University of Washington Commuter Services (CS) for the years ended June 30, 2015 and 2014. This discussion has been prepared by management and should be read in conjunction with the financial statements and accompanying notes, which follow this section.

## Using the Financial Statements

CS's financial statements include the statements of net position, statements of revenues, expenses, and changes in net position, statements of cash flows, and notes to financial statements. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities. The financial health of CS can be measured by reviewing the summaries and explanations that follow.

## Statements of Net Position Summary

The statements of net position in the financial statements reflect the financial condition of CS at the end of the year and report the various categories of all assets and liabilities. The following statement of net position summary show CS's total assets, total liabilities, and net position as of June 30, 2015 and 2014:

**Statements of Net Position Summary**

| | | 2015 | 2014 |
|---|---|---|---|
| Current assets | $ | 4,736,773 | 4,194,862 |
| Noncurrent assets: | | | |
| Capital assets, net | | 45,544,554 | 48,989,956 |
| Other noncurrent assets | | 14,257,092 | 11,839,214 |
| Total assets | | 64,538,419 | 65,024,032 |
| Pension deferred outflows of resources | | 263,995 | — |
| Total assets and deferred outflows of resources | $ | 64,802,414 | 65,024,032 |
| Current liabilities | $ | 1,797,271 | 1,814,978 |
| Noncurrent liabilities | | 14,206,468 | 13,205,602 |
| Total liabilities | | 16,003,739 | 15,020,580 |
| Pension deferred inflows of resources | | 677,575 | — |
| Net position | | 48,121,100 | 50,003,452 |
| Total liabilities, deferred inflows of resources, and net position | $ | 64,802,414 | 65,024,032 |



(Continued)

Following are comments about the changes highlighted by the statements of net position summary:

- Current assets consist of cash, accounts receivable, current portion of internal note receivable, and prepaid expenses. Current assets were $2.9 million, and $2.4 million greater than current liabilities at the end of fiscal years 2015, and 2014, respectively. The 2015 increase of $560 thousand or 24% was caused by an increase in cash resulting from a slight increase in parking volume and an increase in accounts receivable primarily due to payment in transit from Commute Options – Active Transportation for the Burke Gilman Trail.
- Noncurrent assets consist of due from University, internal note receivable, capital assets, and advances to University of Washington (the University) for capital projects. Noncurrent assets decreased by $1.0 million or 2% in 2015. The 2015 decrease was primarily because of a new internal note receivable of $6.6 million offset by a $3.9 million decrease in advances to the University for capital projects. Additionally, an increase of $1.2 million of capital asset additions offset by $2.2 million of depreciation and $2.5 million of adjustments to construction in progress related to the transfer out of the Burke Gilman Trail project to Commute Options – Active Transportation due to the timing of projects compared to 2014.
- Deferred outflows are $264 thousand and are new this year as a result of implementing GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*.
- Current liabilities decreased by $18 thousand or 1% during fiscal year 2015 and are materially remained unchanged from 2014.
- Noncurrent liabilities increased by $1.0 million or 8% in fiscal year 2015. The 2015 increase was due to $1.6 million for the net pension liability for GASB 68 implementation offset by the $602,000 moving into the current portion of Internal Lending Program payable due to a 2016 principal payment.
- Deferred inflows are $678 thousand and are new this year as a result of implementing GASB 68.
- The change in net position measures whether the overall financial condition has improved or deteriorated during the year. Total net position decreased by $2.2 million or 4% during fiscal year 2015. The 2015 decreases are mostly due to the adjustments to construction in progress related to the transfer out of the Burke Gilman Trail project to Commute Options – Active Transportation in 2015.

**Net Position**

The following table is a summary of the net position for CS at June 30, 2015, and 2014:

**Net Position Summary**

| | | **2015** | **2014** |
|---|---|---|---|
| Net investment in capital assets | $ | 32,060,848 | 35,207,103 |
| Unrestricted | | 16,060,252 | 14,796,349 |
| Total net position | $ | 48,121,100 | 50,003,452 |

The categories of net position listed in the table above are defined as follows:

- "Net investment in capital assets" is CS's total investment in property, plant, equipment and infrastructure and unspent debt proceeds, net of accumulated depreciation, and any outstanding debt obligations related to those capital assets.
- "Unrestricted net position" is all other funds available to CS for any purpose. Unrestricted net position is often internally designated for specific purposes.

Following are comments about the changes in CS's net position summary:

- Net investment in capital assets decreased by $3.1 million or 9% in fiscal year 2015 to a total of $32.1 million. The balance decreases as CS's payable to the University's Internal Lending Program (ILP) are paid down offset by increases in depreciation and adjustments for construction in progress.
- Unrestricted net position increased by $1.3 million or 9%, in fiscal year 2015. The increase in 2015 was caused by the increase of operating revenue due to a slight increase in parking volume and a decrease in operating expenses.
- Implementation of GASB 68 resulted in the restatement of beginning unrestricted net position reducing it by $2.1 million.

**Capital Improvements and Related Debt**

- In fiscal year 2015, capital additions were $1.2 million, which included $2.1 million for Plant Services South parking lot offset by the refund of $1.1 million for the E 12 Parking Study because actual costs are expected to come in under budget.
- Total debt decreased from $13.8 million of outstanding principal due at the end of fiscal year 2014 to $13.2 million at the end of fiscal year 2015 as a result of scheduled principal payments.

**Statements of Revenues, Expenses, and Changes in Net Position**

The statements of revenues, expenses, and changes in net position present how CS's operations and nonoperating items resulted in changes in net position. In accordance with GASB reporting principles, revenues, and expenses are classified as either operating or nonoperating. The following summary shows the revenues, expenses, and changes in net position for the years ended June 30, 2015 and 2014.

**Revenues, Expenses, and Changes in Net Position Summary**

| | | 2015 | 2014 |
|---|---|---|---|
| Operating revenues | $ | 13,156,056 | 12,338,660 |
| Operating expenses | | (11,941,223) | (12,613,132) |
| Operating income (loss) | | 1,214,833 | (274,472) |
| Nonoperating expenses | | (151,112) | (363,130) |
| Other revenues and transfers | | (810,091) | 1,769,775 |
| Increase in net position | | 253,630 | 1,132,173 |
| Net position, beginning of year, as originally presented | | 50,003,452 | 48,871,279 |
| Effect of accounting and reporting entity changes | | (2,135,982) | — |
| Net position, end of year | $ | 48,121,100 | 50,003,452 |

**Revenues from All Sources**

The following table summarizes revenues from all sources for the years ended June 30, 2015 and 2014:

**Revenues from All Sources Summary**

| | | 2015 | 2014 |
|---|---|---|---|
| Parking revenue | $ | 11,221,627 | 10,406,575 |
| Fine revenue | | 869,448 | 814,225 |
| Reimbursement for football-related expenses | | 149,028 | 166,464 |
| Revenue from Triangle Garage | | 915,953 | 951,396 |
| Interest income | | 476,640 | 289,534 |
| Capital contribution | | — | 2,584,000 |
| Due from University | | 60,512 | — |
| Total revenue – all sources | $ | 13,693,208 | 15,212,194 |

Following are comments about the changes highlighted by the revenues from all sources summary:

- Parking revenue continues to be the largest source of revenue for CS. Parking revenue increased by $815 thousand or 8% in 2015 primarily due to an increase in volume and in 2014 there was a significant reimbursement to Intercollegiate Athletics (ICA) for construction-related parking.
- Fine revenue in 2015 increased $55 thousand or 7% from 2014 as a result of an increase in the number of citations issued and collected.

- Interest income in 2015 increased $187 thousand or 65% due to an increase in the average cash balance and the addition of a new note receivable. A portion of interest income represents interest earned from cash and cash equivalents in the University's Invested Funds Pool and advances to the University for capital projects. The new note receivable is with Commute Options – Active Transportation for the construction of the Burke Gilman Trail project.

**Expenses and Expense Transfers**

The following table summarizes expenses and expense transfers for the years ended June 30, 2015 and 2014:

**Expenses and Expense Transfers Summary**

| | | 2015 | 2014 |
|---|---|---|---|
| Salaries and wages | $ | 2,613,117 | 2,606,907 |
| Employee benefits | | 630,535 | 807,154 |
| Temporary services | | 234,886 | 61,386 |
| Maintenance | | 1,806,857 | 3,150,651 |
| Printing | | 90,407 | 63,613 |
| Outside services | | 343,441 | 243,543 |
| Utilities | | 326,392 | 267,973 |
| Data processing | | 179,665 | 224,030 |
| Motorpool | | 122,129 | 129,032 |
| Garage rental | | 35,488 | 35,248 |
| Insurance | | 23,435 | 23,401 |
| Supplies and materials | | 437,602 | 416,660 |
| Telephone | | 58,631 | 56,687 |
| Campus services | | 1,511,221 | 1,443,423 |
| Miscellaneous | | 285,859 | 95,144 |
| University overhead | | 1,064,797 | 991,250 |
| Depreciation | | 2,176,761 | 1,997,030 |
| Interest | | 627,752 | 652,664 |
| Total expenses | | 12,568,975 | 13,265,796 |
| Transfer to the University for UPASS | | 869,448 | 814,225 |
| Loss on disposal of equipment | | 1,155 | — |
| Total expense transfers | | 870,603 | 814,225 |
| Total expenses and expense transfers | $ | 13,439,578 | 14,080,021 |

Following are comments about the changes in expenses and expense transfers highlighted by the expenses and transfers summary:

- CS's expenses decreased by $697 thousand or 5% in fiscal year 2015. The decrease in 2015 is primarily due to a $1.3 million decrease in maintenance expense offset by increases in temporary services, miscellaneous, and depreciation expenses discussed below.
- CS's temporary services expense increased $174 thousand or 283% in fiscal year 2015. The increase was due to a significant number of retirements and the addition of a second maintenance shift.
- CS's maintenance expense decreased by $1.3 million or 43% in fiscal year 2015. The primary decrease in 2015 was the result of less work performed on painting and paving garages and parking lots.
- CS's outside services expense increased by $100 thousand or 41% in fiscal year 2015. The increase in 2015 is the result of an increase in the use of an outside contractor for a new parking gate access system.
- CS's campus services expense increased by $68 thousand or 5% in fiscal year 2015. The increase in 2015 is due to general increases in shared services expenses.
- CS's miscellaneous expense increased by $191 thousand or 200% in fiscal year 2015. The increase is due to consulting services for a condition assessment of parking lots and garages.
- CS's depreciation expense increased by $180 thousand or 9% in fiscal year 2015, because of the capital asset additions in the fiscal year.
- CS's transfer to the University for UPASS increased by $55 thousand, or 7% in fiscal 2015. The fine revenue in 2015 was used to support the UPASS program. The UPASS program is operated by the University's Commute Options Group and provides a package of flexible, low cost transportation choices for faculty, staff, and students. It includes unlimited access to public transit, and a parking management component that subsidizes carpool and vanpool parking rather than single occupant vehicles.

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

Statement of Net Position

June 30, 2015

**Assets and Deferred Outflows of Resources**

| | | |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents in the University of Washington Invested Funds Pool (note 2) | $ | 3,985,880 |
| Note receivable, current portion (note 3) | | 107,266 |
| Accounts receivable | | 609,562 |
| Prepaid expenses | | 34,065 |
| Total current assets | | 4,736,773 |
| Noncurrent assets: | | |
| Due from University | | 11,331 |
| Note receivable, net of current portion (note 3) | | 6,629,581 |
| Advances to University for capital projects | | 7,616,180 |
| Capital assets (less accumulated depreciation of $41,922,865) (note 4) | | 45,544,554 |
| Total noncurrent assets | | 59,801,646 |
| Total assets | | 64,538,419 |
| Pension deferred outflows of resources (note 8) | | 263,995 |
| Total assets and deferred outflows of resources | $ | 64,802,414 |

**Liabilities, Deferred Inflows of Resources, and Net Position**

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | $ | 575,866 |
| Accrued salaries and vacation payable | | 403,827 |
| Unearned revenue | | 215,327 |
| Internal lending program payable, current portion (note 6) | | 602,251 |
| Total current liabilities | | 1,797,271 |
| Noncurrent liabilities: | | |
| Internal lending program payable, net of current portion (note 6) | | 12,603,351 |
| Net Pension Liability (note 8) | | 1,603,117 |
| Total noncurrent liabilities | | 14,206,468 |
| Total liabilities | | 16,003,739 |
| Pension deferred inflows of resources (note 8) | | 677,575 |
| Net position: | | |
| Net investment in capital assets | | 32,060,848 |
| Unrestricted | | 16,060,252 |
| Total net position | | 48,121,100 |
| Total liabilities, deferred inflows of resources, and net position | $ | 64,802,414 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

Statement of Revenues, Expenses, and Changes in Net Position

Year ended June 30, 2015

| | |
|---|---|
| Operating revenues: | |
| Parking revenue | $ 11,221,627 |
| Fine revenue | 869,448 |
| Reimbursement for football-related expenses | 149,028 |
| Revenue from Triangle Garage | 915,953 |
| Total operating revenues | 13,156,056 |
| Operating expenses: | |
| Salaries and wages | 2,613,117 |
| Employee benefits | 630,535 |
| Temporary services | 234,886 |
| Maintenance | 1,806,857 |
| Printing | 90,407 |
| Outside services | 343,441 |
| Utilities | 326,392 |
| Data processing | 179,665 |
| Motorpool | 122,129 |
| Garage rental | 35,488 |
| Insurance | 23,435 |
| Supplies and materials | 437,602 |
| Telephone | 58,631 |
| Campus services | 1,511,222 |
| Miscellaneous | 285,858 |
| University overhead | 1,064,797 |
| Depreciation | 2,176,761 |
| Total operating expenses | 11,941,223 |
| Operating income | 1,214,833 |
| Nonoperating revenues (expenses): | |
| Interest income | 476,640 |
| Interest expense | (627,752) |
| Loss on disposal of equipment | (1,155) |
| Total net nonoperating expenses | (152,267) |
| Income before other revenues and transfers | 1,062,566 |
| Other revenues and (transfers): | |
| Transfer to the University for UPASS | (869,448) |
| Due from University | 60,512 |
| Total other revenues and transfers | (808,936) |
| Increase in net position | 253,630 |
| Net position: | |
| Net position at beginning of year, as restated (note1(b)) | 47,867,470 |
| Net position at end of year | $ 48,121,100 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

Statement of Cash Flows

Year ended June 30, 2015

| | |
|---|---|
| Cash flows from operating activities: | |
| Receipts from parking fees and fines | $ 11,979,096 |
| Receipts from reimbursement for football-related expenses | 149,028 |
| Receipts from Triangle Garage | 915,953 |
| Payments to suppliers | (5,515,300) |
| Payments to employees | (2,614,163) |
| Payments for benefits | (761,150) |
| Payments to the University for overhead | (1,064,797) |
| Net cash provided by operating activities | 3,088,667 |
| Cash flows from noncapital financing activities: | |
| Transfer to the University for UPASS | (869,448) |
| Other Transfers from the University | 60,512 |
| Net cash used in noncapital financing activities | (808,936) |
| Cash flows from capital and related financing activities: | |
| Payment to University for capital assets | (1,298,085) |
| Principal paid on bonds payable | (577,251) |
| Interest paid | (627,752) |
| Net cash used in capital and related financing activities | (2,503,088) |
| Cash flows from investing activities: | |
| Principal received on note receivable – internal | 51,756 |
| Interest income | 476,640 |
| Net cash provided by investing activities | 528,396 |
| Net increase in cash and cash equivalents | 305,039 |
| Cash and cash equivalents at beginning of year | 3,680,841 |
| Cash and cash equivalents at end of year | $ 3,985,880 |
| Reconciliation of operating income to net cash provided by operating activities: | |
| Operating income | $ 1,214,833 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | |
| Depreciation expense | 2,176,761 |
| Changes in assets and liabilities: | |
| Decrease in net pension liability | (738,887) |
| Increase in pension-related deferred outflows/inflows of resources | 619,603 |
| Increase in due from University | (11,331) |
| Increase in accounts receivable | (134,250) |
| Decrease in prepaid expenses | 4,645 |
| Decrease in accounts payable | (63,932) |
| Decrease in accrued salaries and vacation payables | (1,046) |
| Increase in unearned revenue | 22,271 |
| Net cash provided by operating activities | $ 3,088,667 |

See accompanying notes to financial statements.

## (1) Organization and Summary of Significant Accounting Policies

### *(a) Organization*

The University of Washington Commuter Services (Unit or CS), a unit of Facilities Services, is responsible for the operation of the parking facilities of the University of Washington (the University).

### *(b) Basis of Presentation*

The financial statements of the Unit have been prepared in accordance with the Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* as amended by GASB Statement No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. The Unit is reporting as a special-purpose government engaged in business-type activities (BTA). In accordance with BTA reporting, the Unit presents a management's discussion and analysis, statement of net position, statement of revenues, expenses, and changes in net position, statement of cash flows, and notes to the financial statements. The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. The Unit reports capital assets net of accumulated depreciation (as applicable), and reports depreciation expense in the statement of revenues, expenses, and changes in net position.

On July 1, 2014 CS adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This statement requires governments providing defined-benefit pensions to their employees to recognize their long-term obligation for pension benefits as a liability for the first time, along with the associated assets, which have been set aside to fund the plan. Since the University participates in several cost sharing pension plans which are administered by the state of Washington Department of Retirement Systems (DRS), this statement will require the University to recognize its proportionate share of the statewide net pension liability or net pension asset for each of the plans in which it participates. The Statement also eliminates the method of amortizing the liability balances over several years, and instead requires full recognition of the net liability upon implementation. Implementation of this standard resulted in the restatement of beginning unrestricted net position reducing it by $2,135,982. The University's proportionate share of the state's collective pension amounts are disclosed in note 8.

With the adoption of GASB Statement No. 68, net position was restated at July 1, 2014. Below is a reconciliation of the total net position as previously reported at June 30, 2014, to the restated net position:

| | | |
|---|---|---|
| Net position at June 30, 2014, as previously reported | $ | 50,003,452 |
| Effect of accounting and reporting entity changes | | (2,135,982) |
| Net position at July 1, 2014, as restated | $ | 47,867,470 |

### *(c) Internal Note Receivable*

Internal Note Receivable represents the amount owed by Commute Options – Active Transportation for the construction of the Burke Gilman Trail project. An Internal Note Receivable requires a signed agreement. The agreement is signed by the borrowing unit Assistant Director, the Administrative Services Group Assistant Director, and the Director of Transportation Services.

### *(d) Capital Assets*

Capital expenditures for facilities and equipment funded by the Unit are reflected as capital assets on the Unit's statements of net position. Buildings and equipment are stated at cost. Additions, replacements, major repairs, and renovations are capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 15–50 years for building components, 20–50 years for infrastructure and land improvements, and 5–7 years for equipment. Expenditures for equipment and repairs that represent normal replacement of such equipment and routine maintenance of the buildings are expensed as incurred.

### *(e) Advances to University for Capital Projects*

Advances to the University for capital projects represent the difference between the cash paid and the capital expenditures incurred by the University for various capital projects at year-end, which CS expects to use in capital expenditures or be refunded if not used in the future.

### *(f) Revenue Recognition*

Parking sales are recognized as revenue in the period when the parking is utilized.

The University Department of Intercollegiate Athletics (ICA) and CS entered into a formal written agreement whereby CS operates the parking for Husky football home games for ICA.

The University of Washington Medical Center (UWMC) and CS entered into a formal written agreement whereby UWMC operates the Triangle Garage for CS and pays the Net Operating Revenue from the Triangle Garage to CS. The Net Operating Revenue accrued per the Triangle Garage operating results is reported as CS's operating revenue.

*(g) Unearned Revenues*

Funds received from the sale of permits to be utilized for periods subsequent to June 30 are reported as unearned. Permit sales are recognized as revenue in the period when the parking is utilized. At June 30, 2015, unearned revenues were $215,327.

*(h) Federal Income Taxes*

As a part of the University, the Commuter Services is exempt from federal income taxes, except to the extent of unrelated business taxable income. Commuter Services did not incur unrelated business income tax during fiscal year 2015, and accordingly, the financial statements do not include a provision for federal income taxes.

**(2) Cash and Cash Equivalents in the University of Washington Invested Funds Pool**

All of the Unit's cash and cash equivalents are invested in the University of Washington's Invested Funds Pool. The following information is for the entire pool.

The Board of Regents (the Board) of the University of Washington is responsible for the management of the University's investments. The Board establishes investment policy, which is carried out by the Chief Investment Officer. The University of Washington Investment Committee, comprising Board members and investment professionals, advises on matters relating to the management of the University's investment portfolios. The composition of the carrying amounts of investments by type at June 30, 2015 are listed below:

**University Investments**

| Investment type | | Carrying value (Dollars in thousands) |
|---|---|---|
| Cash equivalents | $ | 403,978 |
| Fixed income | | 1,726,481 |
| Equity | | 1,733,102 |
| Nonmarketable alternatives | | 353,053 |
| Absolute return | | 561,999 |
| Real assets | | 189,447 |
| Miscellaneous | | 8,603 |
| Total investments | $ | 4,976,663 |

*Investment Pools* – The University combines most short-term cash balances into the Invested Funds Pool. At June 30, 2015, the Invested Funds Pool totaled $1,526,380,000. The Invested Funds Pool also owns units in the Consolidated Endowment Fund valued at $806,198,000 on June 30, 2015. By University policy, departments with qualifying funds in the Invested Funds Pool receive distributions based on their average balances and on the type of balance. Campus depositors received 2% in fiscal year 2015. Endowment operating and gift accounts received 3% in fiscal year 2015. The difference between the actual earnings of



(Continued)

the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The majority of the endowed funds are invested in a pooled fund called the Consolidated Endowment Fund (CEF). Individual endowments purchase units in the pool on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held. RCW 24.55 of the Washington State Code and the Uniform Prudent Management of Institutional Funds Act allow for total return expenditure under comprehensive prudent standards.

*Interest Rate Risk* – The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform, while controlling the interest rate risk in the portfolio. The weighted average effective duration of the University's fixed income portfolio was 1.81 years at June 30, 2015.

*Credit Risk* – Fixed income securities are subject to credit risk, which is the risk that the issuer or other counterparty to a financial instrument will not fulfill its obligations, or that negative perceptions of the issuer's ability to make these payments will cause prices to decline. Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University Investment Policies limit fixed income exposure to investment grade assets. The Investment Policy for the Invested Funds' cash pool requires each manager to maintain an average quality rating of "AA" as issued by a nationally recognized rating organization. The Invested Funds' liquidity pool requires each manager to maintain an average quality rating of "A" and to hold 25% of their portfolios in government and government agency issues. The Investment Policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investment-to-investment grade credits.

Duration and credit risk figures at June 30, 2015 exclude $36,027,000, of fixed income securities held outside the CEF and the Invested Funds Pool. These amounts make up 1.69%, of the University's fixed income investments (including cash equivalents), and are not included in the duration figures detailed in the following table.

The composition of the fixed income securities at June 30, 2015, along with credit quality and effective duration measures is summarized below:

**Fixed Income: Credit Quality and Effective Duration**

| Investments | U.S. government | Investment grade* | Noninvestment grade | Not rated | Total | Duration (in years) |
|---|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | | |
| 2015: | | | | | | |
| U.S. Treasuries | $ 842,525 | — | — | — | 842,525 | 1.43 |
| U.S. government agency | 644,721 | — | — | — | 644,721 | 2.46 |
| Mortgage backed | — | 107,070 | 75,060 | 22,415 | 204,545 | 2.01 |
| Asset backed | — | 195,968 | 6,998 | 24,111 | 227,077 | 1.73 |
| Corporate and other | — | 175,364 | — | 200 | 175,564 | 1.18 |
| Total | $ 1,487,246 | 478,402 | 82,058 | 46,726 | 2,094,432 | 1.81 |

* Investment grade securities are those that are rated BBB and higher by Standard and Poor's or Baa and higher by Moody's.

*Foreign Currency Risk* – The University's Investment Policies permit investments in international equity and other asset classes, which can include foreign currency exposure. The University held non-U.S. denominated securities at June 30, 2015 of $1,195,070,000.

**Investments Denominated in Foreign Currency**

| | | (Dollars in thousands) |
|---|---|---|
| Chinese Renminbi (RMB) | $ | 211,184 |
| Euro (EUR) | | 174,487 |
| Indian Rupee (INR) | | 112,679 |
| Japanese Yen (JPY) | | 110,617 |
| Hong Kong Dollar (HKD) | | 60,046 |
| South Korean Won (KRW) | | 56,835 |
| British Pound (GBP) | | 54,880 |
| Brazilian Real (BRL) | | 54,225 |
| Swiss Franc (CHF) | | 39,061 |
| Russian Ruble (RUB) | | 36,218 |
| Canadian Dollar (CAD) | | 35,385 |
| Philippine Peso (PHP) | | 29,100 |
| Taiwanese Dollar (TWD) | | 27,055 |
| Mexican Peso (MXN) | | 23,898 |
| Remaining currencies | | 169,400 |
| Total | $ | 1,195,070 |

## (3) Internal Note Receivable

The Internal Note Receivable from Commute Options – Active Transportation for the construction of the Burke Gilman Trail project bears an interest rate of 4.75% with interest and principal payments due at the end of each month over a 30-year period. The outstanding balance as of June 30, 2015 was $6,736,847 of which $107,266 is the current portion. The total interest income earned on the note in 2015 was $160,720.



(Continued)

## (4) Capital Assets

Capitalized asset activity for the year ended June 30, 2015 is summarized as follows:

| | Balance at June 30, 2014 | Additions/ Transfers | Retirements/ Adjustments | Balance at June 30, 2015 |
|---|---|---|---|---|
| Buildings | $ 85,198,611 | — | — | 85,198,611 |
| Furniture, fixtures, and equipment | 1,286,667 | 241,765 | (285,213) | 1,243,219 |
| Construction in progress* | 2,250,781 | 950,872 | (2,460,122) | 741,531 |
| Total | 88,736,059 | 1,192,637 | (2,745,335) | 87,183,361 |
| Less accumulated depreciation: | | | | |
| Buildings | 38,597,495 | 2,100,128 | — | 40,697,623 |
| Furniture, fixtures, and equipment | 1,148,608 | 76,634 | (284,058) | 941,184 |
| Total accumulated depreciation | 39,746,103 | 2,176,762 | (284,058) | 41,638,807 |
| Capital assets, net | $ 48,989,956 | (984,125) | (2,461,277) | 45,544,554 |

* Nondepreciable

## (5) Operating Leases

CS has lease agreements with the University's Real Estate Office in effect that are considered operating leases for leased parking spaces from May 1, 2010 through June 30, 2021. During the year ended June 30, 2015, CS recorded rent expense of $35,488. Future lease payments under these leases as of June 30, 2015 are as follows:

| | Dollars |
|---|---|
| Years ending June 30: | |
| 2016 | $ 42,034 |
| 2017 | 42,034 |
| 2018 | 42,034 |
| 2019 | 42,034 |
| 2020 | 3,903 |
| 2021 | 3,902 |
| Total minimum lease payment | $ 175,941 |

## (6) Revenue Bond Refinancing and Internal Lending Program

During 2004, Commuter Services issued $20,410,000 of Revenue Bonds to refund the outstanding Series 1995 Revenue Bonds and to finance various parking projects. The Revenue Bonds are held by the University and bear interest at rates from 3.00% to 5.00% depending on the fiscal year, with interest and principal payments due on May 1 and November 1 of each year. The Bonds are secured by the pledge of the Parking System revenues over operating expenses.

On March 7, 2012, these 2004 Revenue Bonds were refunded and replaced by General Revenue and Refunding Bonds by the University. The amount refunded was $16,405,000, which resulted in no change in the total debt service payments and resulted in an economic gain of $210,023 to the University. The new bonds are administered under the Internal Lending Program (ILP). Total amount of defeased bonds as of June 30, 2015 was zero as they were fully redeemed during the fiscal year.

The purpose of the ILP is to lower the University's overall cost of capital and provide internal borrowing units with a stable and predictable borrowing rate. The ILP makes loans to internal borrowers at a uniform internal lending rate. These loans are funded through the issuance of University General Revenue bonds and notes. ILP program policies include a provision for a rate stabilization reserve and a provision for rate adjustments if necessary.

Under the terms of the ILP, rate adjustments will apply to all outstanding debt obligations, including debt issued prior to the ILP implementation. The ILP lending rate will be reviewed annually and a preliminary indication of a rate adjustment will be announced to ILP participants 12 months in advance of the effective date. Final rate adjustments require approval by the Board of Regents.

Future principal and interest payments due through maturity dates are as follows:

| | | Principal | Interest |
|---|---|---|---|
| Years ending June 30: | | | |
| 2016 | $ | 602,251 | 601,052 |
| 2017 | | 627,251 | 573,352 |
| 2018 | | 657,251 | 544,552 |
| 2019 | | 687,251 | 514,073 |
| 2020 | | 727,251 | 478,170 |
| Thereafter | | 9,904,347 | 2,217,386 |
| | $ | 13,205,602 | 4,928,585 |

ILP activity for the year ended June 30, 2015 is summarized as follows:

| | | Balance as of June 30, 2014 | Additions | Reductions | Balance as of June 30, 2015 |
|---|---|---|---|---|---|
| Internal lending program payable | $ | 13,782,853 | — | 577,251 | 13,205,602 |

## (7) Related-Party Transactions

The University provides support to Commuter Services by performing the following services:

- The University requires a discretionary transfer for overhead equal to 8.88% of certain Commuter Services' revenues in exchange for providing the following:
  - Use of the University's buildings and equipment
  - Administrative and accounting support
  - Serving as the purchasing and disbursing agent
  - Various other operational and support services
- The University has included Commuter Services in its liability self-insurance program and allocates a portion of the program's cost to Commuter Services in an amount established at the University's discretion.
- Additionally, transfers to and from the University are made at the discretion of the University and Commuter Services.

The UPASS program is operated by the University's Transportation Commute Options Department and provides a package of flexible, low cost transportation choices for faculty, staff, and students. It includes unlimited access to public transit, and a parking management component that subsidizes carpool and vanpool parking rather than single occupant vehicles. The University offers several contributory pension plans administered by the Washington State Department of Retirement Systems: the Public Employees' Retirement System plan, the Teachers' Retirement System plan, and the Law Enforcement Officers' and Fire Fighters' Retirement System plan, which are defined-benefit retirement plans. Additionally, the University offers the University of Washington Retirement plan, a defined-contribution plan, and the University of Washington Supplemental Retirement plan, a defined-benefit plan.

## (8) Pension Plan

### *(a) Public Employees' Retirement System (PERS)*

PERS was established in 1947 and its retirement benefit provisions are contained in chapters 41.34 and 41.40 of the Revised Code of Washington (RCW). PERS is a cost-sharing multiple-employer retirement system comprising three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined benefit plans, and PERS Plan 3 is a defined-benefit plan with a defined-contribution component. PERS members include higher education employees not participating in other higher education retirement programs.

PERS comprises and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined-benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined-contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined-benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

### *(b) The Pension Plans' Fiduciary Net Positions*

The pension plans' fiduciary net positions have been determined on the same basis used by the pension plans. Washington State Department of Retirement Systems (DRS) financial statements have been prepared in conformity with generally accepted accounting principles (GAAP). The retirement plans are accounted for in pension trust funds using the flow of economic resources measurement focus and the accrual basis of accounting. Plan member contributions are recognized as revenues in the period in which the contributions are earned. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

The Washington State Investment Board (WSIB) has been authorized by statute (Chapter 43.33A of the RCW) as having the investment management responsibility for the pension funds. Investments are reported at fair value, and unrealized gains and losses are included as investment income in the Statement of Changes in Fiduciary Net Position presented in the DRS Comprehensive Annual Financial Report. Purchases and sales of investments are recorded on a trade-date basis.

DRS publishes an annual report for retirement plans which is available at: http://www.drs.wa.gov/administration/annual-report/.

### *(c) Actuarial Assumptions*

The total pension liability for each plan was determined by an actuarial valuation as of June 30, 2013, with the results rolled forward to June 30, 2014. The following actuarial assumptions have been applied to all prior periods included in the measurement:

| | |
|---|---|
| Inflation | 3.0% total economic inflation, 3.75% salary inflation |
| Salary increase | Expected to grow by promotions and longevity in addition to the salary inflation assumption |
| Investment rate of return | 7.50% |

Mortality rates were based on the RP-2000 Combined Healthy Table and Combined Disabled Table published by the Society of Actuaries. The Washington State Office of the State Actuary (OSA) applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100% Scale BB. Mortality rates are applied on a generational basis, meaning members are assumed to receive additional mortality improvements in each future year, throughout their lifetime.

The actuarial assumptions used in the June 30, 2013 valuation were based on the results of OSA's 2007–2012 Experience Study. Additional assumptions for subsequent events and law changes are current as of the 2013 actuarial valuation report.

### *(d) Discount Rate*

The discount rate used to measure the total pension liabilities was 7.50% for all plans in which the University participates. To determine the discount rate, an asset sufficiency test was completed to test whether each pension plan's fiduciary net position was sufficient to make all projected future benefit payments of current plan members. Consistent with current law, the completed asset sufficiency tests for PERS included an assumed 7.70% long-term discount rate to determine funding liabilities for calculating future contribution rate requirements.

Consistent with the long-term expected rate of return, a 7.50% future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue to be made at contractually required rates (including the component of PERS 2/3 employer rates pertaining to the unfunded actuarial accrued liability for PERS 1, respectively, as provided for in chapter 41.45 of the RCW).

Based on those assumptions, the fiduciary net position for each pension plan was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.50% on pension plan investments was applied to determine the total pension liability.

### *(e) Sensitivity of the Net Pension Liability to Changes in the Discount Rate*

The following table presents the University's net pension liability calculated using the discount rate of 7.50%, as well as what the net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower (6.50%) or one-percentage-point higher (8.50%) than the current rate.

**Discount Rate Sensitivity**
**Net Pension Liability**
(Dollars in thousands)

| | | 1% Decrease | Current discount | 1% Increase |
|---|---|---|---|---|
| Plan: | | | | |
| PERS 1 | $ | 514,278 | 417,231 | 333,926 |
| PERS 2/3 | | 843,524 | 202,225 | (287,608) |

### *(f) Long-Term Expected Rate of Return*

The long-term expected rate of return of 7.50% on pension plan investments was determined by the WSIB. The rate approximately equals the median of the simulated investment returns over a 50-year time horizon, increased slightly to remove WSIB's implicit, small, short-term downward adjustment due to assumed mean reversion. WSIB's implicit short-term adjustment, while small and appropriate over a 10- to 15-year period, becomes amplified over a 50-year measurement period.

The long-term expected rate of return was determined by the WSIB using a building-block method in which a best estimate of expected future rates of return (expected returns, net of pension plan investment expense, but including inflation) are developed for each major asset class by the WSIB. Those expected returns make up one component of WSIB's Capital Market Assumptions (CMAs).

The CMAs contain three pieces of information for each class of assets the WSIB currently invest in:

- Expected annual return
- Standard deviation of the annual return
- Correlations between the annual returns of each asset class with every other asset class

WSIB uses the CMAs and their target asset allocation to simulate future investment returns over various time horizons.

Best estimates of arithmetic real rates of return for each major asset class included in the target asset allocation for each pension plan, as of June 30, 2014 are summarized in the following table:

| Asset class | Target allocation | Long-term expected real rate of return |
|---|---|---|
| Fixed income | 20.00% | 0.80% |
| Tangible assets | 5.00 | 4.10 |
| Real estate | 15.00 | 5.30 |
| Global equity | 37.00 | 6.05 |
| Private equity | 23.00 | 9.05 |

The inflation component used to create the above table is 2.70%, and represents WSIB's most recent long-term estimate of broad economic inflation.

### *(g) Employer Contribution Rates*

Employer contribution rates are developed in accordance with chapter 41.45 of the RCW by the OSA, and include an administrative expense component that is currently set at 0.18%. The statute provides authority to the Pension Funding Council to adopt changes to economic assumptions and contribution rates.

### *(h) University Proportionate Share*

Collective pension amounts are determined as of a measurement date, which can be no earlier than an employer's prior fiscal year. The measurement date for the net pension liabilities recorded by the University as of June 30, 2015 was June 30, 2014. University contributions received and processed by DRS during the fiscal year ended June 30, 2014 have been used as the basis for determining the University's proportionate share of the collective pension amounts reported by DRS in their June 30, 2014 Schedules of Employer and Nonemployer Allocations for all plans in which the University participates.

| Plan | Proportionate share for year ended June 30, 2015 |
|---|---|
| PERS 1 | 8.28% |
| PERS 2/3 | 10.00 |

### *(i) Commuter Services Aggregated Balances*

Commuter Services' aggregated balances of net pension liabilities and deferrals as of June 30, 2015 are presented in the table below:

| | June 30, 2015 | | |
|---|---|---|---|
| | Net pension liability | Deferred outflows | Deferred inflows |
| | | (Dollars in thousands) | |
| PERS 1 | $ 1,093 | 127 | 137 |
| PERS 2/3 | 510 | 137 | 541 |
| Total | $ 1,603 | 264 | 678 |

**PERS Plan 1**

PERS Plan 1 is closed to new entrants.

***Vesting***

PERS Plan 1 members were vested after the completion of five years of eligible service.

***Benefits provided***

PERS Plan 1 provides retirement, disability, and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service.

Members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and nonduty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

***Contributions***

The PERS Plan 1 employer contribution rate for the fiscal years ended June 30, 2015 and 2014 was 9.21% in both years. The Commuter Services' contributions to PERS Plan 1 for the year ended June 30, 2015 were $127,000.

***Proportionate Share of PERS Plan 1 Pension Expense and Deferrals Related to Pensions***

The Commuter Services' proportionate share of PERS Plan 1 pension expense for the fiscal year ended June 30, 2015 was $71,000, and is reported on the statement of revenues, expenses, and changes in net position in benefits expense.

The Commuter Services' deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 1 as of June 30, 2015 are presented in the following table:

| **Description** | | **Deferred outflows of resources** | **Deferred inflows of resources** |
|---|---|---|---|
| Difference between projected and actual earnings on pension plan investments, net | $ | — | 137,000 |
| Commuter Services pension plan contributions subsequent to the measurement date of collective net pension liability | | 127,000 | — |
| Total | $ | 127,000 | 137,000 |

Deferred outflows of resources related to Commuter Services contributions subsequent to the measurement date of $127,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred inflows of resources pertaining to PERS Plan 1 will be recognized in pension expense as follows:

| | | |
|---|---|---|
| Year: | | |
| 2016 | $ | (34,250) |
| 2017 | | (34,250) |
| 2018 | | (34,250) |
| 2019 | | (34,250) |
| 2020 | | — |
| Thereafter | | — |
| Total | $ | (137,000) |

**PERS Plan 2/3**

***Vesting***

PERS Plan 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined-benefit portion of their plan after 10 years of service, or after 5 years of service if twelve months of that service are earned after age 44.

***Benefits provided***

PERS Plan 2/3 provides retirement, disability, and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2, and one percent of AFC times the member's years of service for Plan 3.

The AFC is the monthly average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at age 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age, for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 2, 2013:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other PERS Plan 2/3 benefits include duty and nonduty disability payments, a cost-of-living allowance (based on the Consumer Price Index), capped at three percent annually, and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

### *Contributions*

The PERS Plan 2/3 employer contribution rate for the fiscal years ended June 30, 2015 and 2014 was 9.21% in both years. The Plan 2/3 employer rate includes a component to address the PERS Plan 1 unfunded actuarial accrued liability. Commuter Services' contributions to PERS Plan 2/3 for the year ended June 30, 2015 were $143,000.

### *Proportionate Share of PERS Plan 2/3 Pension Expense and Deferrals Related to Pensions*

Commuter Services' proportionate share of PERS Plan 2/3 pension expense for the fiscal year ended June 30, 2015 was $80,000, and is reported on the statement of revenues, expenses, and changes in net position in benefits expense.

Commuter Services' deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 as of June 30, 2015 are presented in the following table:

| Description | Deferred outflows of resources | Deferred inflows of resources |
|---|---|---|
| Difference between projected and actual earnings on plan investments, net | $ — | 541,000 |
| Changes in Commuter Services' proportion | (6,000) | — |
| Commuter Services' contributions to plans subsequent to the measurement date of collective net pension liability | 143,000 | — |
| Total | $ 137,000 | 541,000 |

Deferred outflows of resources related to Commuter Services contributions subsequent to the measurement date of $143,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 will be recognized in pension expense as follows:

| | | |
|---|---|---|
| Year: | | |
| 2016 | $ | (153,000) |
| 2017 | | (153,000) |
| 2018 | | (153,000) |
| 2019 | | (76,000) |
| 2020 | | — |
| Thereafter | | — |
| Total | $ | (535,000) |

## (9) University of Washington Retirement Plan

*Plan Description* – Professional staff and certain other salaried employees are eligible to participate in the UWRP, a defined-contribution plan administered by the University. Contributions to the plan are invested in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations.

Benefits from fund sponsors are available upon separation or retirement at the member’s option. RCW 28.B.10.400 et. seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

The Plan has a supplemental payment component that guarantees a minimum retirement benefit based upon a onetime calculation at each employee’s retirement date. The University makes direct payments to qualifying retirees when the retirement benefits provided by the fund sponsors do not meet the benefit goals. During the fiscal year ended June 30, 2011, the University amended the supplemental retirement plan, limiting participation to those individuals who were active participants on February 28, 2011.

*Funding Policy* – Employee contribution rates, based on age, are 5.0%, 7.5%, or 10.0% of salary. The University matches the contributions of employees. Within parameters established by the legislature, contribution requirements may be established or amended by the University of Washington Board of Regents. Employee and employer contributions for the year ended June 30, 2015 were $64,426. The supplemental component of the UWRP is financed on a pay as you go basis.

**(10) Other Postemployment Benefits (OPEB)**

The University funds OPEB obligations at a university-wide level on a pay-as-you-go basis. Disclosure information, as required under GASB Statement No. 45 (GASB 45), *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*, does not exist at the Unit level, and as a result, the Actuarial Accrued Liability (AAL) is not available for auxiliary entities. The University is ultimately responsible for the payment of the obligation; therefore, the annual required contribution (ARC) is not recorded on the Unit's financial statements.

**(11) Commitments and Contingencies**

The Unit is subject to various claims and lawsuits that are covered by the University's self-insurance fund in excess of $100,000.

**(12) Subsequent Events**

A capital contribution in September 2015 resulted from the transfer of the Lander Garage from Housing and Food Services to Commuter Services.

The department is periodically subject to ongoing audits, and that a city parking tax audit has concluded; however, findings have not been finalized at this time.

Commuter Services has performed an evaluation of subsequent events through November 10, 2015.

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

Schedules of Required Supplementary Information

Unaudited – see accompanying independent auditors' report

June 30, 2015

The Schedules of Required Supplementary Information below reflect the information for the University of Washington as a whole due to the constraints of available information for the University of Washington Commuter Services.

**Schedule of the University's Proportionate Share of the Net Pension Liability**
**PERS 1 Pension Plan**
(Dollar amounts in thousands)

| | | 2015 |
|---|---|---|
| University's proportion of the net pension liability | | 8.28243% |
| University's proportionate share of the net pension liability | $ | 417,231 |
| University's covered-employee payroll | | 25,376 |
| University's proportionate share of the net pension liability as a percentage of its covered-employee payroll | | 1,644.20% |
| Plan fiduciary net position as a percentage of the total pension liability | | 61.19 |

**Schedule of University's Contributions**
**PERS 1 Pension Plan**
(Dollar amounts in thousands)

| | | |
|---|---|---|
| Contractually required contribution | $ | 2,311 |
| Contributions in relation to the contractually required contribution | | 2,313 |
| Contribution excess | | (2) |
| University's covered-employee payroll | | 25,376 |
| Contributions as a percentage of covered-employee payroll | | 9.11% |

**Schedule of the University's Proportionate Share of the Net Pension Liability**
**PERS 2/3 Pension Plan**
(Dollar amounts in thousands)

| | | |
|---|---|---|
| University's proportion of the net pension liability | | 10.004398% |
| University's proportionate share of the net pension liability | $ | 202,225 |
| University's covered-employee payroll | | 856,839 |
| University's proportionate share of the net pension liability as a percentage of its covered-employee payroll | | 23.60% |
| Plan fiduciary net position as a percentage of the total pension liability | | 93.29% |



(Continued)

**UNIVERSITY OF WASHINGTON**
**COMMUTER SERVICES**
(A Department of University of Washington)

Schedules of Required Supplementary Information

Unaudited – see accompanying independent auditors' report

June 30, 2015

**Schedule of University's Contributions**
**PERS 2/3 Pension Plan**
(Dollar amounts in thousands)

| | | 2015 |
|---|---|---|
| Contractually required contribution | $ | 78,164 |
| Contributions in relation to the contractually required contribution | | 78,160 |
| Contribution deficiency (excess) | | 4 |
| University's covered-employee payroll | | 856,839 |
| Contributions as a percentage of covered-employee payroll | | 9.12% |

**Notes to Schedules of Required Supplementary Information (Unaudited) for the Year Ended June 30, 2015**

*Changes of benefit terms*. Amounts reported in 2015 reflect no change in benefit terms.

*Changes of assumptions*. Amounts reported in 2015 reflect no changes in assumptions.

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Financial Statements and Schedules

June 30, 2015

(With Independent Auditors' Report Thereon)

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

## Table of Contents

**KPMG LLP**
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

# Independent Auditors' Report

The Board of Regents
University of Washington:

We have audited the accompanying financial statements of the University of Washington Department of Intercollegiate Athletics (the Department), which comprise the statement of net position as of June 30, 2015, and the related statement of revenues, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

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

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

## *Auditors' Responsibility*

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

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

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

As discussed in note 1 to the financial statements, the financial statements of the Department, an auxiliary enterprise within the University of Washington (the University), are intended to present the financial position, the changes in financial position and cash flows of only the respective portion of the business-type activities of the University that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the University as of June 30, 2015, the changes in its financial position or its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington Department of Intercollegiate Athletics as of June 30, 2015, and the changes in its net position and its cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.

### *Other Matters*

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 10, and the schedules of required supplementary information on pages 32 through 33, be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries with management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information included on pages 34 and 35 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

### *Emphasis of Matter*

As discussed in note 1 to the financial statements, on July 1, 2014, the Department adopted new accounting guidance requiring governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, as well as recognizing most changes in the net pension liability within pension expense. Our opinion is not modified with respect to this matter.

KPMG LLP

Seattle, Washington
November 18, 2015

### Discussion and Analysis Prepared by Management

The following discussion and analysis provides an overview of the financial position and activities of the University of Washington Department of Intercollegiate Athletics (ICA) for the years ended June 30, 2015 and 2014. This discussion has been prepared by management and should be read in conjunction with the financial statements and accompanying notes, which follow this section.

### Using the Financial Statements

ICA's financial statements include the statement of net position, statement of revenues, expenses, and changes in net position, statement of cash flow, and notes to financial statements. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities. The financial health of ICA can be measured by reviewing the summaries and explanations that follow.

### Statements of Net Position Summary

The statement of net position in the financial statements reflect the financial conditions of ICA at the end of the last two years and report the various categories of all assets and liabilities. The following statements of net position summary shows ICA's total assets, total liabilities, and net position as of June 30, 2015 and 2014:

**Statements of net position summary**

| | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|
| Current assets | $ 17,642 | $ 19,071 |
| Noncurrent assets: | | |
| Capital assets, net | 364,066 | 378,330 |
| Other | 88,766 | 82,614 |
| Total assets | 470,474 | 480,015 |
| Pension deferred outflows of resources | 727 | — |
| Total assets and pension deferred outflows of resources | $ 471,201 | $ 480,015 |
| Current liabilities | 37,608 | 34,413 |
| Noncurrent liabilities | 262,491 | 268,765 |
| Total liabilities | 300,099 | 303,178 |
| Pension deferred inflows of resources | 1,606 | — |
| Net position | 169,496 | 176,837 |
| Total liabilities, pension deferred inflows of resources and net position | $ 471,201 | $ 480,015 |

Following are comments about the changes highlighted by the statements of net position summary:

- Current assets consist primarily of cash and cash equivalents, accounts receivable, and prepaid expenses. Current assets were $20 million less than current liabilities at the end of 2015. The negative working capital is due to unearned income of $17.8 million largely related to ticket sales for the 2015 football season and will be recorded as revenue in 2016. Increases and decreases in current assets occur due to the timing of payments and receipts from operations.
- Noncurrent assets consist primarily of long-term investments, endowments, and capital assets. Noncurrent assets were $8.1 million less at the end of 2015 due to an increase in accumulated depreciation on capital assets. There is $27.6 million of noncurrent assets in long-term investment funds, and these investments can be used to meet ICA's long-term obligations.
- Pension deferred outflows were $727 thousand as a result of implementing GASB Statement No. 68 (GASB 68), *Accounting and Financial Reporting for Pensions*.
- Current liabilities increased by $3.2 million during 2015 to a total of $37.6 million. This change is comprised primarily of increases in accounts payable due to the timing of payments near year-end and increases in accrued salary and vacation payable as well as the current portion due for debt obligations.
- Noncurrent liabilities decreased by $6.3 million in 2015 because of principal payments due to the Internal Lending Program (ILP) of the University of Washington (University).
- Pension deferred outflows were $1.6 million as a result of implementing GASB 68.
- The change in net position or "equity" measures whether the overall financial condition has improved or deteriorated during the year. The total of net position decreased by $7.3 million during 2015 due to the combination of a decrease in gate revenue, a decrease in related contributions in the current year, and a lower return on market value of long-term investments and endowments.

**ICA's Net Position or "Equity"**

The following table is a summary of the net position or "equity" for ICA at June 30, 2015 and 2014:

| | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| Net investment in capital assets | $ | 99,679 | 104,976 |
| Restricted: | | | |
| Nonexpendable | | 47,586 | 43,832 |
| Expendable | | 12,885 | 15,897 |
| Unrestricted | | 9,346 | 12,132 |
| Total net position | $ | 169,496 | 176,837 |

The categories of net position or "equity" listed in the table above are defined as follows:

- "Net investment in capital assets" is ICA's total investment in property, plant, equipment, and infrastructure, net of accumulated depreciation and any outstanding debt obligations related to those capital assets.
- "Restricted nonexpendable net position" consists of funds for which the donor has made the restriction that the principal is not available for expenditures, but investment earnings can be used for specific purposes.
- "Restricted expendable net position" are resources that ICA is obligated to spend in accordance with the restrictions placed by donors and/or external parties.
- "Unrestricted net position" are all other funds available to ICA for any purpose. Unrestricted assets are often internally designated for specific purposes.

Following are comments about the changes highlighted in the net position or "equity" summary:

- Net investment in capital assets decreased by $5.3 million in 2015 to a total of $99.7 million. This balance increases as debt is paid off or when ICA funds fixed asset purchases without financing. The balance decreases as assets are depreciated.
- Restricted nonexpendable net position increased by $3.8 million in 2015. The increase in 2015 was a combination of an increase in the value of endowments and an increase in additions for new endowments of $3.4 million that were donated to ICA.
- Restricted expendable net position decreased by $3.0 million in 2015 to a total of $12.9 million due to contributions received offset by expenditures for the Husky Stadium renovation project made in accordance with the donors' stipulations.
- Unrestricted net position decreased by $2.8 million in 2015 to $9.3 million. On July 1, 2014, ICA adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. Implementation of this standard resulted in the restatement of beginning unrestricted net position reducing it by $4.4 million. This was partially offset by the recording of financing cost expenses for the ILP debt for Husky Stadium and Husky Ballpark.

### Endowments and Other Investments

- The fair market value of ICA's endowments was $59.9 million at June 30, 2015. The increase in 2015 is due to improvements in the market as well as additional endowment contributions of $3.4 million.
- ICA had $27.6 million of long-term investments, not including endowments, in the Consolidated Endowment Fund (CEF) at June 30, 2015.
- Short-term investments in the Invested Funds Pool used as operating funds for ICA yielded returns of 2.0% in 2015.

### Capital Improvements and Related Debt

- In 2015, there was a net decrease of $14.3 million in capital assets, primarily related to the depreciation of capital assets exceeding the acquisition of capital assets.

 (Continued)

- Total noncurrent liabilities at the end of 2015 was $262.5 million. The decrease is primarily due to settlement of the payable to the University for construction in progress and retainage for Husky Stadium.

**Statements of Revenues, Expenses, and Changes in Net Position**

The statements of revenues, expenses, and changes in net position present how ICA's operating and nonoperating items resulted in changes in net position. In accordance with GASB reporting principles, revenues and expenses are classified as either operating or nonoperating. The following summary shows the revenues, expenses, and changes in net position for the years ended June 30, 2015 and 2014:

**Revenues, expenses, and changes in net position summary**

| | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| Operating revenues | $ | 79,818 | 70,777 |
| Operating expenses | | (110,127) | (112,180) |
| Operating loss | | (30,309) | (41,403) |
| Nonoperating revenues and expenses | | 17,233 | 25,386 |
| Other revenues | | 10,167 | 16,826 |
| (Decrease) Increase in net position | | (2,909) | 809 |
| Net position, beginning of year | | 176,837 | 176,028 |
| Effect of accounting and reporting entity changes | | (4,432) | — |
| Net position, end of year | $ | 169,496 | 176,837 |

## Revenues from All Sources

The following table summarizes revenues from all sources for the years ended June 30, 2015 and 2014:

**Revenues from all sources summary**

| | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| Gate ticket sales | $ | 25,422 | 28,830 |
| NCAA/conference distributions | | 35,762 | 24,935 |
| Sponsorships | | 11,993 | 10,668 |
| Concessions/souvenirs/parking/boat moorage | | 3,296 | 3,408 |
| Other operating revenue | | 3,345 | 2,935 |
| Contributions (noncapital) | | 22,778 | 24,031 |
| Investment income, net | | 1,914 | 1,918 |
| Gain on investments | | 2,704 | 8,274 |
| University funded tuition waivers | | 3,895 | 3,550 |
| Capital gifts | | 6,763 | 11,092 |
| Settlement agreement | | 1,250 | — |
| Amortization on debt refinance gain | | — | 86 |
| Endowment gifts | | 3,404 | 5,733 |
| Total revenue – all sources | $ | 122,526 | 125,460 |

Following are comments about the changes highlighted by the revenues from all sources summary:

- Gate ticket sales continue to be a large source of revenue for ICA. Gate ticket sales decreased by $3.4 million in 2015 from 2014, due to a decrease in Football and Men's Basketball season ticket sales and in 2015 from 2014.
- NCAA/Conference distributions increased by $10.8 million in 2015 from 2014. The increase in 2015 is mainly due to a multimedia rights agreement signing bonus of $7.3 million. Conference postseason/regular season shares increased $3.1 million from 2014. In addition, $1.7 million was paid out related to the Pac-12 Network in 2015, which is a $527 thousand increase from 2014.
- Sponsorship revenue increased by $1.3 million in 2015 from 2014. The increase in 2014 is mainly due to an increase in donated advertising related to the new radio contract with KOMO radio.
- Concessions/souvenirs/parking/boat moorage revenue decreased by $112 thousand in 2015 from 2014. This decrease is due to having lower attendance at Football and Men's Basketball games.
- Other operating revenue increased $410 thousand from 2014. This increase is mostly due to increased revenue from fundraising from the sport teams.

- Contributions related to noncapital gifts decreased by $1.3 million in 2015 from 2014. The majority of the decrease is due to lower seat related contributions due to lower football and men's basketball season ticket sales.
- Investment income decreased by $4 thousand in 2015. Investment income is earned on two categories including investments in the CEF and short-term investments with the activity described as follows:
  - Investment income in the CEF increased by $250 thousand in 2015 mainly due to an increase in the balance held in the CEF during these periods.
  - Short-term investments received 2.0% distributions in 2015. Since the returns were the same for each year, the change in the average investment balances accounted for any change in investment income.
- In 2015 there was a decrease of gain on investments of $5.6 million due to the decreased value of long-term investments and endowment funds.
- University funded tuition waivers increased by $345 thousand in 2015 due to the impact of increasing tuition rates.
- Capital gifts were $6.8 million in 2015. The decrease of $4.3 million is due to a decrease in the remaining pledges due for the stadium.
- In 2015, there was a settlement agreement reached with a former coach, which resulted in $1.3 million in settlement agreement revenue.
- Endowment gifts decreased by $2.3 million in 2015 to a total of $3.4 million.

**Expenses and Losses**

The following table summarizes expenses and losses for the years ended June 30, 2015 and 2014:

**Expenses and losses summary**

| | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| Salaries and wages | $ | 29,089 | 26,786 |
| Payroll taxes and employee benefits | | 6,585 | 7,155 |
| Athletic student aid | | 11,959 | 11,806 |
| Guarantees paid to visiting teams | | 2,113 | 1,593 |
| Team travel | | 6,008 | 5,595 |
| Day of game | | 6,749 | 7,156 |
| Direct facilities, maintenance, and utilities | | 4,039 | 4,455 |
| Advertising | | 1,728 | 531 |
| Uniforms and supplies | | 6,205 | 6,046 |
| Training table | | 2,558 | 1,643 |
| Department relations | | 774 | 887 |
| Banquets and special events | | 639 | 566 |
| Depreciation | | 17,270 | 17,598 |
| Noncapitalized equipment and repairs | | 2,546 | 8,485 |
| Institutional overhead | | 1,748 | 2,454 |
| Other operating expenses | | 10,116 | 9,424 |
| Total operating expenses | | 110,126 | 112,180 |
| Financing costs | | 2,566 | — |
| Loss on disposal of capital assets | | 34 | 5 |
| Interest expense | | 12,709 | 12,467 |
| Total nonoperating expenses and losses | | 15,309 | 12,472 |
| Total | $ | 125,435 | 124,652 |

Following are comments about the changes in expenses highlighted by the expenses and losses summary:

- Salaries and wages increased by $2.3 million in 2015 from 2014 due to an increase in fixed extra guaranteed compensation per employment contracts.
- Payroll taxes and employee benefits decreased by $570 thousand in 2015 from 2014. Since payroll taxes and employee benefits are a percentage of salaries and wages, the impact from increases in salaries and wages was more than offset by decreases in the percentage charged. There were decreases in the percentages charged for employee benefit load rates in 2015. The percentages charged to ICA on professional and contract staff salaries decreased from 30.9% in 2014 to 27.7% in 2015. The percentage decreased from 35.3% in 2014 to 33.8% in 2015 for classified staff salaries. The smaller amount spent on classified staff salaries compared to professional and contract staff salaries only had a small impact on increasing the total amount

of payroll taxes and employee benefits paid. The percentages charged on hourly staff, overtime, and additional compensation for contract staff increased from 15.2% in 2014 to 17% in 2015.

- Athletic student aid increased by $153 thousand in 2015 from 2014 due to rate increases for out of state tuition and increases for room and board. The increases in 2015 were 0% for in-state tuition and 5% for out of state tuition.
- Guarantees paid to visiting teams fluctuate due to the difference in the nonconference football game schedule.
- Team travel increased by $413 thousand in 2015 from 2014, due to increase costs for airfare and meals in 2015.
- Day of game decreased by $407 thousand in 2015 from 2014 mostly due to not having a weekday game, which increases fan bus transportation costs as an additional bus transportation vendor is required for weekday games.
- Advertising increased by $1.2 million in 2015 from 2014 due to the change in the value of the radio contract. The radio contract with IMG changed from KJR to KOMO.
- Training table increased by $915 thousand in 2015 from 2014 due mostly to deregulation of NCAA food policies. This change allowed more opportunities for university to provide meals and snacks for student athletes.
- Depreciation expense decreased $328 thousand in 2015 from 2014 due to more assets becoming fully depreciated and an increase in buildings being depreciated, which are depreciated over a longer period of time than equipment.
- Noncapitalized equipment and repairs decreased by $5.9 million in 2015 primarily due to not having additional equipment and maintenance costs related to the Husky Stadium renovation and Husky Ballpark projects.
- Financing costs increased $2.6 million, as the financing costs were fully recognized in 2015.
- Other expenses increased $691 thousand in 2015 from 2014 due to additional costs for the Pac-12 Conference Office assessment.

**Operating Loss**

There was an operating loss of approximately $30.3 million in 2015. There were sufficient nonoperating revenues from contributions, investment income, and University funded tuition waivers to cover the operating losses for 2015.

**Economic Factors Affecting the Future**

The greatest factor that determines the amount of gate revenues and contributions for Intercollegiate Athletics is having winning seasons for the football team. Football revenue supports the operations of all 22 Intercollegiate Athletic programs. Additionally, an economic downturn would have a negative financial impact on Athletic programs.

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Statement of Net Position

June 30, 2015

**Assets and Deferred Outflows of Resources**

| | | |
|---|---|---|
| Current assets: | | |
| Cash and cash equivalents in the University of Washington Invested Funds Pool (note 2) | $ | 8,736,190 |
| Accounts receivable | | 7,648,464 |
| Prepaid expenses | | 1,257,251 |
| Total current assets | | 17,641,905 |
| Noncurrent assets: | | |
| Investments: | | |
| University of Washington Consolidated Endowment Fund (note 2) | | 27,602,270 |
| Endowments (note 2) | | 59,889,483 |
| Advances to University for capital projects | | 1,274,955 |
| Capital assets, less accumulated depreciation of $101,396,456 (note 3) | | 364,065,727 |
| Total noncurrent assets | | 452,832,435 |
| Total assets | | 470,474,340 |
| Pension deferred outflows of resources (note 7) | | 726,871 |
| Total assets and deferred outflows of resources | | 471,201,211 |

**Liabilities, Deferred Inflows of Resources, and Net Position**

| | | |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | | 5,660,647 |
| Accrued salaries and vacation payable | | 7,505,571 |
| Admission taxes payable | | 988,756 |
| Accrued interest payable | | 1,377 |
| Unearned income | | 17,794,055 |
| Capitalized equipment lease payable, current portion (note 5) | | 1,475,797 |
| Internal lending program payable, current portion (note 4) | | 4,181,483 |
| Total current liabilities | | 37,607,686 |
| Noncurrent liabilities: | | |
| Capitalized equipment lease payable, net of current portion (note 5) | | 7,113,764 |
| Internal lending program payable, net of current portion (note 4) | | 251,615,939 |
| Net pension liability (note 7) | | 3,761,644 |
| Total noncurrent liabilities | | 262,491,347 |
| Total liabilities | | 300,099,033 |
| Pension deferred inflows of resources (note 7) | | 1,606,167 |
| Net position: | | |
| Net investment in capital assets | | 99,678,744 |
| Restricted: | | |
| Nonexpendable (note 2) | | 47,586,520 |
| Expendable: | | |
| Expendable endowment principal (note 2) | | 1,062,325 |
| Expendable endowment gains | | 11,240,638 |
| Other expendable | | 582,137 |
| Unrestricted | | 9,345,647 |
| Total net position | | 169,496,011 |
| Total liabilities, deferred inflows of resources, and net position | $ | 471,201,211 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Statement of Revenue, Expenses, and Changes in Net Position

Year ended June 30, 2015

| | |
|---|---|
| Operating revenue: | |
| Gate ticket sales | $ 25,422,152 |
| NCAA/conference distributions | 35,761,948 |
| Sponsorships | 11,993,208 |
| Concessions, souvenirs, parking, and boat moorage | 3,295,618 |
| Trademarks and licensing | 713,588 |
| Facility income | 1,771,156 |
| Other | 860,145 |
| Total operating revenue | 79,817,815 |
| Operating expenses: | |
| Salaries and wages | 29,088,904 |
| Payroll taxes and employee benefits | 6,584,886 |
| Athletic student aid | 11,959,293 |
| Guarantees paid to visiting teams | 2,113,355 |
| Team travel | 6,008,183 |
| Day of game expenses | 6,749,070 |
| Direct facilities, maintenance, and utilities | 4,039,305 |
| Advertising | 1,728,355 |
| Uniforms and supplies | 6,204,882 |
| Training table | 2,558,318 |
| Department relations | 773,928 |
| Banquets and special events | 638,761 |
| Depreciation | 17,270,117 |
| Noncapitalized equipment and repairs | 2,545,820 |
| Institutional overhead | 1,747,945 |
| Medical expenses | 1,312,222 |
| Fund-raising, marketing, and promotions | 415,488 |
| Recruiting | 449,753 |
| Equipment | 3,845 |
| Other | 7,934,182 |
| Total operating expenses | 110,126,612 |
| Operating loss | (30,308,797) |
| Nonoperating revenues (expenses): | |
| Contributions | 22,777,825 |
| Investment income (expense) on Invested Funds | (110,683) |
| Investment income on Consolidated Endowment Fund (CEF) | 2,024,433 |
| Gain on investments | 2,704,298 |
| Loss on disposal of capital assets | (34,046) |
| University funded tuition waivers | 3,895,000 |
| Settlement agreement | 1,250,000 |
| Financing Cost on Stadium and Ballpark | (2,565,509) |
| Interest expense | (12,708,645) |
| Total nonoperating revenues (expenses) | 17,232,673 |
| Income (loss) before other revenues | (13,076,124) |
| Other revenues: | |
| Capital gifts | 6,762,971 |
| Gifts to permanent endowments | 3,404,439 |
| Total other revenues | 10,167,410 |
| Decrease in net position | (2,908,714) |
| Net position: | |
| Net position at beginning of year, as restated (note1(b)) | 172,404,725 |
| Net position at end of year | $ 169,496,011 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Statement of Cash Flows

Year ended June 30, 2015

| | |
|---|---|
| Cash flows from operating activities: | |
| Gate ticket sales | $ 24,430,570 |
| NCAA/conference distributions | 36,624,498 |
| Sponsorships | 7,571,283 |
| Concessions and souvenirs | 3,316,675 |
| Trademarks and licensing | 752,512 |
| Facility income | 1,721,865 |
| Other | 917,840 |
| Payments to suppliers | (39,780,312) |
| Payments to employees | (27,599,729) |
| Payments for benefits | (6,923,213) |
| Payments for scholarships | (11,961,836) |
| Net cash used in operating activities | (10,929,847) |
| Cash flows from noncapital financing activities: | |
| Contributions, excluding permanent endowments and capital | 22,777,825 |
| Contributions to permanent endowments | 3,404,439 |
| Settlement agreement | 781,250 |
| University funded tuition waivers | 3,895,000 |
| Net cash provided by noncapital financing activities | 30,858,514 |
| Cash flows from capital and related financing activities: | |
| Capital gifts received | 6,762,971 |
| Proceeds from Internal Lending Program | 4,176,075 |
| Acquisition and construction of capital assets | (11,047,673) |
| Financing cost paid on capital debt | (2,565,509) |
| Principal paid on capital debt | (4,767,981) |
| Interest paid on capital debt | (12,707,284) |
| Net cash used in capital and related financing activities | (20,149,401) |
| Cash flows from investing activities: | |
| Purchases of investments | (3,816,314) |
| Investment income | 1,912,392 |
| Net cash used in investing activities | (1,903,922) |
| Net decrease in cash and cash equivalents | (2,124,656) |
| Cash and cash equivalents at beginning of year | 10,860,846 |
| Cash and cash equivalents at end of year | 8,736,190 |
| Reconciliation of operating loss to net cash used in operating activities: | |
| Operating loss | (30,308,797) |
| Adjustments to reconcile operating loss to net cash used in operating activities: | |
| Depreciation expense | 17,270,117 |
| Changes in assets and liabilities: | |
| Increase in accounts receivable | (261,006) |
| Decrease in prepaid expenses | 35,445 |
| Increase in accounts payable | 3,173,822 |
| Decrease in unearned income | (1,074,073) |
| Increase in accrued salaries and vacation payable | 1,486,387 |
| Decrease in pension liability | (1,397,377) |
| Increase in admissions taxes payable | 145,635 |
| Net cash used in operating activities | $ (10,929,847) |
| Supplemental disclosure of noncash activities: | |
| Donated supplies | $ 2,623,669 |

See accompanying notes to financial statements.

## (1) Organization and Summary of Significant Accounting Policies

### *(a) Organization*

The University of Washington Department of Intercollegiate Athletics (Department or ICA) is an auxiliary enterprise within the University of Washington (the University). The records of the Department are maintained as part of the general records of the University.

### *(b) Basis of Presentation*

The financial statements of the Department have been prepared in accordance with the Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*. The Department is reporting as a special purpose government engaged in business-type activities (BTA). In accordance with BTA reporting, the Department presents a management's discussion and analysis, statement of net position, statement of revenues, expenses, and changes in net position, statement of cash flows, and notes to the financial statements. The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. The Department reports capital assets net of accumulated depreciation (as applicable) and reports depreciation expense in the statement of revenues, expenses, and changes in net position.

On July 1, 2014, ICA adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. This Statement requires governments providing defined benefit pensions to their employees to recognize their long-term obligation for pension benefits as a liability for the first time, along with the associated assets which have been set aside to fund the plan. Since the University participates in several cost sharing pension plans which are administered by the state of Washington Department of Retirement Systems (DRS), this statement will require the University to recognize its proportionate share of the statewide net pension liability or net pension asset for each of the plans in which it participates. The Statement also eliminates the method of amortizing the liability balances over several years and instead requires full recognition of the net liability upon implementation. Implementation of this standard resulted in the restatement of beginning unrestricted net position reducing it by $4,432,149. The University's proportionate share of the state's collective pension amounts are disclosed in note 7.

With the adoption of GASB Statement No. 68, net position was restated at July 1, 2014. Below is a reconciliation of the total net position as previously reported at June 30, 2014, to the restated net position.

| | |
|---|---|
| Net position at June 30, 2014, as previously reported | $ 176,836,874 |
| Effect of accounting and reporting entity changes | (4,432,149) |
| Net position at July 1, 2014, as restated | $ 172,404,725 |

### *(c) Capital Assets*

Expenditures for equipment and repairs that represent normal replacement of such equipment and routine maintenance of the buildings are expensed as incurred. Capital expenditures for facilities and equipment funded by the Department are reflected as capital assets on the Department's balance sheets. Buildings and equipment are stated at cost, or if acquired by gift, at fair market value at the date of the gift. Additions, replacements, major repairs, and renovations are capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 15–50 years for building components, 20–50 years for infrastructure and land improvements, and 5–7 years for equipment.

### *(d) Advances to University for Capital Projects*

Advances to University for capital projects represent the difference between the cash paid and the expenditures incurred by the University for various capital projects that are in process at year-end, which ICA expects to expense or capitalize in the next fiscal year.

### *(e) Payable to University for Construction in Progress and Retainage*

Construction in progress and retainage provided before year-end yet not paid by the Department is accrued as of year-end and recorded as a payable to the University.

### *(f) Unearned Income*

Funds received from the sale of tickets (which could be shared with visiting teams) for games to be played subsequent to June 30, 2015 are unearned. The Department's share of such receipts is recognized as income in the period in which the games are played, less any amount owed to visiting teams. At June 30, 2015, unearned revenues consist of the following:

| | 2015 |
|---|---|
| Advance sales of football tickets | $ 16,431,360 |
| Advance sales for men's and women's basketball | 296,390 |
| Other unearned income | 1,066,305 |
| | $ 17,794,055 |

### *(g) Contributions*

Contributions are recorded as income when all conditions have been met.

### *(h) Sponsorships*

Sponsorships revenue for donated advertising and supplies is recognized as an exchange transaction and is recorded in income when the related advertising or supplies are received.

The Department recorded $4.3 million in sponsorship revenue for these transactions in the year ended June 30, 2015.

### *(i) Income Taxes*

As a part of the University, the Department is exempt from federal income taxes, except to the extent of unrelated business taxable income. Unrelated business tax was not significant to the financial statements taken as a whole at June 30, 2015.

## (2) Cash and Cash Equivalents in the University of Washington Invested Funds Pool and Investments

The Department's cash and investments are managed by the University through the Treasurer of the Board of Regents.

The Department's funds on deposit with the University and nonendowment investments were invested in the University's Invested Funds Pool (IFP). The IFP is unrated and the principal balance in each account is available to be withdrawn at any time. Since the IFP funds can be withdrawn at any time, the IFP funds are recorded on the financial statements as cash and cash equivalents. The IFP funds are invested in highly liquid, shorter-term investments. For funds invested in the IFP, the University credits the Department with interest at rates established at the University's discretion (2.0% for fiscal year 2015) on the average month-end balance of IFP funds. The Department's cash and cash equivalents and University IFP investments represent 1% of the IFP balance as of June 30, 2015.

The Department purchases or sells units in the University's Consolidated Endowment Fund (CEF) on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed by the University based on the number of units held. The Department records its permanent endowments at fair value. Net appreciation/depreciation in the fair value is recorded as gain or loss on investments in the statements of revenue, expenses, and changes in net assets. For the investment portion of the CEF funds, the principal balance can be withdrawn at the end of each quarter. The Department earned investment income on these investment funds based on the performance of the University's CEF funds net of investment management and University administrative fees. The total return on the investments portion of the CEF funds for the year ended June 30, 2015 was approximately 15.8%. During fiscal year 2011, the Board of Regents adopted a new long-term spending policy for the CEF replacing the interim spending policy, which was effective in fiscal year 2010. Under the new policy, quarterly distributions to programs are based on an annual percentage rate of 4.0%, applied to the five-year rolling average of the CEF's market valuation. The new policy was effective with the December 2010 quarterly distributions with the five-year averaging period implemented incrementally. The administrative fee of 1.0% supporting campuswide fund-raising and stewardship activities (0.8%) and offsetting the internal cost of managing endowment assets (0.2%) continues, but is now based on a five-year average value similar to program distributions. The Department's endowments represent 3.1% of the CEF balance as of June 30, 2015.

At June 30, 2015, the fund balance of the Endowment and Expendable Endowment funds stated at fair value comprised the following:

| | | 2015 |
|---|---|---|
| Expendable endowments: | | |
| Graham* | $ | 429,923 |
| Spence* | | 632,402 |
| Endowments (including expendable gains) | | 58,827,158 |
| Total | $ | 59,889,483 |

* Expenditure of principal is permitted under certain circumstances.

The Department received $3,404,439 in endowment gifts in 2015, which is invested in the CEF.

***University of Washington Investment***

All of the Department's cash and cash equivalents are invested in the University of Washington's Invested Funds Pool. The following information is for the entire pool and are audited disclosures as a part of the University of Washington audit.

The Board of Regents of the University of Washington is responsible for the management of the University's investments. The Board establishes investment policy, which is carried out by the Chief Investment Officer. The University of Washington Investment Committee, comprising Board members and investment professionals, advises on matters relating to the management of the University's investment portfolios. The composition of the carrying amounts of investments by type at June 30, 2015 is listed below.

**University investments**

| Investment type | | Carrying value 2015 (In thousands) |
|---|---|---|
| Cash equivalents | $ | 403,978 |
| Fixed income | | 1,726,481 |
| Equity | | 1,733,102 |
| Nonmarketable alternatives | | 353,053 |
| Absolute return | | 561,999 |
| Real assets | | 189,447 |
| Miscellaneous | | 8,603 |
| Total investments | $ | 4,976,663 |

*Investment Pools* – The University combines most short-term cash balances into the Invested Funds Pool. At June 30, 2015, the Invested Funds Pool totaled $1,526,380,000. The Invested Funds Pool also owns units in the Consolidated Endowment Fund valued at $806,198,000 on June 30, 2015. By University policy, departments with qualifying funds in the Invested Funds Pool receive distributions based on their average balances and on the type of balance. Campus depositors received 2% in fiscal year 2015. Endowment operating and gift accounts received 3% in fiscal year 2015. The difference between the actual earnings of


(Continued)

the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The majority of the endowed funds are invested in a pooled fund called the Consolidated Endowment Fund (CEF). Individual endowments purchase units in the pool on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held. RCW 24.55 of the Washington State Code and the Uniform Prudent Management of Institutional Funds Act allow for total return expenditure under comprehensive prudent standards.

*Interest Rate Risk* – The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed-income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform, while controlling the interest rate risk in the portfolio. The weighted average effective duration of the University's fixed-income portfolio was 1.81 years at June 30, 2015.

*Credit Risk* – Fixed-income securities are subject to credit risk, which is the risk that the issuer or other counterparty to a financial instrument will not fulfill its obligations, or that negative perceptions of the issuer's ability to make these payments will cause prices to decline. Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University Investment Policies limit fixed-income exposure to investment grade assets. The Investment Policy for the Invested Funds' cash pool requires each manager to maintain an average quality rating of "AA" as issued by a nationally recognized rating organization. The Invested Funds' liquidity pool requires each manager to maintain an average quality rating of "A" and to hold 25% of their portfolios in government and government agency issues. The Investment Policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investment to investment grade credits.

Duration and credit risk figures at June 30, 2015 exclude $36,027,000, of fixed-income securities held outside the CEF and the Invested Funds Pool. These amounts make up 1.69% of the University's fixed income investments (including cash equivalents), and are not included in the duration figures detailed below.

The composition of the fixed-income securities at June 30, 2015, along with credit quality and effective duration measures is summarized below:

**Fixed income credit quality and effective duration**

| Investments | U.S. government | Investment grade | Noninvestment grade | Not rated | Total | Duration (in years) |
|---|---|---|---|---|---|---|
| | | | (Dollars in thousands) | | | |
| 2015: | | | | | | |
| U.S. Treasuries | $ 842,525 | — | — | — | 842,525 | 1.43 |
| U.S. government agency | 644,721 | — | — | — | 644,721 | 2.46 |
| Mortgage backed | — | 107,070 | 75,060 | 22,415 | 204,545 | 2.01 |
| Asset backed | — | 195,968 | 6,998 | 24,111 | 227,077 | 1.73 |
| Corporate and other | — | 175,364 | — | 200 | 175,564 | 1.14 |
| Total | $ 1,487,246 | 478,402 | 82,058 | 46,726 | 2,094,432 | 1.81 |

*Foreign Currency Risk* – The University's Investment Policies permit investments in international equity and other asset classes, which can include foreign currency exposure. The University held non-U.S. denominated securities at June 30, 2015 of 1,195,070,000.

**Investments denominated in foreign currency**

| | **June 30, 2015** (In thousands) |
|---|---|
| Euro (EUR) | $ 174,487 |
| Chinese Renminbi (RMB) | 211,184 |
| Indian Rupee (INR) | 112,679 |
| Japanese Yen (JPY) | 110,617 |
| Brazilian Real (BRL) | 54,225 |
| Russian Ruble (RUB) | 36,218 |
| British Pound (GBP) | 54,880 |
| Hong Kong Dollar (HKD) | 60,046 |
| South Korean Won (KRW) | 56,835 |
| Canadian Dollar (CAD) | 35,385 |
| Swiss Franc (CHF) | 39,061 |
| Taiwanese Dollar (TWD) | 27,055 |
| Philippine Peso (PHP) | 29,100 |
| Mexican Peso (MXN) | 23,898 |
| Remaining Currencies | 169,400 |
| Total | $ 1,195,070 |

## (3) Capital Assets

Capitalized asset activity for the year ended June 30, 2015 is summarized as follows:

| | **Balance at June 30, 2014** | **Additions/ transfers** | **Retirements** | **Balance at June 30, 2015** |
|---|---|---|---|---|
| Buildings | $ 447,756,688 | 1,978,643 | — | 449,735,331 |
| Furniture, fixtures, and equipment | 13,338,433 | 969,804 | (276,987) | 14,031,250 |
| Construction in progress* | 1,604,339 | 91,263 | — | 1,695,602 |
| Total | $ 462,699,460 | 3,039,710 | (276,987) | 465,462,183 |

| | | Balance at June 30, 2014 | Additions/ transfers | Retirements | Balance at June 30, 2015 |
|---|---|---|---|---|---|
| Less accumulated depreciation: | | | | | |
| Buildings | $ | 77,120,405 | 14,690,413 | — | 91,810,818 |
| Furniture, fixtures, and equipment | | 7,248,875 | 2,579,704 | (242,941) | 9,585,638 |
| Total accumulated depreciation | | 84,369,280 | 17,270,117 | (242,941) | 101,396,456 |
| Capital assets, net | $ | 378,330,180 | (14,230,407) | (34,046) | 364,065,727 |

* Nondepreciable

## (4) Internal Lending Program

In February 2012, ICA began drawing money from the ILP for the costs related to renovating Husky Stadium. The Board of Regents at their November 18, 2010 meeting approved ICA to use the ILP for up to $250 million in project and capitalized interest costs for the renovation of Husky Stadium. On November 11, 2011, the Board of Regents approved to increase ICA's use of the ILP to $261.5 million for the costs of renovating Husky Stadium and adding a Sports Medicine and Sport Performance Center. Any amounts drawn from the ILP greater than $261.5 million will be funded by the Department. At the end of June 2015, ICA had drawn $259.1 million from the ILP relating to the construction of the Husky Stadium renovation and Husky Ballpark. Capitalized interest at June 30, 2015 was $8.5 million.

The purpose of the ILP is to lower the University's overall cost of capital and provide internal borrowing units with a stable and predictable borrowing rate. The ILP will make loans to internal borrowers at a uniform internal lending rate. These loans will be funded through the issuance of University General Revenue bonds and notes. ILP program policies include a provision for a rate stabilization reserve and a provision for rate adjustments if necessary.

Under the terms of the ILP, rate adjustments will apply to all outstanding debt obligations, including debt issued prior to the ILP implementation. The ILP lending rate will be reviewed annually, and a preliminary indication of a rate adjustment will be announced to ILP participants 12 months in advance of the effective date. Final rate adjustments require approval by the Board of Regents.

Future principal and interest payments due through maturity dates are as follows:

| | | Principal | Interest |
|---|---|---|---|
| Years ending June 30: | | | |
| 2016 | | 4,181,483 | 12,060,128 |
| 2017 | | 4,384,485 | 11,857,125 |
| 2018 | | 4,597,343 | 11,644,268 |
| 2019 | | 4,820,534 | 11,421,077 |
| 2020 | | 5,054,561 | 11,187,051 |
| Thereafter | | 232,759,016 | 158,392,998 |
| | $ | 255,797,422 | 216,562,647 |

Internal Lending Program activity for the year ended June 30, 2015 is summarized as follows:

| | | |
|---|---|---|
| Balance as of June 30, 2014 | $ | 254,940,379 |
| Additions | | 4,176,075 |
| Reductions | | (3,319,032) |
| Balance as of June 30, 2015 | $ | 255,797,422 |

## (5) Capital Lease

Future minimum lease payments under capital lease and the present value of the net minimum lease payments as of June 30, 2015 are as follows:

| | | Future payments |
|---|---|---|
| Years ending June 30: | | |
| 2016 | $ | 1,653,481 |
| 2017 | | 1,605,808 |
| 2018 | | 1,077,449 |
| 2019 | | 997,934 |
| 2020 | | 997,934 |
| Thereafter | | 2,993,802 |
| Total minimum lease payments | | 9,326,408 |
| Less amount representing interest cost | | 736,847 |
| Present value of minimum payments | $ | 8,589,561 |

Equipment under capital lease are as follows:

| | Balance at June 30, 2014 | Additions | Retirements | Balance at June 30, 2015 |
|---|---|---|---|---|
| Equipment | $ 7,674,654 | — | — | 7,674,654 |
| Total | 7,674,654 | — | — | 7,674,654 |
| Less accumulated depreciation: Equipment | 3,418,209 | 1,980,448 | — | 5,398,657 |
| Total accumulated depreciation | 3,418,209 | 1,980,448 | — | 5,398,657 |
| Leased capital assets, net | $ 4,256,445 | (1,980,448) | — | 2,275,997 |

## (6) Related-Party Transactions

The University provides support to the Department by performing the following services:

- Providing use of University buildings and equipment
- Serving as the depository, purchasing, and disbursing agent
- Providing certain administrative and accounting services

In addition, the Department purchases operating and office supplies and other services from the University and is allocated institutional overhead from the University for services provided and payment for utility costs. The institutional overhead allocated from the University for fiscal year 2015 was $1,747,945.

The Department is covered by the University's self-insurance program and is responsible for the first $100,000 of costs in general, automobile, and employment practices liability claims. Payments over $100,000 are covered by the University's self-insurance program and excess carriers, except that in claims related to coaches' contracts or the acts of trainers and non-University physicians to the athletes' medical services program, all costs are the exclusive responsibility of the Department.

## (7) Pension Plans

The University offers several contributory pension plans administered by the Washington State Department of Retirement Systems. ICA has employees in the Public Employee's Retirement System Plan, which is a defined-benefit retirement plan. Additionally, the University offers the University of Washington Retirement plan, a defined-contribution plan, and the University of Washington Supplemental Retirement plan, a defined-benefit plan.

### Public Employees' Retirement System (PERS)

PERS was established in 1947 and its retirement benefit provisions are contained in chapters 41.34 and 41.40 of the Revised Code of Washington (RCW). PERS is a cost-sharing multiple-employer retirement system



(Continued)

comprised of three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined benefit plans, and PERS Plan 3 is a defined benefit plan with a defined contribution component. PERS members include higher education employees not participating in other higher education retirement programs.

PERS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3, and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

**The Pension Plans' Fiduciary Net Positions**

The pension plans' fiduciary net positions have been determined on the same basis used by the pension plans. Washington State DRS financial statements have been prepared in conformity with generally accepted accounting principles (GAAP). The retirement plans are accounted for in pension trust funds using the flow of economic resources measurement focus and the accrual basis of accounting. Plan member contributions are recognized as revenues in the period in which the contributions are earned. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

The Washington State Investment Board (WSIB) has been authorized by statute (chapter 43.33A of the RCW) as having the investment management responsibility for the pension funds. Investments are reported at fair value, and unrealized gains and losses are included as investment income in the Statement of Changes in Fiduciary Net Position presented in the DRS Comprehensive Annual Financial Report. Purchases and sales of investments are recorded on a trade-date basis.

DRS publishes an annual report for retirement plans which is available at:
http://www.drs.wa.gov/administration/annual-report/

**Actuarial assumptions**

The total pension liability for each plan was determined by an actuarial valuation as of June 30, 2013, with the results rolled forward to June 30, 2014. The following actuarial assumptions have been applied to all prior periods included in the measurement:

| | |
|---|---|
| Inflation | 3.0% total economic inflation, 3.75% salary inflation |
| Salary Increase | Expected to grow by promotions and longevity in addition to the salary inflation assumption |
| Investment rate of return | 7.50% |

Mortality rates were based on the RP-2000 Combined Healthy Table and Combined Disabled Table published by the Society of Actuaries. The Washington State Office of the State Actuary (OSA) applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100% Scale BB. Mortality rates are applied on a generational basis, meaning members are assumed to receive additional mortality improvements in each future year, throughout their lifetime.

The actuarial assumptions used in the June 30, 2013 valuation were based on the results of OSA's 2007–2012 Experience Study. Additional assumptions for subsequent events and law changes are current as of the 2013 actuarial valuation report.

**Discount rate**

The discount rate used to measure the total pension liabilities was 7.50% for all plans in which the University participates. To determine the discount rate, an asset sufficiency test was completed to test whether each pension plan's fiduciary net position was sufficient to make all projected future benefit payments of current plan members. Consistent with current law, the completed asset sufficiency tests for PERS included an assumed 7.70% long-term discount rate to determine funding liabilities for calculating future contribution rate requirements.

Consistent with the long-term expected rate of return, a 7.50% future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue to be made at contractually required rates (including the component of PERS 2/3 employer rates pertaining to the unfunded actuarial accrued liability for PERS 1 as provided for in chapter 41.45 of the RCW).

Based on those assumptions, the fiduciary net position for each pension plan was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.50% on pension plan investments was applied to determine the total pension liability.

**Sensitivity of the net pension liability to changes in the discount rate**

The following table presents ICA's net pension liability calculated using the discount rate of 7.50%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50%) or 1-percentage-point higher (8.50%) than the current rate.

**Discount Rate Sensibility**
**Net Pension Liability**
**(Dollars in thousands)**

| Plan | | 1% Decrease | Current Discount Rate | 1% Increase |
|---|---|---|---|---|
| PERS 1 | $ | 3,139 | 2,547 | 2,038 |
| PERS 2/3 | | 5,067 | 1,215 | (1,728) |

**Long-term expected rate of return**

The long-term expected rate of return of 7.50% on pension plan investments was determined by the WSIB. The rate approximately equals the median of the simulated investment returns over a 50-year time horizon, increased slightly to remove WSIB's implicit, small, short-term downward adjustment due to assumed mean reversion. WSIB's implicit short-term adjustment, while small and appropriate over a 10- to 15-year period, becomes amplified over a 50-year measurement period.

The long-term expected rate of return was determined by the WSIB using a building-block method in which a best estimate of expected future rates of return (expected returns, net of pension plan investment expense, but including inflation) are developed for each major asset class by the WSIB. Those expected returns make up one component of WSIB's Capital Market Assumptions (CMAs).

- Expected annual return
- Standard deviation of the annual return
- Correlations between the annual returns of each asset class with every other asset class

WSIB uses the CMAs and their target asset allocation to simulate future investment returns over various time horizons.

Best estimates of arithmetic real rates of return for each major asset class included in the target asset allocation for each pension plan, as of June 30, 2014, are summarized in the following table:

| Asset Class | Target Allocation | Long-term Expected Real Rate of Return |
|---|---|---|
| Fixed Income | 20.00% | 0.80% |
| Tangible Assets | 5.00% | 4.10% |
| Real Estate | 15.00% | 5.30% |
| Global Equity | 37.00% | 6.05% |
| Private Equity | 23.00% | 9.05% |

The inflation component used to create the above table is 2.70%, and represents WSIB's most recent long-term estimate of broad economic inflation.

**Employer contribution rates**

Employer contribution rates are developed in accordance with chapter 41.45 of the RCW by the OSA, and include an administrative expense component that is currently set at 0.18%. The statute provides authority to the Pension Funding Council to adopt changes to economic assumptions and contribution rates.

**ICA proportionate share**

Collective pension amounts are determined as of a measurement date, which can be no earlier than an employer's prior fiscal year. The measurement date for the net pension liabilities recorded by the University as of June 30, 2015 was June 30, 2014. University contributions received and processed by DRS during the fiscal year ended June 30, 2014 have been used as the basis for determining the University's proportionate share of the collective pension amounts reported by DRS in their June 30, 2014 Schedules of Employer and Nonemployer Allocations for all plans in which the University participates.

ICA's proportionate share for the year ended June 30, 2015 was determined by the proportion of ICA's employer contributions to total employer contributions as of the measurement date:

| Plan | Proportionate share for year ended June 30, 2015 |
|---|---|
| PERS 1 | 0.51% |
| PERS 2/3 | 0.61% |

**ICA aggregated balances**

ICA's aggregated balances of net pension liabilities and deferrals as of June 30, 2015 are presented in the table below.

**June 30, 2015**
**(Dollars in thousands)**

| Plan | | Net pension liability | Deferred outflows | Deferred inflows |
|---|---|---|---|---|
| PERS 1 | $ | 2,547 | 231 | 318 |
| PERS 2/3 | | 1,215 | 496 | 1,288 |
| Total | $ | 3,762 | 727 | 1,606 |

**PERS Plan 1**

PERS Plan 1 is closed to new entrants.

**Vesting**

PERS Plan 1 members were vested after the completion of five years of eligible service.

**Benefits provided**

PERS Plan 1 provides retirement, disability, and death benefits. Retirement benefits are determined as 2% of the member's average final compensation (AFC) times the member's years of service. The AFC is the average of the member's 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service.

Members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

**Contributions**

The PERS Plan 1 employer contribution rate for the fiscal years ended June 30, 2015 and 2014 was 9.21% in both years. The ICA's contributions to PERS Plan 1 for the years ended June 30, 2015 was $231,000.

**Proportionate share of PERS Plan 1 pension expense and deferrals related to pensions**

ICA's proportionate share of PERS Plan 1 pension expense for the fiscal year ended June 30, 2015 was $441,000 and is reported on the statement of revenues, expenses and changes in net position in benefits expense.

ICA's deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 1 as of June 30, 2015 are presented in the following table:

| Description | | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|---|---|
| Difference between projected and actual earnings on pension plan investments, net | $ | — | 318,000 |
| ICA's contributions to plans subsequent to the measurement date of collective net pension liability | | 231,000 | — |
| Total | $ | 231,000 | 318,000 |

Deferred outflows of resources related to ICA contributions subsequent to the measurement date of $231,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred inflows of resources pertaining to PERS Plan 1 will be recognized in pension expense as follows:

| | | |
|---|---|---|
| 2016 | $ | (79,500) |
| 2017 | | (79,500) |
| 2018 | | (79,500) |
| 2019 | | (79,500) |
| 2020 | | — |
| Thereafter | | — |
| Total | $ | (318,000) |

## PERS Plan 2/3

### Vesting

PERS Plan 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after 10 years of service, or after five years of service if 12 months of that service are earned after age 44.

**Benefits provided**

PERS Plan 2/3 provides retirement, disability, and death benefits. Retirement benefits are determined as 2% the member's average final compensation (AFC) times the member's years of service for Plan 2, and one percent of AFC times the member's years of service for Plan 3.

The AFC is the monthly average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at age 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age, for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 2, 2013:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the Consumer Price Index), capped at 3% annually, and a one-time duty-related death benefit, if found eligible by the Washington State Department of Labor and Industries.

**Contributions**

The PERS Plan 2/3 employer contribution rate for the fiscal years ended June 30, 2015 and 2014 was 9.21% in both years. The Plan 2/3 employer rate includes a component to address the PERS Plan 1 unfunded actuarial accrued liability. ICA's contributions to PERS Plan 2/3 for the years ended June 30, 2015 was $263,000, as determined by rates established in accordance with RCW 41.45.

**Proportionate share of PERS Plan 2/3 pension expense and deferrals related to pensions**

ICA's proportionate share of PERS Plan 2/3 pension expense for the fiscal year ended June 30, 2015 was $262,000, and is reported on the statement of revenues, expenses and changes in net position in benefits expense.

ICA's deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 as of June 30, 2015 are presented in the following table:

| Description | | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|---|---|
| Difference between projected and actual earnings on pension plan investments, net | $ | — | 1,288,000 |
| Changes in ICA's proprotion | | 233,000 | — |
| ICA's contributions to plans subsequent to the measurement date of collective net pension liability | | 263,000 | — |
| Total | $ | 496,000 | 1,288,000 |

Deferred outflows of resources related to ICA contributions subsequent to the measurement date of $233,000 will be recognized as a reduction of the net pension liability as of June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources pertaining to PERS Plan 2/3 will be recognized in pension expense as follows:

| | | |
|---|---|---|
| 2016 | $ | (66,571) |
| 2017 | | (66,571) |
| 2018 | | (66,571) |
| 2019 | | (33,287) |
| 2020 | | — |
| Thereafter | | — |
| Total | $ | (233,000) |

## UNIVERSITY OF WASHINGTON RETIREMENT PLAN (403(B))

Faculty, librarians, and professional staff are eligible to participate in the University of Washington Retirement Plan, a 403(b) defined-contribution plan administered by the University.

403(b) Plan Description: Contributions to the plan are invested by participants in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations. Benefits from the plan are available upon separation or retirement at the member's option. RCW 28B.10.400 et. seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

The number of participants in the 403(b) plan for the years ended June 30, 2015 was 15,415.

403(b) Funding Policy: Employee contribution rates, based on age, are 5%, 7.5%, or 10% of salary. The University matches the contributions of employees. Within parameters established by the legislature, contribution requirements may be established or amended by the University of Washington Board of Regents. Employee and employer contributions for the years ended June 30, 2015 was $105,266,000.

## UNIVERSITY OF WASHINGTON SUPPLEMENTAL RETIREMENT PLAN (401 (A))

The University of Washington Supplemental Retirement Plan (UWSRP), a 401(a) defined-benefit retirement plan, operates in tandem with the 403(b) plan, and is closed to new participants.

The Unfunded Actuarial Accrued Liability (UAL) and Annual Required Contribution (ARC) as of July 1 of the respective years were:

| | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| UAL | $ | 373,711 | 292,535 |
| Normal cost | | 14,250 | 9,529 |
| Amortization of UAL, including interest | | 38,807 | 29,021 |
| ARC | | 53,057 | 38,550 |

| Actuarial assumptions | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| Payroll covered by Plan | $ | 1,050,000 | 1,047,000 |
| Rate of return assumption | | 4.00% | 4.25% |
| Salary increases for years 1 and 2 | | 3.75% | 3.00% |
| Salary increase for third year | | 3.75% | 3.00% |
| Salary increases thereafter | | 3.75% | 3.00% |

The UAL and ARC were established using the entry age normal cost method.

The following table reflects the activity in the Net Pension Obligation for the years ended June 30, 2015 and 2014:

| | | 2015 (In thousands) | 2014 (In thousands) |
|---|---|---|---|
| Balance at beginning of fiscal year | $ | 198,895 | 163,372 |
| ARC | | 53,057 | 38,550 |
| Payments to beneficiaries | | (3,709) | (3,027) |
| Balance at end of fiscal year | $ | 248,243 | 198,895 |

***Other Postemployment Benefits (OPEB)***

The University funds OPEB obligations at a university-wide level on a pay-as-you-go basis. Disclosure information, as required under GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, does not exist at the Department level, and as a result, the Actuarial Accrued Liability (AAL) is not available for auxiliary entities. The University is ultimately responsible for the payment of the obligation; therefore, the (ARC) is not recorded on the Department's financial statements.


(Continued)

## (8) Commitments and Contingencies

The Department is subject to various claims and lawsuits that are covered by the University's self-insurance fund, subject to a deductible of $100,000 per occurrence.

## (9) Subsequent Events

On September 10, 2015, UW regents approved a naming rights agreement with Alaska Airlines for the naming rights of Husky Stadium, Hec Edmundson Pavilion, and the athletic village. The $40 million agreement over 10 years begins September 1, 2016. A $1 million dollar payment will be paid to ICA during fiscal year 2016.

The Department has evaluated subsequent events from the statements of net position date through November 18, 2015, the date at which the financial statements were available to be issued.

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Schedules of Required Supplementary Information

June 30, 2015

Unaudited – see accompanying independent auditor's report

(Dollar amounts in thousands)

The Schedules of Required Supplementary Information below reflect information for the University of Washington as a whole due to the constraints of available information for the University of Washington Department of Intercollegiate Athletics.

### Schedule of the University's Proportionate Share of the Net Pension Liability

### PERS 1 Pension Plan

| | | |
|---|---|---|
| University's proportion of the net pension liability (asset) | | 8.28243% |
| University's proportionate share of the net pension liability (asset) | $ | 417,231 |
| University's covered-employee payroll | | 25,376 |
| University's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll | | 1,644.20% |
| Plan fiduciary net position as a percentage of the total pension liability | | 61.19 |

### Schedule of the University's Contributions

### PERS 1 Pension Plan

| | | |
|---|---|---|
| Contractually required contribution | $ | 2,311 |
| Contributions in relation to the contractually required contribution | | 2,313 |
| Contribution deficiency (excess) | | (2) |
| University's covered-employee payroll | | 25,376 |
| Contributions as a percentage of covered-employee payroll | | 9.11% |

### Schedule of the University's Proportionate Share of the Net Pension Liability

### PERS 2/3 Pension Plan

| | | |
|---|---|---|
| University's proportion of the net pension liability (asset) | | 10.004398% |
| University's proportionate share of the net pension liability (asset) | $ | 202,225 |
| University's covered-employee payroll | | 856,839 |
| University's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll | | 23.60% |
| Plan fiduciary net position as a percentage of the total pension liability | | 93.29 |

### Schedule of the University's Contributions

### PERS 2/3 Pension Plan

| | | |
|---|---|---|
| Contractually required contribution | $ | 78,164 |
| Contributions in relation to the contractually required contribution | | 78,160 |
| Contribution deficiency (excess) | | 4 |
| University's covered-employee payroll | | 856,839 |
| Contributions as a percentage of covered-employee payroll | | 9.12% |

**Notes to Schedules of Required Supplementary Information (Unaudited) for the Year Ended June 30, 2015**

*Changes of benefit terms.* Amounts reported in 2015 reflect no change in benefit terms.

*Changes of assumptions.* Amounts reported in 2015 reflect no changes in assumptions.

Schedule 2

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Operating and Other Revenue by Specific Function

Year ended June 30, 2015

| | Men's football | Men's basketball | Women's basketball | Other sports Men's | Other sports Women's | Administration and other | Total |
|---|---|---|---|---|---|---|---|
| Gate ticket sales revenue: | | | | | | | |
| Ticket sales for home events | $ 22,116,985 | 2,516,981 | 173,785 | 204,564 | 581,390 | — | 25,593,705 |
| Admission taxes | (1,052,444) | (119,799) | (8,258) | (9,686) | (27,691) | — | (1,217,878) |
| Ticket-processing fees | 302,829 | 39,697 | 4,892 | 3,613 | 25,294 | — | 376,325 |
| | 21,367,370 | 2,436,879 | 170,419 | 198,491 | 578,993 | — | 24,752,152 |
| University's share of gate revenue for away games | 400,000 | 215,000 | — | 42,420 | 12,580 | — | 670,000 |
| Total gate ticket sales revenue | 21,767,370 | 2,651,879 | 170,419 | 240,911 | 591,573 | — | 25,422,152 |
| NCAA/conference distributions: | | | | | | | |
| PAC-12 television share | 22,067,130 | 2,556,675 | — | — | — | — | 24,623,805 |
| PAC-12 rose/other bowl shares | 5,109,272 | — | — | — | — | — | 5,109,272 |
| Bowl Participation | 1,000,000 | — | — | — | — | — | 1,000,000 |
| NCAA MBB tournament | — | 1,235,500 | — | — | — | — | 1,235,500 |
| Football Pac-12 Championship Game | 294,584 | — | — | — | — | — | 294,584 |
| MBB PAC-12 tournament | — | (37,917) | — | — | — | — | (37,917) |
| Pac-12 Network Share | 1,425,875 | 251,625 | — | — | — | — | 1,677,500 |
| Other | — | — | — | — | — | 1,859,204 | 1,859,204 |
| Total NCAA/conference distributions | 29,896,861 | 4,005,883 | — | — | — | 1,859,204 | 35,761,948 |
| Royalties, advertisements, and sponsorships: | | | | | | | |
| Sponsorships | 5,000 | — | — | 38,374 | 59,909 | 7,537,901 | 7,641,184 |
| Donated advertising | — | — | — | — | — | 1,728,355 | 1,728,355 |
| Trademarks and licensing | — | — | — | — | — | 713,588 | 713,588 |
| Donated supplies | 860,000 | 160,000 | 160,000 | 554,200 | 712,800 | 176,669 | 2,623,669 |
| Total royalties, advertisements, and sponsorships | 865,000 | 160,000 | 160,000 | 592,574 | 772,709 | 10,156,513 | 12,706,796 |
| Contributions | 17,213,437 | 2,706,931 | 42,915 | 1,016,967 | 868,505 | 929,070 | 22,777,825 |
| Capital gifts | — | — | — | — | — | 6,762,971 | 6,762,971 |
| Gifts to permanent endowments | — | — | — | — | — | 3,404,439 | 3,404,439 |
| Gain on investments | — | — | — | — | — | 2,704,298 | 2,704,298 |
| Investment income, net | — | — | — | — | — | 1,913,750 | 1,913,750 |
| University funded tuition waivers | — | — | — | — | — | 3,895,000 | 3,895,000 |
| Concessions, souvenirs, parking, and boat moorage | 2,595,266 | 84,951 | 23,814 | 16,165 | 35,753 | 539,669 | 3,295,618 |
| Facility income | — | — | — | — | — | 1,771,156 | 1,771,156 |
| Settlement Agreement | — | — | — | — | — | 1,250,000 | 1,250,000 |
| Other | 56,306 | — | (24) | 296,785 | 274,215 | 232,863 | 860,145 |
| Total revenue | $ 72,394,240 | 9,609,644 | 397,124 | 2,163,402 | 2,542,755 | 35,418,933 | 122,526,098 |

See accompanying independent auditors' report.

Schedule 3

**UNIVERSITY OF WASHINGTON**
**DEPARTMENT OF INTERCOLLEGIATE ATHLETICS**

Operating Expenses and Other Deductions by Specific Function

Year ended June 30, 2015

| | Men's football | Men's basketball | Women's basketball | Other sports: Men's | Other sports: Women's | Postseason activity | Administration | Facilities maintenance and event management | Department relations and visiting recruits | Total |
|---|---|---|---|---|---|---|---|---|---|---|
| Operating expenses: | | | | | | | | | | |
| Salaries and wages | $ 8,109,270 | 2,684,629 | 952,793 | 2,041,956 | 2,803,482 | 187,765 | 10,463,071 | 1,841,162 | 4,776 | 29,088,904 |
| Payroll taxes and employee benefits | 1,588,401 | 549,187 | 245,761 | 522,102 | 713,282 | 28,663 | 2,369,443 | 554,853 | 13,194 | 6,584,886 |
| Athletic student aid | 3,336,438 | 491,412 | 498,845 | 2,367,256 | 4,207,966 | — | 934,149 | — | 123,227 | 11,959,293 |
| Guarantees paid to visiting teams | 1,625,000 | 379,912 | 46,000 | 27,331 | 35,112 | — | — | — | — | 2,113,355 |
| Team travel | 1,355,751 | 456,592 | 341,920 | 877,189 | 1,281,044 | 1,436,431 | 222,290 | — | 36,966 | 6,008,183 |
| Day of game expenses | 1,830,295 | 253,224 | 146,222 | 196,338 | 319,322 | 26,188 | 696,317 | 501,920 | 2,779,244 | 6,749,070 |
| Direct facilities, maintenance, and utilities | 173,092 | — | — | 69,979 | 94,743 | — | 2,671,975 | 1,029,516 | — | 4,039,305 |
| Donated advertising | — | — | — | — | — | — | 1,728,355 | — | — | 1,728,355 |
| Uniforms and supplies | 1,431,122 | 79,985 | 39,370 | 366,946 | 465,101 | 138,539 | 782,945 | 294,470 | 6,404 | 3,604,882 |
| Donated supplies | 860,000 | 160,000 | 160,000 | 554,200 | 712,800 | — | 153,000 | — | — | 2,600,000 |
| Institutional overhead | — | — | — | — | — | — | 1,747,945 | — | — | 1,747,945 |
| Medical expenses | 37,736 | 2,000 | 1,531 | 13,407 | 17,940 | — | 1,220,382 | — | 19,226 | 1,312,222 |
| Fund-raising, marketing, and promotions | — | — | — | — | 10,062 | — | 405,426 | — | — | 415,488 |
| Recruiting | — | — | — | — | — | — | — | — | 449,753 | 449,753 |
| Equipment | — | — | — | — | — | — | — | 3,845 | — | 3,845 |
| Training table | 720,779 | 28,044 | 14,214 | 144,624 | 220,075 | 139,384 | 206,678 | — | 1,084,520 | 2,558,318 |
| Department relations | 58,973 | 10,872 | 3,788 | 38,293 | 44,048 | 39,411 | 55,123 | 1,573 | 521,847 | 773,928 |
| Banquets and special events | 19,142 | 14,299 | 1,599 | 58,940 | 24,381 | — | 139,954 | — | 380,446 | 638,761 |
| Depreciation | — | — | — | — | — | — | 17,270,117 | — | — | 17,270,117 |
| Noncapitalized equipment and repairs | — | — | — | — | — | — | — | 2,545,820 | — | 2,545,820 |
| Other | 450,051 | 247,465 | 168,389 | 399,039 | 528,683 | 109,589 | 4,795,900 | 38,725 | 1,196,341 | 7,934,182 |
| Total operating expenses | 21,596,050 | 5,357,621 | 2,620,432 | 7,677,600 | 11,478,041 | 2,105,970 | 45,863,070 | 6,811,884 | 6,615,944 | 110,126,612 |
| Other deductions: | | | | | | | | | | |
| Loss on disposal of capital assets | — | — | — | — | — | — | — | 34,046 | — | 34,046 |
| Financing Cost | — | — | — | — | — | — | 2,565,509 | — | — | 2,565,509 |
| Interest expense | — | — | — | — | — | — | 12,708,645 | — | — | 12,708,645 |
| Total other deductions | — | — | — | — | — | — | 15,274,154 | 34,046 | — | 15,308,200 |
| Total operating expenses and other deductions | $ 21,596,050 | 5,357,621 | 2,620,432 | 7,677,600 | 11,478,041 | 2,105,970 | 61,137,224 | 6,845,930 | 6,615,944 | 125,434,812 |

See accompanying independent auditors' report.

**UNIVERSITY OF WASHINGTON MEDICAL CENTER**

(A Division of the University of Washington)

Financial Statements

June 30, 2015

(With Independent Auditors' Report Thereon)

**UNIVERSITY OF WASHINGTON MEDICAL CENTER**
(A Division of the University of Washington)

## Table of Contents

**KPMG LLP**
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

# Independent Auditors' Report

The University of Washington
UW Medicine Board:

We have audited the accompanying financial statements of University of Washington Medical Center (UW Medical Center), which comprise the statement of net position as of June 30, 2015, and the related statements of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements.

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

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

## *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our 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 financial statements are free from material misstatement.

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

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

## *Emphasis of Matter*

As discussed in note 1, the financial statements of UW Medical Center, a division of the University of Washington (the University), are intended to present the net position, the changes in net position, and the cash flows of only that portion of the business-type activities of the University that are attributable to the transactions of UW Medical Center. They do not purport to, and do not, present fairly the net position of the University as of June 30, 2015, the change in its net position, or its cash flows for the year ended, in accordance with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

As discussed in note 2 to the financial statements, on July 1, 2014, UW Medical Center adopted new accounting guidance requiring governments providing defined benefit pensions to their employees to recognize their proportionate share of the pension plan's net pension liability or net pension asset, as well as recognizing most changes in the net pension liability within pension expense. Our opinion is not modified with respect to this matter.

***Opinion***

In our opinion, the financial statements referred to above present fairly in all material respects, the financial position of University of Washington Medical Center as of June 30, 2015, and the results of its operation and its cash flow for the years then ended, in accordance with U.S. generally accepted accounting principles.

***Other Matter***

U.S. generally accepted accounting principles require that the Management's Discussion and Analysis on pages 3 through 15, and the schedules of required supplementary information on page 48, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

KPMG LLP

Seattle, Washington
October 16, 2015

The following discussion and analysis provides an overview of the financial position and activities of the University of Washington Medical Center (UW Medical Center), for the years ended June 30, 2015 and 2014. This discussion has been prepared by management and is designed to focus on current activities, resulting changes, and current known facts and should be read in conjunction with the audited financial statements and accompanying notes that follow this section.

UW Medical Center is a division of the University of Washington (the University) and part of UW Medicine that includes: Harborview Medical Center (Harborview), Northwest Hospital & Medical Center (Northwest Hospital), Valley Medical Center (VMC), UW Physicians Network dba UW Neighborhood Clinics (UWNC), UW Physicians (UWP), the UW School of Medicine (School), and Airlift Northwest (Airlift).

**Using the Financial Statements**

UW Medical Center's financial statements consist of three statements: statement of net position; statement of revenues, expenses, and changes in net position; and statement of cash flows. These financial statements and related notes provide information about the activities of UW Medical Center, including resources held by UW Medical Center but restricted for specific purposes by contributors, grantors, or enabling legislation.

The statement of net position include all of UW Medical Center's assets and liabilities, using the accrual basis of accounting. The statement also provides an indication about which assets can be used for general purposes and which are designated for a specific purpose and includes information to help compute the rate of return on investments, evaluate the capital structure of UW Medical Center, and assess the liquidity and financial flexibility of the organization.

The statement of revenues, expenses, and changes in net position reports all revenues, expenses, and other activity affecting net position during the time period indicated. Net position, the difference between assets and liabilities, is one way to measure the financial health of UW Medical Center and whether the organization has been able to recover all costs through net patient service revenue and other revenue sources.

The statement of cash flows reports the cash provided by UW Medical Center's operating activities, as well as other cash sources such as investment income, cash payments for capital additions and improvements, and payments for debt service, interest payments funding to affiliates. The statement provides meaningful information on where UW Medical Center's cash was generated and what it was used for.

**Financial Highlights for Fiscal Year 2015**

UW Medical Center reported operating income of $64.6 million in fiscal year 2015 and a increase in net position of $26.8 million for the year ended June 30, 2015 compared to operating income of $32.5 million and an increase in net position of $14.7 million for the year ended June 30, 2014. The increase in operating income is a result of strong case volumes in cardiology, oncology, neurosurgery, and transplants which results in higher acuity patients. Fiscal year 2015 included the full year of operations at the UW Medicine Sports Medicine Center at Husky Stadium, the UW Medical Center Eastside Specialty Center, and a state of the art hybrid operating room.

| | | 2015 | 2014 |
|---|---|---|---|
| | | (In thousands) | |
| Total operating revenues | $ | 1,083,584 | 967,651 |
| Total operating expenses | | 1,018,987 | 935,111 |
| Operating income | | 64,597 | 32,540 |
| Investment income, net | | 11,228 | 17,074 |
| Interest expense | | (10,983) | (11,218) |
| Other, net | | (38,097) | (24,300) |
| Nonoperating expenses | | (37,852) | (18,444) |
| Capital contributions and transfers | | 31 | 557 |
| Increase in net position | | 26,776 | 14,653 |
| Net position, beginning of year | | 682,537 | 667,884 |
| Cumulative effect of accounting change | | (227,267) | — |
| Net position, beginning of year, as adjusted | | 455,270 | 667,884 |
| Net position, end of year | $ | 482,046 | 682,537 |

UW Medical Center employees can participate in the Washington Public Employees Retirement System (PERS). The University, as a cost-sharing employer of the PERS plan, has a financial responsibility for pension benefits associated with its defined benefit plans. UW Medical Center's beginning net position for fiscal year 2015 has been restated for the proportionate share of the University's pension expense in accordance with Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions*. Pension expense is allocated to the UW Medical Center based on the proportionate share of employer contributions for the fiscal year.



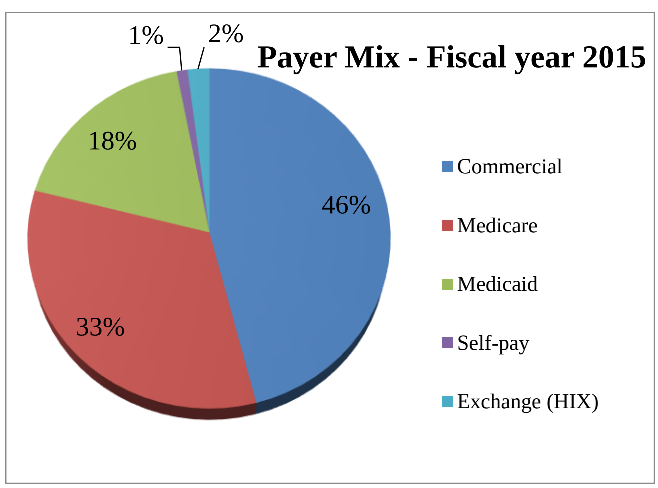
(Continued)

The following chart represents the key statistics of UW Medical Center:

| | 2015 | 2014 |
|---|---|---|
| Available beds | $ 432 | 422 |
| Admissions | 18,092 | 18,033 |
| Patient days | 126,239 | 124,513 |
| Average length of stay | 6.98 | 6.90 |
| Occupancy | 80.0% | 81.0% |
| Case mix index (CMI) | 2.126 | 2.021 |
| Surgery cases | 15,313 | 14,538 |
| Emergency room visits | 26,465 | 25,338 |
| Primary care clinic visits | 56,928 | 55,941 |
| Specialty care clinic visits | 245,110 | 235,434 |
| Full-time equivalents (FTEs) | 4,498 | 4,369 |
| Births | 2,043 | 1,997 |
| Solid Organ Transplants | 321 | 308 |
| NICU Admissions | 579 | 630 |

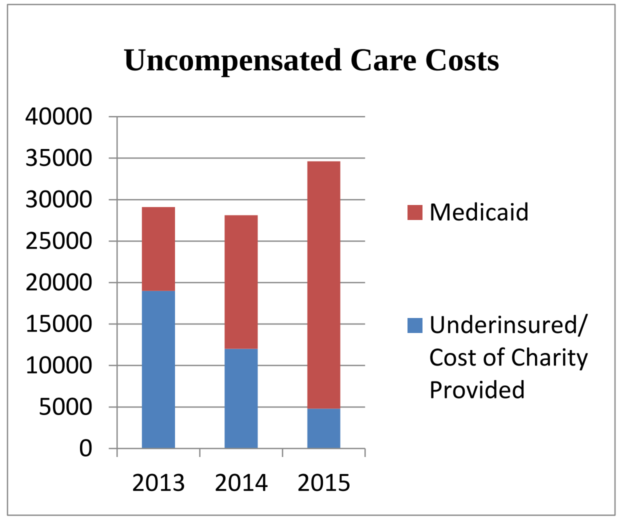
***Total Operating Revenues***

Total operating revenues consists primarily of net patient service revenues and other operating revenues. Net patient service revenues are recorded based on standard billing rates less contractual adjustments, charity, and a provision for uncollectible accounts. UW Medical Center has agreements with federal and state agencies, and commercial insurers that provide for payments at amounts different from gross charges. UW Medical Center provides care at no charge or reduced charges to patients who qualify under UW Medical Center's charity policy. UW Medical Center also estimates the amount of patient responsibility accounts receivable that will become uncollectible, which is reported as a reduction of net patient service revenue. The difference between gross charges and the estimated net realizable amounts from payers and patients is recorded as an adjustment to charges. The resulting net patient service revenue is shown in the statements of revenues, expenses, and changes in net position.




Net patient service revenues comprise of inpatient and outpatient revenue. Outpatient revenue consists of both hospital-based and clinic network revenue. Other operating revenue comprises hospital-related revenues such as parking and cafeteria sales.

UW Medical Center's payer mix is a key factor in the overall financial operating performance. The chart to the right illustrates payer mix for 2015. For the year ended June 30, 2015 and 2014, Medicaid revenue represented 18% and 17%, respectively, and self-pay revenue represented 1% and 1%, respectively. This increase in Medicaid revenue is a direct result of the Medicaid program expansion in Washington State as part of the Affordable Care Act.

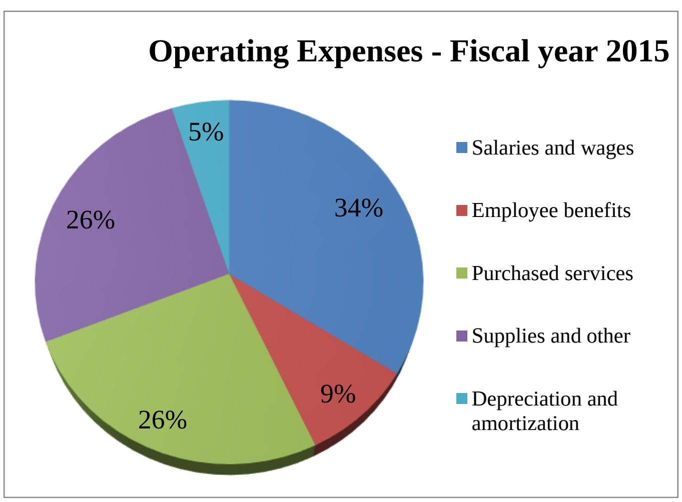



Due to Medicaid expansion, patients who were previously self-pay now qualify for Medicaid coverage, thus there was a decrease in the number of applicants for charity care and a decrease in the cost of charity care provided. However, UW Medical Center has seen a corresponding increase in uncompensated care costs related to providing care to Medicaid patients. The table to the right shows the shift in of uncompensated care costs from charity care to Medicaid.

Reimbursement from governmental payers is generally below commercial rates and reimbursement rules are complex and subject to both interpretation and settlements. With the expansion of Medicaid, UW Medical Center will have higher government revenues, which are subject to settlements.

For the years ended June 30, 2015 and 2014, UW Medical Center's total operating revenues were $1,083.6 million and $967.7 million comprised of $1,031.9 million and $924.4 million in net patient service revenues and $51.7 million and $43.3 million of state appropriations and other operating revenue, respectively. The increase in operating revenues between fiscal years 2015 and 2014 was driven by higher case acuity that increased net patient service revenue and contract pharmacy revenues, which positively impacted other operating revenue.

***Total Operating Expenses***




Total operating expenses were $1,019.0 million for the fiscal year 2015 compared to $935.1 million for the fiscal year 2014. The composition of fiscal year 2015 operating expenses is illustrated in the chart to the left.

**Salaries and wages** increased $22.5 million from $320.5 million in fiscal year 2014 to $343.0 million in fiscal year 2015. The increase in salaries and wages expenses in fiscal year 2015 was primarily driven by an increase in FTE employees and employee merit increase.

**Employee benefits** decreased $2.7 million from $100.0 million in fiscal year 2014 to $97.3 million in fiscal year 2015. Employee benefit expense decreased as a result of University benefit load rate and the adoption of GASB 68, in which UW Medical Center recorded the actuarially provided pension expense which is less than what was funded in fiscal year 2015.

**Purchased services** expense, which consists of professional and consulting fees, increased $22.7 million from $240.9 million in fiscal year 2014 to $263.6 million in fiscal year 2015. The increase in purchased services between fiscal year 2015 and 2014 is attributed to an increase in the allocation of IT expenses to UW Medical Center as a result of higher expenses at UW Medicine ITS and the School faculty funding expense.

**Supplies and other** expense includes medical and surgical supplies, pharmaceutical supplies, insurance, taxes, and other expenses. In total, these expenses increased $42.2 million from $221.3 million in fiscal year 2014 to $263.5 million in fiscal year 2015. The increase was driven by medical supplies expense as a result of higher costs in pharmaceutical, prosthesis, and surgical expenses.

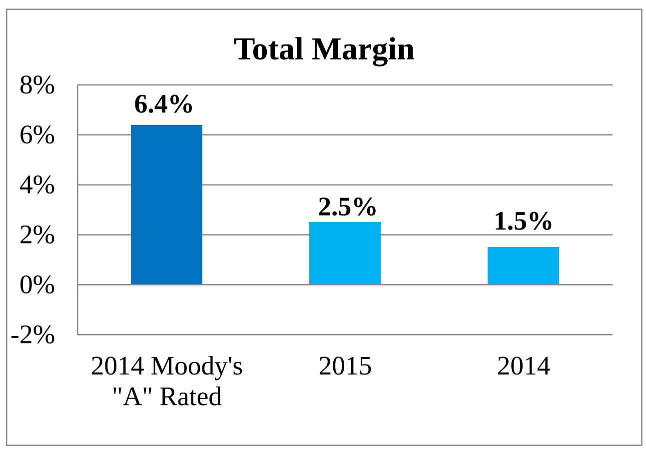
**Depreciation expense** decreased $0.8 million from $52.4 million in fiscal year 2014 to $51.6 million in fiscal year 2015.

***Nonoperating Revenues (Expenses)***

Nonoperating revenues (expenses) consist primarily of investment income, interest expense, intergovernmental transfer expense and strategic funding to UW Medicine entities. Net nonoperating expenses increased $19.4 million between fiscal years 2015 and 2014. The increase in net nonoperating expense is attributable to a decrease in Seattle Cancer Care Alliance (SCCA) investment income, intergovernmental transfers related to UW Medical Center's participation in Washington State Provider Access Payment (PAP) program, and increase in strategic funding to affiliates.

***Total Margin***

Total margin or excess margin is a ratio that defines the percentage of total revenue that has been realized in the form of net income and is a common measure of total hospital profitability. Total margin for the fiscal years 2015 and 2014 compared to industry median is illustrated in the chart to the right.



## Financial Analysis

### *Statements of Net Position*

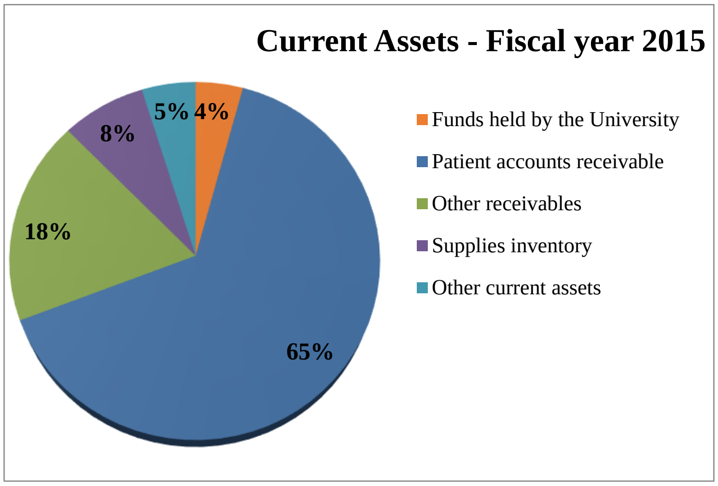
The table below is a presentation of certain condensed financial information derived from UW Medical Center's statements of net position as of the fiscal years ended June 30, 2015 and 2014:

| | | 2015 | 2014 |
|---|---|---|---|
| | | (In thousands) | |
| Current assets | $ | 242,156 | 197,839 |
| Noncurrent assets: | | | |
| Capital assets, net | | 530,659 | 488,314 |
| Funds held by the University | | 250,249 | 243,745 |
| Investment in SCCA | | 107,704 | 101,376 |
| Other noncurrent assets | | 18,764 | 15,627 |
| Total assets | | 1,149,532 | 1,046,901 |
| Deferred outflow of resources | | 25,809 | — |
| Total assets and deferred outflow of resources | | 1,175,341 | 1,046,901 |
| Current liabilities | | 171,936 | 144,036 |
| Noncurrent liabilities | | 271,785 | 220,328 |
| Net pension liability | | 173,633 | — |
| Total liabilities | | 617,354 | 364,364 |
| Deferred inflow of resources | | 75,941 | — |
| Net position | $ | 482,046 | 682,537 |

Total assets and deferred outflow of resources are $1,175.3 million at June 30, 2015 compared to $1,046.9 million at June 30, 2014, an increase of $128.4 million. Significant events within total assets during fiscal year 2015 include an increase in current assets driven by patient accounts receivable and other receivables, increase in capital assets as result of the Montlake Tower construction, and the recording of a deferred inflow of resources due to the adoption of an accounting standard.

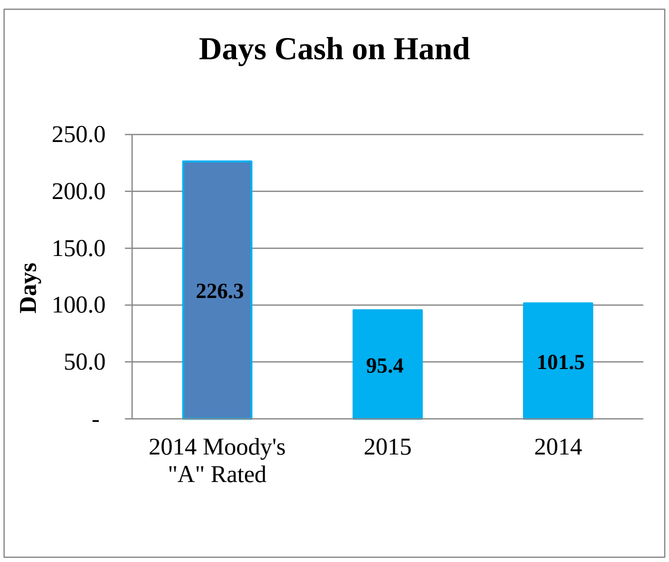
***Current Assets***

Current assets consist of cash and cash equivalents, and other current assets that are expected to be converted to cash within a year. Current assets also include net patient accounts receivable valued at the estimated net realizable amount due from patients and insurers.




Total current assets were $242.2 million at fiscal year-end 2015, compared to $197.8 million at year-end 2014. Fiscal year 2015 composition of current assets is illustrated in the chart to the left.

**Funds held by the University of Washington** (the University) represent cash and short-term investments held by the University on behalf of UW Medical Center. The funds have no principal risk and are available on demand to UW Medical Center. The current portion of funds held by the University generally represents the current annual debt service requirements. All other funds held by the University are shown as noncurrent assets as it is not expected that the funds will be utilized within the next year. The current portion of funds held by the University decreased $0.8 million in 2015 from $11.0 million at June 30, 2014 to $10.2 million at June 30, 2015.

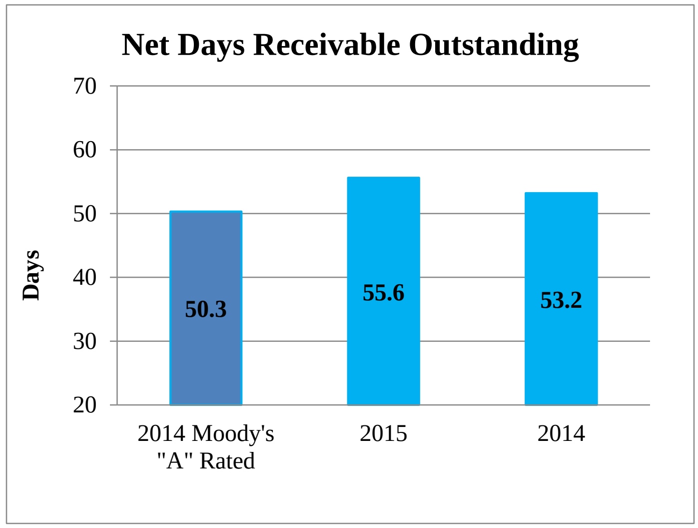



Days cash on hand is utilized to evaluate an organization's continuing ability to meet its short-term operating needs. Days cash on hand (including noncurrent funds held by the University as of June 30 for fiscal year 2015 and 2014 are illustrated in the chart to the left.

UW Medical Center's total days cash on hand, including investments held by the University, decreased 6.1 days from 101.5 days at June 30, 2014 to 95.4 days at June 30, 2015. The decrease in 2015 was driven as a result of higher operating expenses.

**Net patient accounts receivable** was $157.3 million as of June 30, 2015, compared to $134.8 million at June 30, 2014. The increase of $22.5 million is driven by a growth in revenue and volumes.

Net days receivable outstanding illustrates an organization's ability to convert net patient service revenue to cash. Net days receivable outstanding as of June 30 for fiscal years 2015 and 2014 are illustrated in the chart to the right.




UW Medical Center total net days receivable outstanding increased 2.4 days from 53.2 days at June 30, 2014 to 55.6 days at June 30, 2015. The increase during fiscal year 2015 was driven by growth in revenue and higher initial denial rates from payers.

As of June 30, 2015 and 2014, 43% and 45% of the gross patient accounts receivable balance is due from commercial payers, 50% and 48% is due from governmental payers Medicare and Medicaid, and 5% and 6% from self-pay patients and patient responsibility after insurance. On January 1, 2014, the Washington state Medicaid program was expanded to significantly increase the number of eligible Medicaid enrollees receiving benefits. Due to this expansion, UW Medical Center has seen an increase in Medicaid and Medicaid managed care gross patient accounts receivable at June 30, 2015, when compared to the previous fiscal year.

**Other receivables** consist of amounts due from external and related parties for nonpatient services. Other receivables increased $16.7 million from $28.1 million at June 30, 2014 to $44.8 million at June 30, 2015. Other receivables increased in fiscal year 2015 as a result of timing of payments between UW Medical Center and SCCA and timing of settlements with the School.

**Other current assets** include prepaid expenses. The increase in other current assets in fiscal year 2015 of $3.3 million relates to UW Medical Center's current portion of IT prepaid expenses.

***Noncurrent Assets***

**Capital assets, at cost, net of accumulated depreciation** increased $42.4 million during fiscal year 2015 from $488.3 million at June 30, 2014 to $530.7 million at June 30, 2015. The increase in fiscal year 2015 was due to continued construction on the Montlake Tower that has not been placed into service yet.

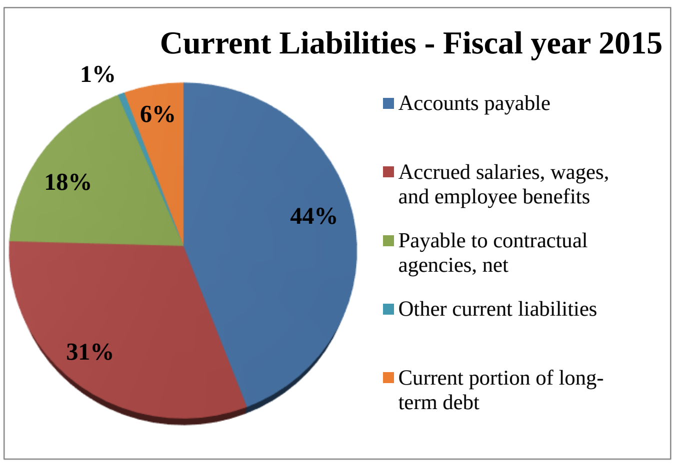
Additional discussion regarding capital asset activity during the fiscal years can be found in the notes to the financial statements.

**Funds held by the University** represents funds invested with the University Invested Funds program (the program) and represent cash in excess of amounts required for operations. Through the program, UW Medical Center receives a rate of return representative of fund performance. For the fiscal years 2015 and 2014, the program generated a rate of return of 2% on UW Medical Center assets. Noncurrent funds held by the University increased by $6.5 million in fiscal year 2015 as a result of cash generated from operations.

**Investment in Seattle Cancer Care Alliance (SCCA)** represents UW Medical Center's interest in SCCA, in which UW Medical Center is a 33.3% owner. UW Medical Center accounts for its interest in the SCCA using the equity method of accounting. Investment in SCCA increased by approximately $6.3 million during fiscal year 2015 from $101.4 million at June 30, 2014 to $107.7 million at June 30, 2015. Changes in the investment value reflect UW Medical Center's proportionate interest in the change in net assets of SCCA. The increase in 2015 was attributable to positive results in operations partially offset by a loss on refinancing of long-term debt.

**Other assets** consist of long-term prepaid expenses. Beginning in July 2013, UW Medicine ITS (a department of the University) began recording enterprise-wide information technology (IT) capital assets that are purchased for use by UW Medicine entities. Previously, these IT capital assets were recorded by UW Medical Center. The long-term prepaid expense reflected in other assets of $14.0 million at June 30, 2015 entitles UW Medical Center access to the enterprise wide IT software and services.

***Current Liabilities***




Current liabilities consist of accounts payable and other accrued liabilities that are expected to be paid within a year. Total current liabilities were $171.9 million at June 30, 2015, compared to $144.0 million at June 30, 2014. Fiscal year 2015 composition of current liabilities is illustrated in the chart below.

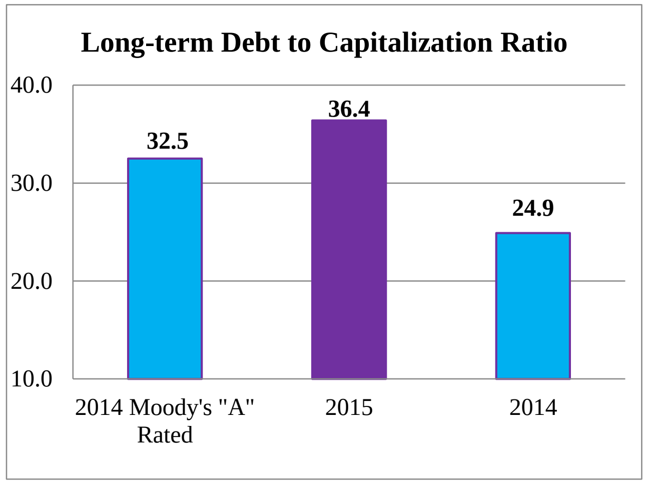
**Accounts payable** increased $13.4 million from $63.0 million at June 30, 2014 to $76.4 million at June 30, 2015. Changes in accounts payable and accrued liabilities are primarily driven by timing of payments to vendors and employees.

**Accrued salaries**, wages, and employee benefits increased $2.9 million from $51.1 million at June 30, 2014 to $54.0 million at June 30, 2015. Changes in accrued salaries, wages, and employee benefits are primarily driven by the number of employees and employee merit increases.

**Payable to contractual agencies, net** consists of estimated reserves for cost report settlements and amounts due as intergovernmental transfers to the Washington State (the State) Healthcare Authority. Payable to contractual agencies increased $12.4 million from $19.1 million at June 30, 2014 to $31.5 million at June 30, 2015. The increase in fiscal year 2015 was driven by development in open Medicare cost reports and Medicaid certified public expenditures (CPE) hold harmless estimates.

***Noncurrent Liabilities***

Noncurrent liabilities consist primarily of Internal Lending Program (ILP) debts and capital leases issued to finance construction and equipment. The ILP debt net of principal payments increased $55.5 million between fiscal years ended June 30, 2014 and 2015. The increase in 2015 is a result of financing needs related to the Montlake Tower expansion.




Long-term debt to capitalization is a ratio used to evaluate capital structure of healthcare organizations. The chart to the right shows the long-term debt to capitalization ratio as of June 30 for 2015 and 2014 in comparison to the freestanding hospital median.

UW Medical Center long-term debt to capitalization increased in 2015 due to the increase in long-term debt and a decrease in net position as UW Medical Center recorded its proportionate share of the University's pension liability. Including UW Medical Center's net pension liability as part of the debt to capitalization ratio would result in a ratio of 48.3% for fiscal year 2015.

Additional discussion regarding long-term debt activity during the fiscal years can be found in the notes to the financial statements.

**Net Pension Liability**

The University has a financial responsibility for pension benefits associated with the PERS defined-benefit plans, which includes University employees deployed at UW Medical Center. UW Medical Center's beginning net position for fiscal year 2015 has been restated for the proportionate share of the University's pension liability. Beginning net position decreased by $227.3 million as a result of recording this standard. The net pension liability allocated to UW Medical Center is based on their proportionate share of employer contributions for the fiscal year. At June 30, 2015, net pension liability of $173.6 million was recorded on the statement of net position for UW Medical Center. In addition, deferred outflow of resources of $25.8 million and deferred inflow of resources of $75.9 million was recorded at June 30, 2015. Additional discussion regarding the adoption and recording of GASB 68 can be found in the notes to the financial statements.

**Factors Affecting the Future**

**UW Medicine Strategic Planning**

***Strategic Collaborations***

In 2015, UW Medicine, Skagit Regional Health, and Cascade Valley Hospital and Clinics entered into a Clinical Affiliation Agreement intended to create a long-term and durable affiliation to integrate clinical programs to achieve the "Triple Aim" of better care for individuals, better health for populations, and lower per capita costs.

In March 2014, UW Medicine and Capital Medical Center (Olympia, WA) signed an agreement selecting UW Medicine as the healthcare system of choice for complex tertiary and quaternary care for Capital Medical Center patients. This strategic collaboration, effective April 1, will provide Capital Medical Center patients prompt access to the highest level of care for advanced services while allowing the organizations to work together to continue improving the quality, safety, and cost-effectiveness of care in the South Sound.

***UW Medicine Accountable Care Network***

In 2014, UW Medicine formed an Accountable Care Network (ACN) with certain other healthcare organizations and healthcare professionals in Western Washington to form a care delivery network to assume responsibility for the healthcare of contracted populations of patients to achieve the Triple Aim: improved healthcare experience for the individual, improved health of the population, and more affordable care.

- The ACN has contracted with the Washington Healthcare Authority (HCA) to participate in its new Puget Sound Accountable Care Program (ACP) for Public Employees Benefits Board (PEBB) members. The Puget Sound Accountable Care Program will initially be offered to all PEBB members who reside in Snohomish, King, Kitsap, Pierce and Thurston Counties, with possible statewide expansion in 2017. This new option will be available to PEBB members with coverage beginning January 1, 2016.
- A subset of the network members have also agreed to participate with the ACN in a contract with Premera as part of its new Accountable Health System (AHS) product. As an AHS, the UW Medicine ACN will share in accountability for the quality and cost of healthcare for Premera members who select this plan. This product will be sold both on and off the Washington Health Exchange in select counties with coverage beginning on January 1, 2016.
- UW Medicine ACN entered into agreements to provide healthcare services to non-Union employees of a large local employer with coverage that began January 1, 2015.

These arrangements provide an opportunity for shared savings between the ACN and the contracted entity based on achieving quality and financial benchmarks. If certain financial benchmarks are not attained, UW Medicine, along with its network members, are at risk for reductions in payment levels from the contracted entity based on the agreement.

***Employee Costs***

Rising benefit costs, particularly for pensions and healthcare, continue to impact the University and UW Medical Center. Employer pension funding rates for the Public Employees' Retirement System (PERS) pension plans were unchanged during fiscal year 2015, but will be increasing 19% to 11% of covered salary during fiscal year 2016. Likewise, although the monthly employer base rate paid by the University and UW Medical Center for employee healthcare expenses decreased during fiscal year 2015, it will increase 27% to $840 per active employee during fiscal year 2016. Both rates are likely to continue increasing over the next few years.

***Regulatory, Legislative and Accounting Changes***

The following regulatory, legislative, and accounting activity will impact all entities in UW Medicine during fiscal year 2015 and beyond:

- ***International Classification of Diseases (ICD) v10*** – Code of Federal Regulations (45 CFR Part 162) requires healthcare providers to implement ICD-10 no later than October 1, 2015. ICD-10 represents a significant change in the standard healthcare coding system and will impact every system, process, and transaction that contains or uses a diagnosis code or inpatient procedure code. The implementation of ICD-10 will impact both healthcare providers and healthcare payers.

  UW Medicine has been undertaking activities related to the implementation of ICD-10 since the beginning of fiscal year 2012.

- ***Medicaid Expansion*** – On January 1, 2014, the Washington State Medicaid program was expanded to significantly increase the number of Medicaid enrollees receiving benefits. Due to the increased access to Medicaid coverage, UW Medical Center is experiencing a reduction in uninsured and underinsured patients and an increase in patients that qualify for Medicaid. The reduction of uninsured and underinsured patients is expected to have an impact on Medicare and Medicaid Disproportionate Share (DSH) reimbursement methodologies in the future. UW Medical Center has experienced a change to their payer mix, which is anticipated to continue in 2016.

- ***Pay for Performance*** – The Affordable Care Act mandated programs that affect reimbursement through evaluation of the quality of care and cost of care provided to patients at the federal level, however, there are an increasing number of programs arising from state and private interests. These programs provide incentives (and/or penalties) for both reporting performance data and on benchmarking performance data against other providers regionally and nationally. The pay for performance programs will continue into the future and UW Medicine is examining performance to attain incentive dollars.

- ***Montlake Tower Expansion Project*** – In February 2008, the University of Washington Board of Regents granted approval to proceed with phase one of a multiphase inpatient expansion known as the Montlake Tower. The scope of phase one included the vertical shell for the entire eight-floor expansion, as well as, a new neonatal intensive care unit, an adult oncology and blood and bone marrow transplant unit, additional diagnostic imaging capacity, and future operating room capacity. In July 2012, phase one was substantially completed and operational components of phase one began servicing patients in October 2012. Total cost of phase one was $210.4 million, which was primarily funded through borrowings from the University of Washington Internal Lending Program.

  In November 2012, the University of Washington Board of Regents granted approval to proceed with phase two of the Montlake Tower project. The scope of phase two will complete three shelled inpatient floors including the addition of intensive care and medical/surgical beds as well as additional operating rooms. Estimated cost of phase two is currently projected at $186.3 million. As part of the approval, the Board of Regents authorized funding from the University of Washington Internal Lending Program up to $136.1 million, with the remaining $50.2 million of anticipated cost to be funded through hospital operations and/or cash reserves. Construction on phase two began in 2015 and is expected to be completed by October 2017.

In fiscal year 2015, project costs associated with phase two of the Montlake Tower project were $72.1 million. Several components of the Montlake Tower expansion project will become operational in fiscal year 2016, including the opening of seven new operating rooms, including two hybrid rooms. Additionally, the number of ICU beds will increase from 53 to 79 beds, and an additional acute care unit of 31 beds will open. The following phase of the project includes build out of the patient prep, hold and recovery areas, and adding 4 additional operating rooms.

**UNIVERSITY OF WASHINGTON MEDICAL CENTER**
(A Division of the University of Washington)

Statement of Net Position

June 30, 2015

(In thousands)

| | | |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Funds held by the University of Washington | $ | 10,201 |
| Patient accounts receivable, less allowance for uncollectible accounts of $10,096 | | 157,296 |
| Other receivables | | 44,776 |
| Supplies inventory | | 18,241 |
| Other current assets | | 11,642 |
| Total current assets | | 242,156 |
| Noncurrent assets: | | |
| Capital assets, at cost, net of accumulated depreciation | | 530,659 |
| Funds held by the University of Washington | | 248,151 |
| Assets whose use is limited | | 2,098 |
| Investment in Seattle Cancer Care Alliance | | 107,704 |
| Other assets | | 18,764 |
| Total noncurrent assets | | 907,376 |
| Total assets | | 1,149,532 |
| Deferred outflow of resources: | | |
| Employer contributions to pensions plans subsequent to measurement date | | 25,809 |
| Total assets and deferred outflow of resources | $ | 1,175,341 |
| **Liabilities** | | |
| Current liabilities: | | |
| Accounts payable | $ | 76,376 |
| Accrued salaries, wages, and employee benefits | | 53,968 |
| Payable to contractual agencies, net | | 31,506 |
| Current portion of long-term debt | | 8,972 |
| Other current liabilities | | 1,114 |
| Total current liabilities | | 171,936 |
| Noncurrent liabilities: | | |
| Long-term debt, net of current portion | | 265,768 |
| Net pension liability | | 173,633 |
| Unearned revenue | | 6,017 |
| Total liabilities | | 617,354 |
| Deferred inflow of resources: | | |
| Difference between projected and actual earnings on pension plan investments, net | | 75,941 |
| Net position: | | |
| Net investment in capital assets | | 255,919 |
| Expendable, restricted | | 2,098 |
| Unrestricted | | 224,029 |
| Total net position | | 482,046 |
| Total liabilities, deferred inflow of resources, and net position | $ | 1,175,341 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON MEDICAL CENTER**
(A Division of the University of Washington)

Statement of Revenues, Expenses, and Changes in Net Position

Year ended June 30, 2015

(In thousands)

| | |
|---|---|
| Operating revenues: | |
| Net patient service revenues (net of provision for uncollectible accounts of $7,976) | $ 1,031,926 |
| State appropriation | 6,501 |
| Other revenue | 45,157 |
| Total operating revenues | 1,083,584 |
| Operating expenses: | |
| Salaries and wages | 342,954 |
| Employee benefits | 97,347 |
| Purchased services | 263,611 |
| Supplies and other | 263,472 |
| Depreciation | 51,603 |
| Total operating expenses | 1,018,987 |
| Income from operations | 64,597 |
| Nonoperating revenues (expenses): | |
| Investment income | 11,228 |
| Interest expense | (10,983) |
| Funding to affiliates | (38,307) |
| Other, net | 210 |
| Nonoperating expenses | (37,852) |
| Income before capital contributions and transfers | 26,745 |
| Gifts, grants, and other capital contributions and transfers | 31 |
| Total increase in net position | 26,776 |
| Net position - As issued | 682,537 |
| Cumulative effect of change in accounting principle | (227,267) |
| Net position – beginning of year, as adjusted | 455,270 |
| Net position – end of year | $ 482,046 |

See accompanying notes to financial statements.

**UNIVERSITY OF WASHINGTON MEDICAL CENTER**
(A Division of the University of Washington)

Statement of Cash Flows

Year ended June 30, 2015

(In thousands)

| | |
|---|---|
| Cash flows from operating activities: | |
| Cash received for patient care | $ 1,021,851 |
| Cash received for other services | 36,301 |
| Cash paid to employees | (440,930) |
| Cash paid to suppliers and others | (529,162) |
| Net cash provided by operating activities | 88,060 |
| Cash flows from noncapital financing activities: | |
| Funding to affiliates | (34,648) |
| Other, net | (18) |
| Net cash used in noncapital financing activities | (34,666) |
| Cash flows from capital and related financing activities: | |
| Proceeds from borrowings | 58,569 |
| Purchases of capital assets | (91,168) |
| Principal payments on long-term debt | (9,886) |
| Interest payments on long-term debt, net of amounts capitalized | (10,297) |
| Net cash used in capital and related financing activities | (52,782) |
| Cash flows from investing activities: | |
| Change in funds held by the University and assets whose use is limited | (6,504) |
| Investment income | 4,968 |
| Distributions from joint ventures | 146 |
| Net cash used in investing activities | (1,390) |
| Decrease in cash and cash equivalents | (778) |
| Cash and cash equivalents, beginning of year | 10,979 |
| Cash and cash equivalents, end of year | $ 10,201 |
| Reconciliation of income from operations to net cash provided by operating activities: | |
| Income from operations | $ 64,597 |
| Adjustments to reconcile income from operations to net cash provided by operating activities: | |
| Depreciation | 51,603 |
| Provision for uncollectible accounts | 7,976 |
| Loss on disposal of capital assets | 67 |
| Pension plans contribution adjustment | (3,501) |
| Net increase in current assets | (56,195) |
| Net increase in current liabilities, except current portion of long-term debt | 22,149 |
| Increase in unearned revenue | 1,364 |
| Net cash provided by operating activities | $ 88,060 |
| Supplemental disclosure of noncash investing, capital, and financing activities: | |
| Change in capital assets included in accounts payable | $ 2,816 |
| Capital contributions | 31 |

See accompanying notes to financial statements.

## (1) Organization

University of Washington Medical Center (UW Medical Center) is a 450 licensed-bed hospital and is a division of the University of Washington (a not-for-profit, tax-exempt agency of the State of Washington) (the University). Authority for specified governance functions of UW Medical Center has been delegated by the Board of Regents (the Regents) to the UW Medicine Board (the Board) as specified in the Board's bylaws, originally adopted by the Regents in 1976 and amended in February 2000. The Board's members during fiscal year 2015 were:

| | |
|---|---|
| Michael D. Garvey, Chairman | Rich Jones, Vice Chairman |
| James K. Anderson | Kristianne Blake |
| Ana Mari Cauce | Alan Frazier |
| Gerald Grinstein | Gary Kohlwes |
| Kimberly McNally | Julie A. Nordstrom |
| Dennis I. Okamoto | Arthur F. "Skip" Oppenheimer |
| Carolyn V. Parnell | Paul G. Ramsey, M.D. |
| William J. Rex | Rogelio Riojas |
| Robert Stacey | Peter van Oppen |

UW Medical Center is under the direction of the Executive Director, who is accountable to the Board and UW Medicine's Chief Health System Officer for the management of UW Medical Center.

UW Medical Center is part of UW Medicine which includes Harborview Medical Center (Harborview), Northwest Hospital & Medical Center (Northwest Hospital), Valley Medical Center (VMC), UW Physicians Network dba UW Neighborhood Clinics (UWNC), UW Physicians (UWP), the UW School of Medicine (the School), and Airlift Northwest (Airlift). In addition, UW Medical Center is an equity shareholder in Seattle Cancer Care Alliance (SCCA), a joint venture partnership with Fred Hutchinson Cancer Research Center (FHCRC) and Seattle Children's Hospital.

## (2) Summary of Significant Accounting Principles

### *(a) Accounting Standards*

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in the United States of America using the accrual basis of accounting. UW Medical Center's financial statements and note disclosures are based on all applicable Government Accounting Standards Board (GASB) pronouncements and interpretations. UW Medical Center uses proprietary fund accounting.

### *(b) Basis of Accounting*

UW Medical Center's financial statements have been prepared using the accrual basis of accounting with the economic resources measurement focus. Under this method of accounting, revenues are recognized when earned and expenses are recorded when liabilities are incurred without regard to receipt or disbursement of cash.

***(c) Use of Estimates***

The preparation of financial statements, in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates in UW Medical Center’s financial statements include patient accounts receivable allowances and third-party payer settlements.

***(d) Funds Held by the University of Washington***

UW Medical Center operating and capital funds are invested directly with the University. All balances are available on demand and are stated at fair value. In exchange, the University offers a stipulated rate of return determined at the end of the reporting period by the University based on pooled investment performance and the University’s reserve fund goals. For fiscal year 2015, the rate used was 2%.

Amounts classified as current assets are considered cash and cash equivalents for presentation in the statement of cash flows and represent the current portion of the debt service requirements.

***(e) Inventories***

Inventories consist primarily of surgical, medical, and pharmaceutical supplies in organized stores at various locations across UW Medical Center. Inventories are recorded at the lower of cost (first-in, first-out (FIFO)) or market.

***(f) Capital Assets***

Capital assets, defined as purchases with a per item cost of $2,000 or greater and a useful life of at least two years, are stated at cost at acquisition or if acquired by gift, at fair value at the date of the gift. Additions, replacements, major repairs, and renovations are capitalized. Maintenance and repairs are expensed. The cost of the capital assets sold or retired and the related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recorded in supplies and other expense in the statement of revenues, expenses, and changes in net position.

The provision for depreciation is determined by the straight-line method, which allocates the cost of tangible property ratably over its estimated useful life. The estimated useful lives used by UW Medical Center are as follows:

| | |
|---|---|
| Land improvements | 10 to 25 years |
| Buildings, renovations, and furnishings | 10 to 40 years |
| Fixed equipment | 15 to 20 years |
| Movable equipment | 3 to 20 years |

Equipment under capital lease is amortized on the straight-line method over the shorter of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the statement of revenues, expenses, and changes in net position.

Interest is capitalized on construction projects as a cost of the related project beginning with commencement of construction and ceases when the construction period ends and the related asset is placed in service. Interest capitalized during 2015 was $2.4 million.

### *(g) Other Assets*

Beginning in July 2013, UW Medicine ITS (a department of the University) began recording enterprise-wide information technology (IT) capital assets that are purchased for use by UW Medicine entities. Previously, these capital assets were recorded at UW Medical Center and Harborview. UW Medical Center provides advance funding to UW Medicine ITS which entitles UW Medical Center access to the enterprise-wide IT software and services. The prepaid portion of this funding is reported within other current assets and other assets on the statement of net position. At June 30, 2015, $8.6 million is recorded in other current assets and $14.0 million is recorded in other assets.

### *(h) Compensated Absences*

UW Medical Center employees earn annual leave at rates based on length of service and sick leave at the rate of one day per month. Annual leave balances, can be converted to monetary compensation upon employment termination. Sick leave balances, which are unlimited, can be converted to monetary compensation annually at 25% of the employees' normal compensation rate for any balance that exceeds 480 hours or for any balance upon retirement or death. UW Medical Center recognizes annual and sick leave liabilities when earned.

Annual leave accrued at June 30, 2015 is $24.2 million. Sick leave accrued as of June 30, 2015 is $8.5 million. Compensated absences are reported within the accrued salaries, wages, and employee benefits on the statement of net position.

### *(i) Payable to Contractual Agencies, Net*

UW Medical Center is reimbursed for Medicare inpatient, outpatient, psychiatric, and rehabilitation services, and for capital and medical education costs during the year either prospectively or at an interim rate. The difference between interim payments and the reimbursement computed based on the Medicare filed cost report results in an estimated receivable from or payable to Medicare at the end of each year. The Medicare program's administrative procedures preclude final determination of amounts receivable from or payable to UW Medical Center until after the cost reports have been audited or otherwise reviewed and settled by Medicare.

Public hospitals located in the state of Washington designated by the Washington State legislature are reimbursed at the "full cost" of Medicaid inpatient covered services under the public hospital certified public expenditure payment method. See note 3(a) for discussion regarding this program.

The estimated settlement amounts for Medicare cost report and Certified Public Expenditures (CPE) payments that are not considered final are included in payable to contractual agencies, net in the accompanying statements of net position.

### *(j) Classification of Revenues and Expenses*

UW Medical Center's statement of revenues, expenses, and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues, such as patient service revenue, result from exchange transactions associated with providing healthcare services—UW Medical Center's primary business. Exchange transactions are those in which each party to the transaction receives and gives up essentially equal values of goods or services.

Operating expenses include all expenses, other than financing costs, incurred by UW Medical Center to provide healthcare services to UW Medical Center patients.

Nonoperating revenues and expenses are recorded for certain exchange and nonexchange transactions. This activities includes investment returns, interest expense, intergovernmental transfer expense, strategic funding to affiliates of UW Medicine, and investment income generated through SCCA joint venture.

### *(k) Net Patient Service Revenues*

UW Medical Center has agreements with third-party payers that provide for payments to UW Medical Center at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers.

Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. A summary of the payment arrangements with major third-party payers is as follows:

**Medicare**

Acute inpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge based on Medicare severity diagnosis-related groupings (MS-DRGs), as well as reimbursements related to capital costs. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Payments for Medicare outpatient services are provided based upon a prospective payment system known as ambulatory payment classifications (APC's). APC payments are prospectively established and may be greater than or less than the primary government's actual charges for its services. The Medicare program utilizes the prospective payment system known as case mix group (CMGs) for rehabilitation services reimbursement. As with MS-DRGs, CMG payments are prospectively established and may be greater than or less than UW Medical Center's actual charges for its services. Geropsychiatric services are also paid prospectively using a federal per diem payment rate adjusted for comorbidity and various adjustment factors. Third-party settlements are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

**Medicaid**

Inpatient services rendered to Medicaid program beneficiaries are paid at approximate cost or hold harmless estimates and settled at prospectively determined rates per discharge. Outpatient services rendered are provided based upon the APC prospective payment system.

**Commercial**

UW Medical Center also has entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to UW Medical Center under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

**Exchange (HIX)**

Washington State health exchange (HIX) entered into agreements with certain commercial insurance plans to provide patients access to healthcare services. The basis for payment to UW Medical Center under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

***(l) Accountable Care Network***

In 2014, UW Medicine entered into a risk contract with a large local employer and also formed an accountable care network (ACN) with certain other health care organizations and healthcare professionals to share financial and clinical responsibility for the healthcare of particular populations of patients. UW Medical Center is a network member of UW Medicine ACN and as such shares in the risk contract surplus or deficits based on agreed upon contractual terms. Since its inception, the ACN has entered into various contracts which include provisions for shared risk as well as shared savings based on achieving certain quality and financial benchmarks. UW Medical Center and the other network members share in the financial risk or savings. At June 30, 2015, UWMC has recorded a liability of $515,000 for its portion of the estimated liability related to these risk-sharing arrangements which is reflected in accounts payable in the accompanying statement of net position.

***(m) Charity Care***

UW Medical Center provides care without charge or at amounts less than established rates to patients who meet certain criteria under its charity care policy. Records are maintained to identify and monitor the level of charity care provided. These records include charges foregone for services and supplies furnished under its charity care policy to the uninsured and the underinsured. Because UW Medical Center does not pursue collection of amounts determined to qualify as charity care, these are not reported as net patient service revenue. The charges associated with charity care and uncompensated care provided by UW Medical Center were approximately $18.0 million for the year ended June 30, 2015.

UW Medical Center estimates the cost of charity care using its cost to charge ratio of 43.5% for the fiscal year ended June 30, 2015. Applying UW Medical Center's cost to charge ratio of 43.5% to total charity and uncompensated care of $18.0 million results in an estimated cost of charity care of $7.9 million for the fiscal year ended June 30, 2015.

***(n) Federal Income Taxes***

UW Medical Center, as a division of University, is not subject to federal income tax under Section 115 of the Internal Revenue Code, unless unrelated business income tax is generated during the year.

***(o) New Accounting Pronouncements***

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions*, which is effective for the fiscal year beginning July 1, 2014. It requires governments providing defined benefit pensions to their employees to recognize the net pension liability for pension benefits on their statement of net position. Net position liability is measured as total pension liability, less the amount of the plan's fiduciary net position. Since the University participates in the Washington State Public Employee Retirement Plans (PERS), this statement required the University to record their proportionate share of the net pension liability at June 30, 2015. UW Medical Center recorded their proportionate share of net pension liability in its 2015 financial statements, which had a material impact to its financial statements. In addition to the reporting changes described above, implementation of this Statement resulted in the restatement of fiscal year 2015 beginning unrestricted net position, reducing it by $227.3 million. See note 9 for further discussion on the adoption of this standard.

In February 2015, the GASB issued Statement No. 72 *Fair Value Measurement and Application*, which will be effective for the fiscal year ending June 30, 2016. This statement provides guidance for determining the fair value measurement for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. This statement establishes a three level hierarchy of inputs to valuation techniques used to measure fair value and requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. UW Medical Center is currently analyzing the impact of this statement.

In June 2015, the GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and No. 68*. Amendments to GASB Statement No. 68 will be effective for the fiscal year ending June 30, 2016 and the guidance for plans not within 68's scope will be effective for the fiscal year ending June 30, 2017. This statement is intended to improve financial reporting of governments whose employees are provided with pensions that are not within the scope of Statement No. 68, improve the usefulness of information associated with governments that hold assets accumulated for purposes of providing defined benefit pensions not within the scope of Statement No. 68, and to clarify the application of certain provisions of statements No. 67 and 68. UW Medical Center is currently analyzing the impact of this statement.

In June 2015, the GASB issued Statement No. 74 *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans*, which is effective for the fiscal year ending June 30, 2017. The objective of this Statement is to improve the usefulness of information about other postemployment benefits (OPEB) such as death benefits, life insurance, disability, and long-term care in financial reports of governments that provide them. This statement replaces Statement No. 43, *Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans*, as amended. UW Medical Center is currently analyzing the applicability of this statement.

In June 2015, the GASB issued Statement No. 75 *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which is effective for the fiscal year ending June 30, 2018. This statement establishes standards of accounting and financial reporting for defined benefit OPEB and defined contribution OPEB that are provided to the employees of state and local governmental employers through OPEB plans that are administered through trusts or equivalent arrangements. This statement also establishes standards of accounting and financial reporting for OPEB plans that are not administered through trusts or equivalent arrangements. UW Medical Center is currently analyzing the impact of this statement.

In June 2015, the GASB issued Statement No. 76, T*he Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which is effective for the fiscal year ending June 30, 2016. The objective of this statement is to identify the hierarchy of generally accepted accounting principles (GAAP). This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. UW Medical Center is currently analyzing the impact of this statement.

## (3) Net Patient Service Revenues

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. In 2015, net patient service revenue includes approximately $8.7 million relating to prior years' net Medicare and Medicaid cost report settlements and revised estimates, including disproportionate share reimbursement and the CPE program.

The following are the components of net patient service revenues for the year ended June 30, 2015 (in thousands):

| | | |
|---|---|---|
| Patient service revenues | $ | 2,194,855 |
| Less adjustments to patient service revenues: | | |
| Contractual discounts | | 1,136,907 |
| Charity care | | 18,046 |
| Provision for uncollectible accounts | | 7,976 |
| Total adjustments to patient service revenues | | 1,162,929 |
| Net patient service revenues | $ | 1,031,926 |

UW Medical Center grants credit without collateral to its patients, most of whom are insured under third-party payer agreements. The mix of gross patient charges and gross receivables from significant third-party payers at June 30, 2015 was as follows:

| | Patient service charges | Accounts receivable |
|---|---|---|
| Medicare | 33% | 31% |
| Medicaid | 18 | 19 |
| Commercial and other | 46 | 43 |
| Exchange (HIX) | 2 | 2 |
| Self-pay | 1 | 5 |
| Total | 100% | 100% |

### *(a) Medicaid Certified Public Expenditure (CPE) Reimbursement*

Public hospitals located in the state of Washington designated by the Washington State legislature are reimbursed at the “full cost” of Medicaid inpatient covered services under the public hospital CPE payment method.

“Full cost” payments are determined using the respective hospital’s Medicaid ratio of cost to charges to determine the cost for covered medically necessary services. The costs will be certified as actual expenditures by the hospital and the State claims federal match on the amount of the related certified public expenditures. According to the Centers for Medicare and Medicaid Services (CMS) approved Medicaid State Plan, participating hospitals receive only the federal match portion of the allowable costs. UW Medical Center received $31.6 million in claims payments under this program for the year ended June 30, 2015.

In addition, UW Medical Center receives the federal match portion of Disproportionate Share (DSH) payments, which are the lesser of qualifying uncompensated care cost or the hospital’s specific limit.


(Continued)

UW Medical Center received $20.2 million in DSH funding under this program for the year ended June 30, 2015.

Since the inception of the program, the Washington State Legislature (the State) has provided through an annual budget proviso, a "hold harmless" provision for hospitals participating in the CPE program. Through this proviso, hospitals participating in the CPE program, will receive no less in combined state and federal payments than they would have received under the previous payment methodology. In addition, the hold harmless provision ensures that participating hospitals receive DSH payments as specified in the legislation.

In the event of a shortfall between CPE program payments and the amount determined under the hold harmless provision, the difference is paid to the hospitals as a grant from state only funds. UW Medical Center received $5.6 million in state grants for the year ended June 30, 2015. Claims payments, DSH payments, and state grant funds are included in net patient service revenues in the statement of revenues, expenses, and changes in net position.

CPE payments are subject to retrospective determination of actual costs once UW Medical Center's Medicare Cost Report is audited. CPE program payments are not considered final until retrospective cost reconciliation is complete, after UW Medical Center receives its Medicare Notice of Program Reimbursements (NPR) for the corresponding cost reporting year. To date, only the 2006 CPE program year has had a final settlement.

Interim state grant payments are retrospectively reconciled to "hold harmless" after actual claims are repriced using the applicable DRG payment methodology. This process takes place approximately 12 months after the end of the fiscal year and results in either a payable to, or receivable from, the state Medicaid Program. UW Medical Center has estimated the expected final settlement amounts based on the difference between CPE payments received and the estimated hold harmless amount.

As of June 30, 2015, for fiscal years 2007 through 2015, UW Medical Center had an estimated payable for the CPE program of $22.2 million, which is included as a liability in payable to contractual agencies in the accompanying statement of net position.

***(b) Professional Services Supplemental Payment (PSSP) Program and Provider Access Payment (PAP)***

The professional services supplemental payment (PSSP) and provider access payment (PAP) are programs managed by the Washington State Healthcare Authority (WSHCA) benefiting certain public hospitals. Center for Medicare and Medicaid Services (CMS) approved the PAP program in August 2014 for services on and after July 1, 2014.

Under the program, UW Medical Center, Harborview, VMC, UWP, and Children's University Medical Group (CUMG) receive supplemental Medicaid payments for the physician and other professional services for which they bill. These supplemental payments equal the difference between the standard Medicaid reimbursement and the upper payment limit allowable by federal law. UW Medical Center and Harborview provide the nonfederal share of the supplemental payments that are used to obtain the matching federal funds.

UW Medical Center recorded $9.6 million for the year ended June 30, 2015, in intergovernmental transfers (IGTs) to WSHCA related to professional claims paid in those fiscal years, which is included in nonoperating expenses in the statement of revenues, expenses, and changes in net position.

WSHCA used the federal match funds to make professional services supplemental payments to UW Medicine entities for PSSP and through the Medicaid managed care plans for PAP. UW Medical Center recognized $0.5 million in supplemental payments for the year ended June 30, 2015. These payments are included in net patient service revenues in the statement of revenues, expenses, and changes in net position.

There is no requirement that UWP and CUMG PSSP and PAP payments be returned to Harborview and UW Medical Center as a condition for making the IGT's. PSSP and PAP funds are combined with other revenues used by the School for the central support of faculty costs. As a result, the School requires less funding from UW Medical Center. The faculty support was reduced by $16.9 million in fiscal year 2015. This reduction is included as an offset to purchased services in the statement of revenue, expenses, and changes in net position.

### *(c) Hospital Safety Net Program*

The Hospital Safety Net Assessment Act (HSNA) uses local funds obtained through an assessment levied on Prospective Payment System (PPS) hospitals and federal matching funds to increase Medicaid payments to hospitals. Under this program, PPS program hospitals are assessed a fee on all non-Medicare patient days. Under the original HSNA program, HSNA funds were used to prevent the significant budget cuts proposed during the 2009 session of the state legislature. The original legislation expired on June 30, 2013.

In its 2013 session, the Washington State legislature passed a new assessment program that was similar to the original program as the State will use federal matching funds to increase Medicaid hospital payments. Under the new HSNA program, PPS hospitals receive supplemental Medicaid payments, Critical Access Hospitals receive disproportionate share payments, and CPE hospitals receive state grants. The safety net assessment was subject to approval by the Center for Medicare and Medicaid Services before it took effect. CMS approved this program in 2014. The program has an expiration date of June 30, 2017.

UW Medical Center is exempt from the assessment as the hospital is operated by an agency of the state government and also participates in the CPE program.

UW Medical Center recognized grant funding of $3.3 million for the year ended June 30, 2015, which is recorded in other operating revenue in the statement of revenues, expenses, and changes in net position.

### *(d) Meaningful Use Incentives*

The American Recovery and Reinvestment Act of 2009 (ARRA) established incentive payments to eligible professionals and hospitals participating in Medicare and Medicaid programs that adopt certified electronic health records (EHRs) but only if the technology is being used in a "meaningful" way that supports the ultimate goals of improving quality, safety, and efficiency of care. "Meaningful use" is defined with specific quality performance metrics for eligible healthcare professionals and hospitals and certain thresholds must be met and maintained to receive payment.

UW Medical Center recognized meaningful use incentives of $6.0 million for the year ended June 30, 2015 which are included in other operating revenues in the statement of revenues, expenses, and changes in net position. These amounts may be subject to future audits.

## (4) State Appropriation

An appropriation is made by the State to the University on a biennial basis. UW Medical Center is designated as a division of the major program "hospitals" included within the total appropriation. This appropriation is specifically designated by the State for the training of future healthcare professionals and to upgrade the skills of current practitioners. Due to the nature of the designation, these amounts are included in operating revenues in the accompanying statement of revenues, expenses, and changes in net position. UW Medical Center recognized $6.5 million for the fiscal year ended June 30, 2015.

## (5) Capital Assets

The activity in UW Medical Center's capital asset and related accumulated depreciation accounts for the year ended June 30, 2015 are set forth below (in thousands):

| | | Balance June 30, 2014 | Additions | Transfers | Retirements | Balance June 30, 2015 |
|---|---|---|---|---|---|---|
| Capital assets, not being depreciated: | | | | | | |
| Land | $ | 2,631 | — | — | — | 2,631 |
| Art | | 1,389 | 31 | — | — | 1,420 |
| Construction in process | | 53,930 | 93,832 | (24,112) | — | 123,650 |
| Total capital assets, not being depreciated | | 57,950 | 93,863 | (24,112) | — | 127,701 |
| Capital assets, being depreciated: | | | | | | |
| Land improvements | | 9,989 | — | — | — | 9,989 |
| Buildings, renovations, and furnishings | | 564,615 | — | 3,443 | — | 568,058 |
| Fixed equipment | | 103,081 | — | 2,528 | (397) | 105,212 |
| Movable equipment | | 366,781 | 152 | 18,141 | (3,062) | 382,012 |
| Total capital assets, being depreciated | | 1,044,466 | 152 | 24,112 | (3,459) | 1,065,271 |
| Total capital assets at historical cost | | 1,102,416 | 94,015 | — | (3,459) | 1,192,972 |

| | Balance June 30, 2014 | Additions | Transfers | Retirements | Balance June 30, 2015 |
|---|---|---|---|---|---|
| Less accumulated depreciation for: | | | | | |
| Land improvements | $ (3,336) | (329) | — | — | (3,665) |
| Buildings, renovations, and furnishings | (231,186) | (19,594) | — | — | (250,780) |
| Fixed equipment | (88,547) | (1,744) | — | 351 | (89,940) |
| Movable equipment | (291,033) | (29,936) | — | 3,041 | (317,928) |
| Total accumulated depreciation | (614,102) | (51,603) | — | 3,392 | (662,313) |
| Total capital assets, net | $ 488,314 | 42,412 | — | (67) | 530,659 |

Capital assets, net include intangible assets, net of accumulated depreciation of $11.3 million as of June 30, 2015.

## (6) Long-Term Debt and Capital Leases

Long-term debt, reported as a part of noncurrent liabilities, consists of the following as of June 30, 2015 (in thousands):

| | |
|---|---|
| Internal Lending Program Debt: | |
| Expansion Project, 4.75% to 5.5% interest rate | $ 221,737 |
| All other debts, 3.5% to 5.0% interest rates | 52,245 |
| Capital leases for medical office building and equipment | 758 |
| Total long-term debt | 274,740 |
| Less current portion | (8,972) |
| Total long-term debt, net of current portion | $ 265,768 |

### *(a) Long-term Debt Overview*

Under the "Debt Management Policy: Statement of Objectives and Policies" UW Medical Center obtains capital financing through the University's Internal Lending Program (ILP). The ILP is an internal financing pool intended to lower the University's overall cost of capital and provide a predictable borrowing rate for borrowers within the University. These loans are funded through the issuance of General Revenue bonds and notes. The ILP program policies include a provision for a rate stabilization reserve and a provision for rate adjustments if necessary.

UW Medical Center signed an ILP financing agreement to fund the Montlake Tower expansion project (Expansion Project) in fiscal year 2009. As part of this financing agreement with the ILP, UW Medical Center has agreed to maintain a debt service coverage ratio of 1.25 and days cash on hand of 75 days.

Management believes it was in compliance with these financial ratios at June 30, 2015. This ILP financing agreement specifies the debt to be repaid over a 30-year period at a 5.5% fixed interest rate. Effective, April 1, 2015, the University Board of Regents reduced the ILP interest rate 75 basis points from 5.5% to 4.75% fixed interest rate.

UW Medical Center borrowed $59.1 million from the ILP for the Expansion Project in fiscal year 2015. During construction, interest owed is paid monthly; UW Medical Center began repaying loan principal for the expansion project loan on January 1, 2012.

All other debts borrowed from ILP have interest rates ranging from 3.5% to 5.0% and have annual maturities of varying amounts between fiscal years 2015 and 2027.

### *(b) Long-Term Debt Maturities, Excluding Capital Leases*

The following schedule shows debt service requirements, excluding capital leases, for the next five years and thereafter, as of June 30, 2015, using the fixed interest rates, for both principal and interest (in thousands):

| | | Principal | Interest | Total |
|---|---|---|---|---|
| 2016 | $ | 8,639 | 13,020 | 21,659 |
| 2017 | | 10,735 | 12,571 | 23,306 |
| 2018 | | 10,494 | 12,078 | 22,572 |
| 2019 | | 10,968 | 11,561 | 22,529 |
| 2020 | | 11,483 | 11,022 | 22,505 |
| 2021–2025 | | 61,461 | 46,109 | 107,570 |
| 2026–2030 | | 47,911 | 32,516 | 80,427 |
| 2031–2035 | | 57,705 | 20,202 | 77,907 |
| 2036–2040 | | 31,077 | 8,083 | 39,160 |
| 2041–2045 | | 19,113 | 3,441 | 22,554 |
| Thereafter | | 4,396 | 114 | 4,510 |
| Total payments | $ | 273,982 | 170,717 | 444,699 |

### *(c) Capital Leases*

In fiscal year 1994, UW Medical Center entered into a capital lease with the UW Alumni Association for the UW Medical Center Roosevelt Clinic land and building. The lease specifies that at the end of the 20-year lease term the building and land will become the property of UW Medical Center. The capital lease expired in August 2014.

UW Medical Center has entered into various other lease agreements for certain equipment.



(Continued)

Future minimum lease payments under these agreements are as follows (in thousands):

| | | |
|---|---|---|
| Fiscal year ending June 30: | | |
| 2016 | $ | 343 |
| 2017 | | 343 |
| 2018 | | 87 |
| 2019 | | — |
| Total minimum lease payments | | 773 |
| Less amount representing interest | | (15) |
| Net | | 758 |
| Less current portion | | (333) |
| Present value of capital lease, net of current portion | $ | 425 |

### *(d) Changes in Noncurrent Liabilities*

Changes in noncurrent liabilities during the fiscal year ended June 30, 2015 are summarized below (in thousands):

| | | Balance June 30, 2014 | Increases | Decreases | Balance June 30, 2015 | Due within one year |
|---|---|---|---|---|---|---|
| Long-term debt, ILP – Expansion | $ | 166,203 | 59,155 | (3,621) | 221,737 | 4,084 |
| Long-term debt, ILP – Others | | 57,766 | — | (5,521) | 52,245 | 4,555 |
| Long-term debt, capital leases | | 1,502 | — | (744) | 758 | 333 |
| Unearned revenue | | 4,653 | 3,036 | (1,672) | 6,017 | — |
| Total noncurrent liabilities | $ | 230,124 | 62,191 | (11,558) | 280,757 | 8,972 |

## (7) Risk Management

UW Medical Center is exposed to risk of loss related to professional and general liability, employee medical, dental and pharmaceutical claims, and injuries to employees. UW Medical Center participates in risk pools managed by the University to mitigate risk of loss related to these exposures.

### *(a) Professional and General Liability*

The University's professional liability program currently includes self-insured and commercial reinsurance coverage components. UW Medical Center's annual funding to the professional liability program is determined by the University administration using information from an annual actuarial study. The actuary used a discount rate of 5.5% for 2015 in recognition of the expected earnings of the self-insurance fund and other factors. In addition to the University, the participants in the professional liability program include UW Medical Center, UWP, CUMG, UWNC, School of Dentistry, Airlift, Northwest Hospital, and Harborview. The various participants in the program contribute to the self-insurance fund and share in the expenses of the Health Sciences Risk Management Office.

UW Medical Center's contribution to the professional liability program was $3.8 million in 2015 and recorded in the supplies and other on the statement of revenues, expenses, and changes in net position.

### *(b) Employee Medical and Workers' Compensation*

The University pools employee benefit costs, including employee medical and workers' compensation, for all University employees. Departments, divisions, agencies, and affiliated organizations with employees covered under University benefit programs are charged a single benefit rate, based on employee salary class.

UW Medical Center, as a division of the University with employees covered under University benefit programs, participates in the benefit pool. See further discussion in note 9.

## (8) Benefit Costs

Benefit costs are pooled centrally for all University employees. Annually, the University reviews total employee benefit costs and prepares standard benefit load rates by employment classification. Departments, divisions, agencies, component units, and related parties of the University that have University employees qualifying for employee benefit coverage are charged a cost allocation using the determined benefit load rate and budgeted salary dollars by employment classification. All funding of obligations are on a pay-as-you-go basis. At the end of the reporting period, the cost allocation is compared to actual benefit costs and differences between actual and budgeted costs are included as a component of the benefit load rates charged in the following year.

Employee benefits covered under the benefit pool include the following:

- Workers' compensation
- Unemployment compensation
- Employee medical, dental, and vision
- Retirement and other postretirement benefit plans
- Social security
- Medicare
- Separation leave

During the fiscal year ended June 30, 2015, UW Medical Center incurred and paid $97.3 million to the University for the employee benefits listed above, which is recorded as employee benefits in the statement of revenues, expenses, and changes in net position.

***Retirement and Other Postretirement Benefit Plans***

UW Medical Center employees can participate in the following state and University sponsored retirement and other postretirement benefit plans:

**University of Washington Retirement Plan (UWRP)** – UWRP is a defined-contribution plan administered by the University. All faculty and professional staff are eligible to participate in the plan. Contributions to UWRP are invested by participants in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations. Benefits from fund sponsors are available upon separation or retirement at the member's option. RCW 28B.10.400 et. Seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

Funding is determined by employee age and ranges from 5% to 10% of employee salary. Funding obligations are calculated at the University level and the University allocates expense to department, divisions, agencies, and component units through the benefit load.

Based on the University's benefit load apportionment UW Medical Center incurred and paid $4.1 million in fiscal year 2015 related to annual UWRP funding, which is recorded in employee benefits on the statement of revenues, expenses, and changes in net position.

**University of Washington Supplemental Retirement Plan (the 401(a) Plan)** – The 401(a) Plan provides for a supplemental payment component, which guarantees a minimum retirement benefit based upon a one-time calculation at each eligible participant's retirement date. The University makes direct payment to qualifying retirees when the retirement benefits provided by UWRP do not meet the benefit goals.

The University receives an independent actuarial valuation to determine funding needs for the supplemental payment component of UWRP. The funding obligation is determined at the University level and the University allocates expense to departments, divisions, agencies, and component units through the benefit load.

Based on the University's benefit load apportionment UW Medical Center incurred and paid $0.8 million in fiscal year 2015, related to annual 401(a) Plan funding, which is recorded in employee benefits on the statement of revenues, expenses, and changes in net position.

**Other Post Employment Benefits (OPEB)** – All University employees, including medical center employees, are eligible for participation in healthcare and life insurance programs administered by the WSHCA. UW Medical Center retirees may elect coverage through state health and life insurance plans, for which they pay less than the full cost of the benefits based on their age and other demographic factors.

The Office of the State Actuary determines total OPEB obligations at the State level using individual state employee data, including age, retirement eligibility, and length of service. Information to support actuarial calculations at the division, department, or component unit level is not available. The State is ultimately responsible for the obligation; therefore, the annual required contribution (ARC) is not recorded at the University or its departments, divisions, agencies, or component units.

## (9) Pension Plans

As University employees, employees who work at UW Medical Center employees can participate in the state and retirement plans in the Public Employees' Retirement System, which is a defined-benefit retirement plan.

### Plan Description

### Public Employees' Retirement System

The Public Employees' Retirement System (PERS) was established in 1947 and its retirement benefit provisions are contained in chapters 41.34 and 41.40 of the Revised Code of Washington (RCW). PERS is a cost-sharing multiple-employer retirement system comprised of three separate pension plans for membership purposes. PERS Plan 1 and PERS Plan 2 are defined benefit plans, and PERS Plan 3 is a defined benefit plan with a defined contribution component. PERS members include higher education employees not participating in higher education retirement programs.

PERS is comprised of and reported as three separate plans for accounting purposes: Plan 1, Plan 2/3 and Plan 3. Plan 1 accounts for the defined benefits of Plan 1 members. Plan 2/3 accounts for the defined benefits of Plan 2 members and the defined benefit portion of benefits for Plan 3 members. Plan 3 accounts for the defined contribution portion of benefits for Plan 3 members. Although members can only be a member of either Plan 2 or Plan 3, the defined benefit portions of Plan 2 and Plan 3 are accounted for in the same pension trust fund. All assets of Plan 2/3 may legally be used to pay the defined benefits of any of the Plan 2 or Plan 3 members or beneficiaries, as defined by the terms of the plan. Therefore, Plan 2/3 is considered to be a single plan for accounting purposes.

### The Pension Plans' Fiduciary Net Positions

The pension plans' fiduciary net position has been determined on the same basis used by the pension plan. The Department of Retirement Systems (DRS) financial statements have been prepared in conformity with GAAP. The retirement plans are accounted for in pension trust funds using the flow of economic resources measurement focus and the accrual basis of accounting. Plan member contributions are recognized as revenues in the period in which the contributions are earned. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

The Washington State Investment Board (WSIB) has been authorized by statute (Chapter 43.33A RCW) as having the investment management responsibility for Retirement Funds. Investments are reported at fair value and unrealized gains and losses are included as investment income in the statement of changes in fiduciary net position. Purchases and sales of investments are also recorded on a trade-date basis.

DRS publishes its annual report for retirement plans that are available at:
http://www.drs.wa.gov/administration/annual-report/.

**Actuarial Assumptions**

The total pension liability was determined by an actuarial valuation as of June 30, 2013, with the results rolled forward to June 30, 2014.

The following actuarial assumptions, applied to all prior periods included in the measurement.

| | |
|---|---|
| Inflation | 3.0% total economic inflation, 3.75% salary inflation |
| Salary increase | Expected to grow by promotions and longevity in addition to salary inflation assumption |
| Investment rate of return | 7.50% |

Mortality rates were based on the RP-2000 Combined Healthy Table and Combined Disabled Table published by the Society of Actuaries. The Office of State Actuary (OSA) applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100% Scale BB. Mortality rates are applied on a generational basis; meaning, each member is assumed to receive additional mortality improvements in each future year throughout their lifetime.

The actuarial assumptions used in the June 30, 2013 valuation were based on the results of OSA's 2007-2012 Experience Study. Additional assumptions for subsequent events and law changes are current as of the 2013 actuarial valuation report.

**Discount Rate**

The discount rate used to measure the total pension liabilities was 7.50% for all plans in which the University participates. To determine the discount rate, an asset sufficiency test was completed to test whether the pension plan's fiduciary net position was sufficient to make all projected future benefit payments of current plan members. Consistent with current law, the asset sufficiency test for PERS included an assumed 7.70% long-term discount rate to determine funding liabilities for calculating future contribution rate requirements.

Consistent with the long-term expected rate of return, a 7.50% future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue to be made at contractually required rates (including the component of PERS Plan 2/3 employer rates intended to address the unfunded actuarial accrued liability for PERS Plan 1 as provided for in Chapter 41.45 RCW).

Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.50% on pension plan investments was applied to determine the total pension liability.



(Continued)

**Sensitivity of the Net Pension Liability to Changes in the Discount Rate**

The following presents the net pension liability of UW Medical Center calculated using the discount rate of 7.50%, as well as what the employers' net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50%) or 1-percentage-point higher (8.50%) than the current rate.

| | | Discount rate | | |
|---|---|---|---|---|
| **Plan** | | **1% lower** | **Current rate** | **1% higher** |
| | | | (in thousands) | |
| PERS 1 | $ | 142,527 | 115,632 | 92,544 |
| PERS 2/3 | | 241,935 | 58,001 | (82,490) |

**Long-term Expected Rate of Return**

The long-term expected rate of return on pension plan investments was determined by the WSIB. The rate approximately equals the median of the simulated investment returns over a fifty-year time horizon, increased slightly to remove WSIB's implicit, small, short-term downward adjustment due to assumed mean reversion. WSIB's implicit short-term adjustment, while small and appropriate over a 10- to 15-year period, becomes amplified over a 50-year measurement period.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which a best-estimate of expected future rates of return (expected returns, net of pension plan investment expense, but including inflation) are developed for each major asset class by the WSIB. Those expected returns make up one component of WSIB's Capital Market Assumptions (CMAs).

The CMAs contain three pieces of information for each class of assets the WSIB currently invest in:

- Expected annual return
- Standard deviation of the annual return
- Correlations between the annual returns of each asset class with every other asset class

WSIB uses the CMAs and their target asset allocation to simulate future investment returns over various time horizons.

 (Continued)

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2014 are summarized in the following table:

| Asset class | Target allocation | % Long-term expected real rate of return |
|---|---|---|
| Fixed income | 20.00% | 0.80% |
| Tangible assets | 5.00 | 4.10 |
| Real estate | 15.00 | 5.30 |
| Global equity | 37.00 | 6.05 |
| Private equity | 23.00 | 9.50 |

The inflation component used to create the above table is 2.70%, and represents WSIB's most recent long-term estimate of broad economic inflation.

### Employer Contribution Rates

Employer contribution rates are developed in accordance with Chapter 41.45 of the RCW by the OSA, and include an administrative expense component that is currently set at 0.18%. The statute provides authority to the Pension Funding Council to adopt changes to economic assumptions and contribution rates.

### UW Medical Center Proportionate Share

Collective pension amounts are determined as of a measurement date, which can be no earlier than an employer's prior fiscal year. The measurement date for the net pension liabilities recorded by the University and UW Medical Center as of June 30, 2015 was June 30, 2014. University contributions received and processed by DRS during the fiscal year ended June 30, 2014 have been used as the basis for determining the University's proportionate share of the collective pension amounts reported by DRS in their June 30, Schedules of Employer and Nonemployer Allocations for all plans in which the University participates.

UW Medical Center proportionate share for the year ended June 30, 2015 was determined by the proportion of UW Medical Center's employer contributions to total University employer contributions as of the measurement date:

| Plan | Proportionate share for the year ended June 30, 2015 |
|---|---|
| PERS 1 | 2.29539% |
| PERS 2/3 | 2.86941% |

### UW Medical Center Aggregated Balances

UW Medical Center aggregated balances of net pension liabilities, net pension assets, and deferrals as of the fiscal year ended June 30, 2015 and are presented in the table below.

| | | June 30, 2015 | | |
|---|---|---|---|---|
| **Plan** | | **Net pension liability** | **Deferred outflows** | **Deferred inflows** |
| | | | (in thousands) | |
| PERS 1 | $ | 115,632 | 10,994 | 14,459 |
| PERS 2/3 | | 58,001 | 14,815 | 61,482 |
| Total | $ | 173,633 | 25,809 | 75,941 |

### PERS Plan 1

PERS Plan 1 is closed to new entrants.

#### Vesting

PERS 1 members were vested after the completion of five years of eligible service.

#### Benefits Provided

PERS Plan 1 provides retirement, disability, and death benefits. Retirement benefits are determined as 2% of the member’s average final compensation (AFC) times the member’s years of service. The AFC is the average of the member’s 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service.

Members retiring from inactive status prior to the age of 65 may receive actuarially reduced benefits. PERS Plan 1 retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and nonduty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries.

#### Contributions

The PERS Plan 1 employer contribution rates for the fiscal years ended June 30, 2015 was 9.21%. UW Medical Center contributions to PERS 1 for the year ended June 30, 2015 was $11.0 million.

#### Proportionate Share of PERS 1 Pension Expense and Deferrals Related to Pensions

UW Medical Center’s pension expense for the fiscal year ended June 30, 2015 was $11.1 million and reported on the statement of revenues, expenses, and changes in net position in benefits expense.

UW Medical Center's deferred outflows of resources and deferred inflows of resources related to pensions for the fiscal year ended June 30, 2015 are presented in the following table (in thousands):

| Description | | Deferred outflows of resources | Deferred inflows of resources |
|---|---|---|---|
| Difference between projected and actual earnings on plan investments, net | $ | — | 14,459 |
| UW Medical Center's contributions to plans subsequent to the measurement date of collective net pension liability | | 10,994 | — |

The amount of $10.9 million reported as a deferred outflow of resource relates to UW Medical Center contributions to the University subsequent to the measurement date and will be recognized as a reduction of the net pension liability for year ended June 30, 2016. Other amounts as reported deferred inflows of resources related to PERS 1 will be recognized in pension expense as follows (in thousands):

| | | |
|---|---|---|
| Year: | | |
| 2016 | $ | 3,615 |
| 2017 | | 3,615 |
| 2018 | | 3,615 |
| 2019 | | 3,614 |
| 2020 | | — |
| Total | $ | 14,459 |

**PERS Plan 2/3**

**Vesting**

PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

**Benefits Provided**

PERS Plan 2/3 provides retirement, disability, and death benefits. Retirement benefits are determined as 2% of the member's AFC times the member's years of service for Plan 2 and 1% of AFC for Plan 3.

The AFC is the monthly average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55 years of age or older are eligible for early retirement with a reduced benefit. The benefit is reduced by a factor that varies according to age, for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions, if hired prior to May 2, 2013:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit.

Other PERS Plan 2/3 benefits include duty and nonduty disability payments, a cost-of-living allowance (based on the Consumer Price Index), capped at three percent annually and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries.

**Contributions**

The PERS Plan 2/3 employer contribution rates for the fiscal years ended June 30, 2015 was 9.21%. The Plan 2/3 employer rates include a component to address the PERS Plan 1 unfunded actuarial accrued liability and an administrative expense that is currently set at 0.18%.

UW Medical Center contributions to PERS 2/3 for the year ended June 30, 2015 was $13.4 million, as determined by rates established in accordance with RCW 41.45.

**Proportionate Share of PERS 2/3 Pension Expense and Deferrals Related to Pensions**

UW Medical Center's pension expense for the fiscal year ended June 30, 2015 was $9.7 million and is reported on the statement of revenues, expenses, and changes in net position in benefits expense.

UW Medical Center's deferred outflows of resources and deferred inflows of resources related to pensions for the fiscal year ended June 30, 2015 are presented in the following table (in thousands):

| Description | | Deferred outflows of resources | Deferred inflows of resources |
|---|---|---|---|
| Difference between projected and actual earnings on plan investments, net | $ | — | 61,482 |
| UW Medical Center's contributions to the University subsequent to the measurement date of collective net pension liability | | 13,353 | — |
| Change in UW Medical Center's proportionate share | | 1,462 | — |

The amount of $13.3 million reported as deferred outflows of resources relates to UW Medical Center contributions to the University subsequent to the measurement date, which will be recognized as a reduction of the net pension liability for year ended June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions pertaining to PERS 2/3 will be recognized in pension expense as follows (in thousands):

| | | |
|---|---|---|
| Year: | | |
| 2016 | $ | 15,005 |
| 2017 | | 15,005 |
| 2018 | | 15,005 |
| 2019 | | 15,005 |
| 2020 | | — |
| Total | $ | 60,020 |

## (10) Related Parties

UW Medical Center has engaged in a number of transactions with related parties. These transactions are recorded by UW Medical Center as either revenue or expense transactions because economic benefits are either provided or received by UW Medical Center. UW Medical Center records cash transfers between UW Medical Center and related parties that are not the result of economic benefits and are presented as other, net on the statements of revenues, expenses, and changes in net position.

### *(a) University of Washington*

University divisions provide various levels of support to UW Medical Center. The following is a summary of services purchased.

**UW School of Medicine**

UW Medical Center purchases a variety of clinical and administrative services from the School, which includes laboratory services and resident and faculty support. UW Medical Center also transfers a portion of its Medicare reimbursement for medical education to the School in support of teaching costs. The amounts for these services are shown below (see (f)).

**UW Medicine Central Costs**

UW Medicine provides services to UW Medical Center such as advancement, compliance, telemedicine, community relations staffing, medical staff oversight, marketing, and other administrative services related to UW Medicine. The amounts paid by UW Medical Center for these services are shown below (see (f)).

**UW Physicians Network dba UW Neighborhood Clinics**

Under an annual agreement between the involved UW Medicine entities, UW Medical Center provides strategic support of approximately 80% of UWNC annual operating loss and capital funding needs for fiscal year 2015. Funding from UW Medical Center to UWNC was $25.2 million for fiscal year 2015 and is recorded as a nonoperating expense in the statement of revenues, expenses, and changes in net position. Included in the amounts above, capital funding of $0.7 million was made by UW Medical Center to UWNC for fiscal 2015.

**University of Washington Consolidated Laundry**

UW Medical Center purchases laundry services from University of Washington Consolidated Laundry (the Laundry). Additionally, the Laundry transfers funds to UW Medical Center for the purposes of satisfying debt and capital accumulation requirements and excess funds for investment with the UW Medical Center's funds held by UW. UW Medical Center records these amounts as payables to the Laundry. The amounts for these transactions are shown below (see (f)).

**Other Divisions of the University**

In addition to the divisions and transactions identified above UW Medical Center purchases information technology services, general and professional liability insurance, printing, internal audit, accounting, temporary staffing, and other administrative and operational services from other divisions of the University. The amounts for these transactions are shown below (see (f)).

***(b) UW Medicine/Northwest dba Northwest Hospital & Medical Center***

In 2015, UW Medical Center provided strategic support to Northwest Hospital for operating purposes. Funding from UW Medical Center to Northwest Hospital was $3.4 million for the year ended June 30, 2015 and is recorded as funding to affiliates in the statement of revenues, expenses, and changes in net position and as accounts payable in the statement of net position.

***(c) Seattle Cancer Care Alliance***

UW Medical Center is a one-third owner in the SCCA and accounts for its interest under the equity method of accounting. Nonoperating income of $6.3 million was recorded in fiscal year 2015 and is included in investment income in the statements of revenues, expenses, and changes in net position. The following is a summary of the SCCA's financial results for the year ended June 30, 2015 (in thousands):

| | | |
|---|---|---|
| Assets | $ | 523,791 |
| Liabilities | $ | 187,969 |
| Unrestricted net assets | | 333,024 |
| Temporarily restricted net assets | | 1,812 |
| Permanently restricted | | 986 |
| Total liabilities and net assets | $ | 523,791 |
| Revenues | $ | 475,921 |
| Expenses | | 441,517 |
| Nonoperating expense | | (17,185) |
| Excess of revenues over expenses | | 17,219 |
| Contributions restricted for capital acquisition | | 21 |
| Change in net unrealized loss on investments | | (32) |
| Increase in unrestricted net assets | $ | 17,208 |

SCCA operates a 20-bed unit located within UW Medical Center in which its adult inpatients receive care. The 20-bed unit qualifies as a hospital within a hospital for Medicare reimbursement purposes. SCCA provides medical oversight and management of the inpatient unit. Under agreements, UW Medical Center provides and bills for inpatient care services to the SCCA including necessary personnel, equipment, and ancillary services and UW Medical Center purchases administrative and program support services from the SCCA. Payments due to UW Medical Center for services provided to the SCCA inpatients in fiscal year 2015 are included in net patient service revenues.

UW Medical Center also provides various services to the SCCA's outpatient facility, including certain pharmacy, laboratory, and pathology services as well as billing, purchasing, and other administrative services. Fees for such services and supplies provided by UW Medical Center are included in other revenue. The amounts for these transactions are shown below (see (f)).

***(d) Fred Hutchinson Cancer Research Center***

The SCCA partnership agreement provides that UW Medical Center will make various payments to FHCRC related to research and development support, data collection and analysis, physician assistance services, consulting services, and license rights to use the FHCRC name in connection with the inpatient oncology services program. These fees are included in other expenses and are included in the tables below (see (f)).

***(e) Harborview Medical Center***

UW Medical Center provides services and support to Harborview such as administrative and operational services. Harborview provides UW Medical Center with services and support such as pharmacy refills and lab testing as well as other administrative and operational services. The amounts paid for these services are included in the tables below (see (f)).

### *(f) Summary of Related-Party Transactions (In Thousands)*

| **Revenue (expense) transactions** | | |
|---|---|---|
| Services and supplies purchased from the University and its departments and affiliates: | | |
| The School | $ | (121,868) |
| UW Medicine Central Costs | | (10,813) |
| The Laundry | | (4,389) |
| UWP | | (488) |
| UW Medicine ITS | | (59,755) |
| Other University division and departments | | (47,559) |
| Services and supplies purchased from Harborview | | (2,417) |
| Services and supplies purchased from SCCA | | (11,775) |
| Services and supplies purchased from FHCRC | | (13,011) |
| Services and supplies provided to the University and its department and affiliates: | | |
| The School | | 2,430 |
| UWP | | 2,295 |
| UWNC | | 4,430 |
| Services and supplies provided to Northwest Hospital | | 1,187 |
| Services and supplies provided to SCCA | | 47,806 |
| Services and supplies provided to Harborview | | 2,687 |

Related-party receivable and payable amounts are recorded in other receivables, accounts payable and accrued expenses, respectively. As of June 30, 2015, UW Medical Center had net amounts (due to) or due from related parties for the various transactions, which are as follows (in thousands):

| **Net receivable (payable)** | | |
|---|---|---|
| University of Washington and its departments and affiliates: | | |
| The School | $ | (10,038) |
| The Laundry | | (367) |
| UWP | | 922 |
| UWNC | | 6,249 |
| Other University divisions and departments | | (11,270) |
| SCCA | | 21,539 |
| Northwest Hospital | | (2,856) |
| Harborview | | (937) |
| FHCRC | | (3,012) |

## (11) Commitments and Contingencies

### *(a) Operating Leases*

UW Medical Center leases medical office space and equipment under operating lease arrangements. Total rental expense in fiscal year ended June 30, 2015 for all operating leases was $11.2 million.


(Continued)

The following schedule shows future minimum lease payments by fiscal years as of June 30 (in thousands):

| | | |
|---|---|---|
| 2016 | $ | 6,817 |
| 2017 | | 6,820 |
| 2018 | | 5,875 |
| 2019 | | 3,062 |
| 2020 | | 1,859 |
| 2021–2025 | | 9,732 |
| 2026–2030 | | 8,931 |
| 2031–2035 | | 5,687 |
| 2036–2040 | | 5,979 |
| 2041–2045 | | 3,787 |
| Total | $ | 58,549 |

***(b) Purchase Commitments***

UW Medical Center has current commitments at June 30, 2015 of approximately $25.5 million related to various construction projects, equipment purchases, and information technology implementations. UW Medical Center intends to use its funds held by UW and ILP for these commitments.

***(c) Regulatory Environment***

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, governmental healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government agencies are actively conducting investigations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs, together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Medical Center is in compliance with the fraud and abuse regulations as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions known or unasserted at this time.

***(d) Litigation***

UW Medical Center is involved in litigation arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect to UW Medical Center’s financial position or results of operations.

### *(e) Collective Bargaining Agreements*

UW Medical Center has a total of approximately 4,368 employees. Of this total, approximately 80% are covered by collective bargaining agreements as of June 30, 2015. Nurses are represented by Washington State Nurses Association (WSNA) and the Service Employees International Union (SEIU) and other healthcare and support workers are represented by the SEIU and Washington Federation of State Employees (WSFE). All UW Medical Center collective bargaining agreements expired on June 30, 2015. UW Medical Center's management and WSNA continue to negotiate the terms of a new agreement, and during the interim period, WSNA members continue to work under the terms of the expired agreement. SEIU and WFSE collective bargaining agreements were signed and expire June 30, 2017.

### *(f) Husky Stadium Lease*

In fiscal year 2013, UW Medical Center entered into a lease agreement with the University of Washington Department of Intercollegiate Athletics for approximately 30,660 square feet within the Husky Stadium. The space will be used for the UW Medicine Sports Medicine Clinic. The lease term is 30 years beginning September 1, 2013 ending on August 31, 2043. Annual rent expense will be between $0.8 million and $1.2 million. In addition to rent expense, UW Medical Center will pay monthly operating expenses that are assessed annually.

**UNIVERSITY OF WASHINGTON MEDICAL CENTER**
(A Division of the University of Washington)

Schedules of Required Supplementary Information

June 30, 2015

The Schedules of Required Supplementary Information below reflect information for the University of Washington as a whole due to the contraints of available information for the University of Washington Medical Center.

**Schedule of the University's Proportionate Share of the Net Pension Liability**
**PERS 1 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| University's proportion of the net pension liability (asset) | | 8.28% |
| University's proportionate share of the net pension liability (asset) | $ | 417,231 |
| University's covered-employee payroll | | 25,376 |
| University's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll | | 1,644.20% |
| Plan fiduciary net position as a percentage of the total pension liability | | 61.19 |

**Schedule of the University's Contributions**
**PERS 1 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| Contractually required contribution | $ | 2,311 |
| Contributions in relation to the contractually required contribution | | 2,313 |
| Contribution deficiency (excess) | | (2) |
| University's covered-employee payroll | | 25,376 |
| Contributions as a percentage of covered-employee payroll | | 9.11% |

**Schedule of the University's Proportionate Share of the Net Pension Liability**
**PERS 2/3 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| University's proportion of the net pension liability (asset) | | 10.00% |
| University's proportionate share of the net pension liability (asset) | $ | 202,225 |
| University's covered-employee payroll | | 856,839 |
| University's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll | | 23.60% |
| Plan fiduciary net position as a percentage of the total pension liability | | 93.29 |

**Schedule of the University's Contributions**
**PERS 2/3 Pension Plan**

(Dollar amounts in thousands)

| | | |
|---|---|---|
| Contractually required contribution | $ | 78,164 |
| Contributions in relation to the contractually required contribution | | 78,160 |
| Contribution deficiency (excess) | | 4 |
| University's covered-employee payroll | | 856,839 |
| Contributions as a percentage of covered-employee payroll | | 9.12% |

**Notes to required supplementary information for the year ended June 30, 2015**

*Changes of Benefit Terms*: Amounts reported in 2015 reflect no change in benefit terms.

**HARBORVIEW MEDICAL CENTER**
(A Component Unit of King County)
(Operated by the University of Washington)

Financial Statements

June 30, 2015 and 2014

(With Independent Auditors' Report Thereon)

**HARBORVIEW MEDICAL CENTER**
(A Component Unit of King County)
(Operated by the University of Washington)

## Table of Contents

**KPMG LLP**
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

# Independent Auditors' Report

The Board of Trustees
Harborview Medical Center:

We have audited the accompanying basic financial statements of the business-type activities of Harborview Medical Center, a discretely presented component unit of King County, which comprise of the statements of net position as of June 30, 2015 and 2014, and the related statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

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

Management is responsible for the preparation and fair presentation of these basic 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 basic 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 basic financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the basic 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 basic 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 basic 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 basic financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of Harborview Medical Center as of June 30, 2015 and 2014, and the changes in its net position and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

***Other Matters***

U.S. generally accepted accounting principles require that the Management's Discussion and Analysis on pages 3 and 15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with U.S. generally accepted accounting principles, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

KPMG LLP

Seattle, Washington
October 16, 2015

The following discussion and analysis provides an overview of the financial position and activities of Harborview Medical Center (Harborview), for the years ended June 30, 2015 and 2014. This discussion has been prepared by management and is designed to focus on current activities, resulting changes, and current known facts and should be read in conjunction with the financial statements and accompanying notes that follow this section.

Harborview is a discretely presented component unit of King County and part of UW Medicine through a management contract that includes: UW Medical Center, Northwest Hospital & Medical Center (Northwest Hospital), Valley Medical Center (VMC), UW Physicians Network dba UW Neighborhood Clinics (UWNC), UW Physicians (UWP), the UW School of Medicine (the School), and Airlift Northwest (Airlift).

## Using the Financial Statements

Harborview's financial statements consist of three statements: statements of net position; statements of revenues, expenses, and changes in net position; and statements of cash flows. These financial statements and related notes provide information about the activities of Harborview, including resources held by Harborview but restricted for specific purposes by contributors, grantors, or enabling legislation.

The statements of net position includes all of Harborview's assets and liabilities, using the accrual basis of accounting, as well as an indication about which assets can be used for general purposes and which are designated for a specific purpose. The statements of net position also include information to help compute the rate of return on investments, evaluate the capital structure of Harborview, and assess the liquidity and financial flexibility of Harborview.

The statements of revenues, expenses, and changes in net position reports all of the revenues and expenses during the time period indicated. Net position, the difference between the sum of assets and the sum of liabilities, is one way to measure the financial health of Harborview and whether the organization has been able to recover all its costs through net patient service revenues and other revenue sources.

The statements of cash flows reports the cash provided by Harborview's operating activities, as well as other cash sources such as investment income and cash payments for capital additions and improvements and funding to affiliates. These statements provide meaningful information on where Harborview's cash was generated and what it was used for.

## Results of Operations for Fiscal Year 2015

Harborview reported operating income of $61.1 million and an increase in net position of $35.2 million for the year ended June 30, 2015 compared to an operating loss of $0.8 million and decrease in net position of $6.8 million for the year ended June 30, 2014. The positive net income in 2015 can primarily be attributed to higher volume of inpatient surgical cases, outpatient pharmacy revenue, higher acuity, as well as additional reimbursement that resulted from previously uninsured patients being eligible for Medicaid under Medicaid expansion. Other factors contributing to the positive financial results include focused management of expenses and successful process improvement initiatives in the areas of revenue cycle and supply chain management.

**HARBORVIEW MEDICAL CENTER**
(A Component Unit of King County)
(Operated by the University of Washington)

Management's Discussion and Analysis (Unaudited)

June 30, 2015 and 2014

| | | 2015 | 2014 | 2013 |
|---|---|---|---|---|
| | | | (In thousands) | |
| Total operating revenues | $ | 929,889 | 814,652 | 788,387 |
| Total operating expenses | | 868,697 | 815,436 | 796,872 |
| Income (loss) from operations | | 61,192 | (784) | (8,485) |
| Investment income, net | | 1,823 | 2,670 | 2,737 |
| Interest expense | | (212) | (161) | (217) |
| Other, net | | (26,297) | (8,855) | (8,345) |
| Nonoperating expenses | | (24,686) | (6,346) | (5,825) |
| Capital contributions and other | | (1,257) | 328 | 1,076 |
| Increase (decrease) in net position | | 35,249 | (6,802) | (13,234) |
| Net position, beginning of year | | 615,667 | 622,469 | 635,703 |
| Net position, end of year | $ | 650,916 | 615,667 | 622,469 |

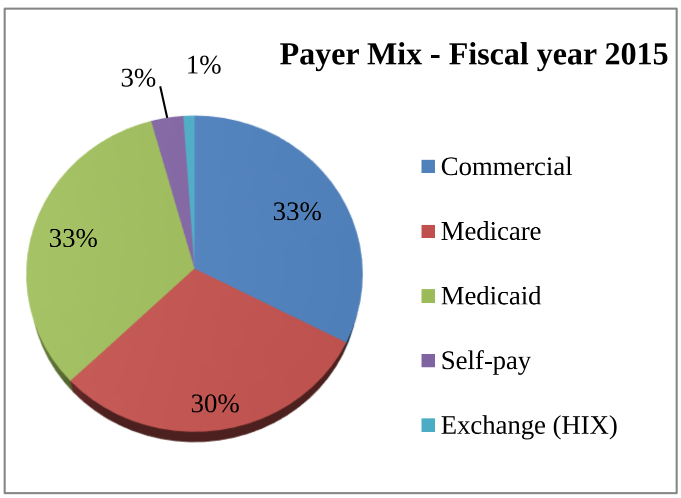
For the year ended June 30, 2014, Harborview reported an operating loss of $0.8 million and decrease in net position of $6.8 million compared to the reported operating loss of $8.5 million and a decrease in net position of $13.2 million for the year ended June 30, 2013. Decreased patient admissions, offset by increased surgical volumes, expansion of Medicaid and federal and state funding programs, such as electronic health record incentive payments and Hospital Safety Net program contributed to the favorable operating performance for fiscal years 2014 as compared to 2013.

| | 2015 | 2014 | 2013 |
|---|---|---|---|
| Available beds | 413 | 413 | 413 |
| Admissions | 17,362 | 17,176 | 17,999 |
| Patient days | 138,214 | 132,284 | 135,779 |
| Average length of stay | 8.0 | 7.7 | 7.5 |
| Occupancy | 92% | 88% | 90% |
| Case mix index (CMI) | 2.150 | 2.100 | 1.986 |
| Surgery cases | 16,280 | 15,938 | 15,488 |
| Emergency room visits | 62,217 | 64,512 | 66,285 |
| Primary care clinic visits | 81,968 | 83,148 | 82,873 |
| Specialty care clinic visits | 165,647 | 164,201 | 162,878 |
| Full-time equivalents (FTEs) | 4,476 | 4,475 | 4,763 |
| Trauma cases | 6,190 | 5,888 | 6,248 |

***Total Operating Revenues***

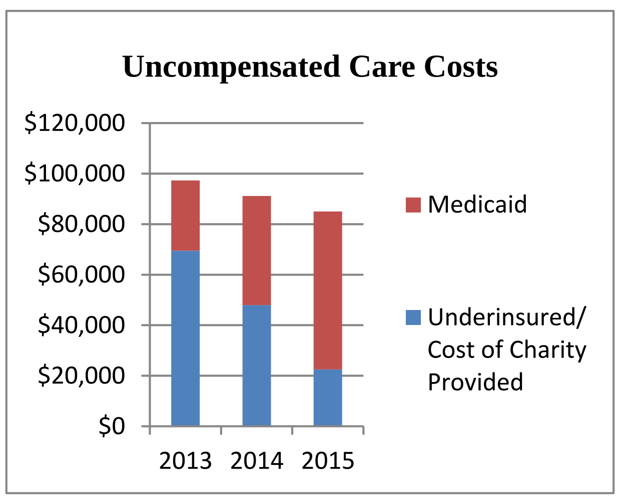
Total operating revenues consists primarily of net patient service revenues, state appropriations, and other operating revenues. Net patient service revenues are recorded based on standard billing rates less contractual adjustments, charity, and a provision for uncollectible accounts. Harborview has agreements with federal and state agencies, and commercial insurers that provide for payments at amounts different from gross charges. Harborview provides care at no charge or reduced charges to patients who qualify under Harborview's charity policy. Harborview also estimates the amount of accounts receivable due from patients that will become uncollectible which is also reported as a reduction of net patient service revenues. The difference between gross charges and the estimated net realizable amounts from payers and patients is recorded as an adjustment to charges. The resulting net patient service revenue is shown in the statements of revenues, expenses, and changes in net position.

Net patient service revenues comprise both inpatient and outpatient revenue. Outpatient revenue consists of both hospital-based and other clinic network revenue. Other operating revenue comprises hospital-related revenues such as grant and contract revenue as well as parking and cafeteria revenues.




Harborview's payer mix is a key factor in the overall financial operating results. The chart to the left illustrates payer mix for 2015. For the years ended June 30, 2015 and 2014, Medicaid revenue represented 33% and 30% and self-pay revenue represented 3% and 7%, respectively. The increase in Medicaid revenue is a direct result of the expansion of the Medicaid program in Washington State as part of the Affordable Care Act.

Due to Medicaid expansion, many patients who were previously self-pay now qualify for Medicaid coverage, thus there is a decrease in the number of applicants for charity care and a decrease in the cost of charity care provided. However, Harborview has seen a corresponding increase in uncompensated costs related to providing care to Medicaid patients. The table to the right shows the shift in uncompensated care costs from charity care to Medicaid.

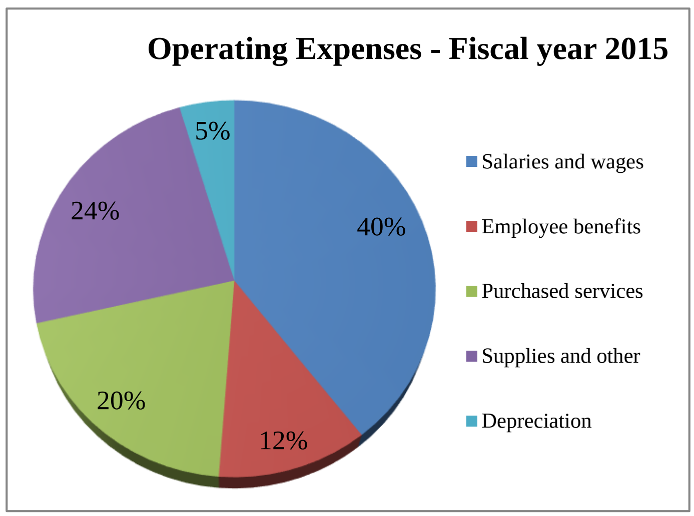


Reimbursement from governmental payers is generally below commercial rates and reimbursement rules are complex and subject to both interpretation and settlements. With the expansion of Medicaid, Harborview has higher government revenues which are subject to settlements.

For the years ended June 30, 2015, 2014, and 2013, Harborview's total operating revenues were $929.9 million, $814.7 million and $788.4 million, which was composed of $858.8 million, $747.9 million, and $724.3 million in net patient service revenues and $71.0 million, $66.8 million, and $64.1 million of state appropriations and other operating revenue, respectively. The increase in fiscal year 2015 was driven by an increase in net patient service revenue as a result of higher case acuity, greater volumes, and favorable payer mix. The increase in fiscal year 2014 was driven by an increase in net patient service revenues due to increases in case acuity and favorable payer mix.

***Total Operating Expenses***

Total operating expenses were $868.7 million for fiscal year 2015 compared to $815.4 million for fiscal year 2014 and $796.9 million for fiscal year 2013. The composition of fiscal year 2015 operating expenses is illustrated in the chart to the right.




Effective July 2013, UW Medicine adopted a purchased service model for their shared services function related to information technology services. With this adoption, Harborview's allocation of IT operating costs are recorded as purchased services in 2014. Previously, IT operating costs allocated to Harborview were recorded as salaries and wages, benefits, purchased services, and depreciation expense.

**Salaries and wages** increased $16.4 million from $327.1 million in fiscal year 2014 to $343.5 million in fiscal year 2015. The increase in salaries and wages in fiscal year 2015 is primarily attributed to labor associated with higher than anticipated occupancy, employee merit increases, and the vacation and sick leave accrual impact.

Salaries and wages decreased $17.7 million from $344.8 million in fiscal year 2013 to $327.1 million in fiscal year 2014. The decrease in salaries and wages in fiscal year 2014 is primarily attributed to the adoption of the purchased service model for IT services as described above, offset by employee merit increases.

**Employee benefits** decreased $2.1 million from $103.2 million in fiscal year 2014 to $101.1 million in fiscal year 2015 and decreased $12.5 million from $115.7 million in fiscal year 2013 to $103.2 million in fiscal year 2014. Employee benefit expense decreased during fiscal year 2014 and 2015 as a result of an overall decrease in the University benefit load rate.

**Purchased services,** which consist of professional and consulting fees, increased $7.1 million from $168.6 million in fiscal year 2014 to $175.7 million in fiscal year 2015, and increased $40.7 million from

\$127.9 million in fiscal year 2013 to \$168.6 million in fiscal year 2014. The increase in purchased services between fiscal year 2015 and 2014 is attributed to an increase in the allocation of IT expenses to Harborview as a result of increase in salaries and wages at UW Medicine ITS.

In 2014 Harborview's allocation of IT operating expenses was recorded as purchased services as a result of adopting a purchased service model for IT expenditures. Additionally, the increase in purchased services in 2014 was driven by major IT projects, such as the implementation of EpicCare, a specialty clinics medical record and computerized physician order entry (CPOE) system in late fiscal year 2014.

**Supplies and other** expense include medical and surgical supplies, pharmaceutical supplies, insurance, taxes, and other expenses. In total, these expenses increased \$34.9 million from \$173.6 million in fiscal year 2014 to \$208.5 million in fiscal year 2015 and increased \$11.3 million from \$162.3 million in fiscal year 2013 to \$173.6 million in fiscal year 2014. In 2014, Harborview began dispensing a new and specialized pharmaceutical drug for the treatment of hepatitis C in their outpatient pharmacy which accounts for the majority of the increase in supplies expense for both fiscal year 2015 and 2014.

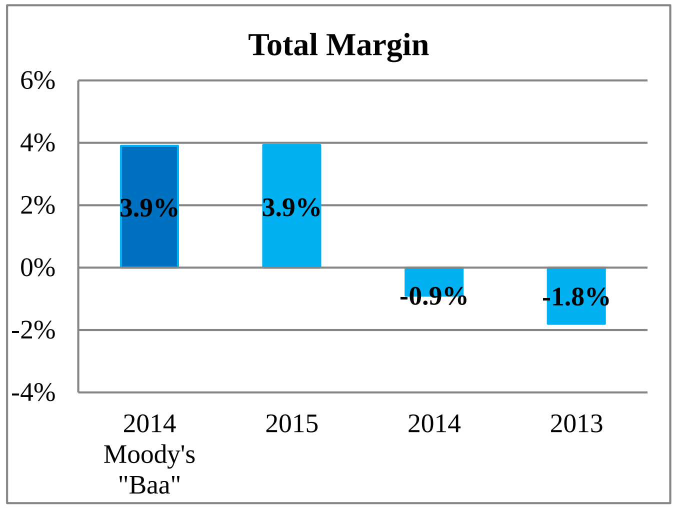
**Depreciation expense** decreased \$3.1 million from \$43.0 million in fiscal year 2014 to \$39.9 million in fiscal year 2015 and increased \$3.2 million from \$46.2 million in fiscal year 2013 to \$43.0 million in fiscal year 2014. The decrease in 2015 and 2014 was primarily due to reduced capital spending and new IT assets not being recorded on Harborview's statement of net position.

**Nonoperating Revenues (Expenses)**

Nonoperating revenues (expenses) consist primarily of investment income, interest expense, intergovernmental transfer expense, and strategic funding to UW Medicine entities. Net nonoperating expenses increased \$18.3 million between fiscal years 2015 and 2014 and decreased \$0.5 million between fiscal years 2014 and 2013. In 2015, the increase in net nonoperating expenses is primarily due to intergovernmental transfers related to Harborview's participation in Washington State Provider Access Payment (PAP) program and an increased strategic funding to affiliates. In 2014, the increase in net nonoperating expenses was attributed to lower realized gains on investments compared to the prior year.

***Total Margin***

Total margin or excess margin is a ratio that defines the percentage of total revenue that has been realized in the form of net income (loss) and is a common measure of total hospital profitability. Total margin for the fiscal years 2015, 2014, and 2013 compared to industry median is illustrated in the chart to the right.




## Financial Analysis

***Net Position***

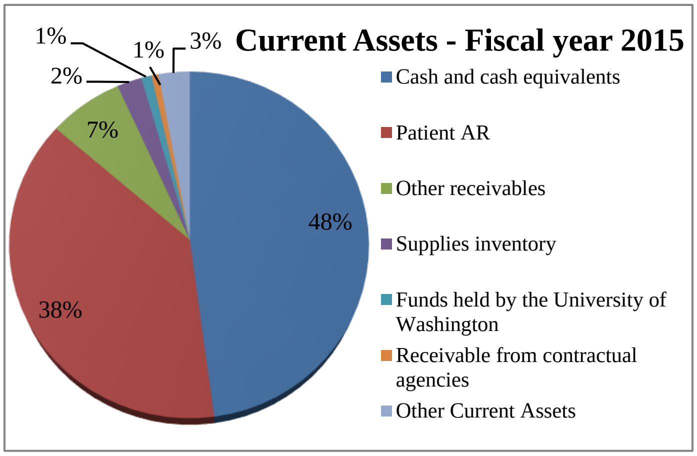
The table below is a presentation of certain condensed financial information derived from Harborview's net position as of the fiscal years ended June 30, 2015, 2014 and 2013:

| | | 2015 | 2014 | 2013 |
|---|---|---|---|---|
| | | | (In thousands) | |
| Current assets | $ | 376,705 | 285,596 | 262,945 |
| Noncurrent assets: | | | | |
| Capital assets, net | | 307,259 | 331,359 | 354,841 |
| Funds held by the University of Washington | | 600 | 600 | 600 |
| Assets whose use is limited | | 121,677 | 113,103 | 113,880 |
| Other assets | | 14,025 | 10,865 | — |
| Total assets | | 820,266 | 741,523 | 732,266 |
| Current liabilities | | 154,851 | 108,860 | 91,614 |
| Noncurrent liabilities | | 14,499 | 16,996 | 18,183 |
| Total liabilities | | 169,350 | 125,856 | 109,797 |
| Net position | $ | 650,916 | 615,667 | 622,469 |

Total assets were $820.3 million at June 30, 2015 compared to $741.5 million at June 30, 2014, an increase of $78.8 million. Significant events within total assets during fiscal year 2015 included an increase in cash and cash equivalents due to positive cash flows from operating activities.

Total assets were $741.5 million at June 30, 2014 compared to $732.3 million at June 30, 2013, an increase of $9.2 million. Significant events within total assets during fiscal year 2014 included an increase in cash and cash equivalents due to positive cash flows from operating activities.

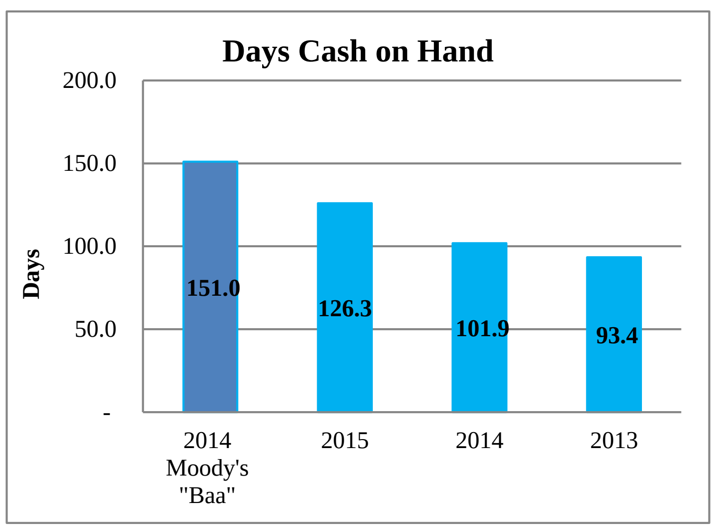
***Current Assets***




Current assets consist of cash and cash equivalents, patient accounts receivable, and other current assets that are expected to be converted to cash within a year. Total current assets were $376.7 million, $285.6 million, and $262.9 million at fiscal year-ends 2015, 2014, 2013, respectively. Fiscal year 2015 composition of current assets is illustrated in the chart to the left.

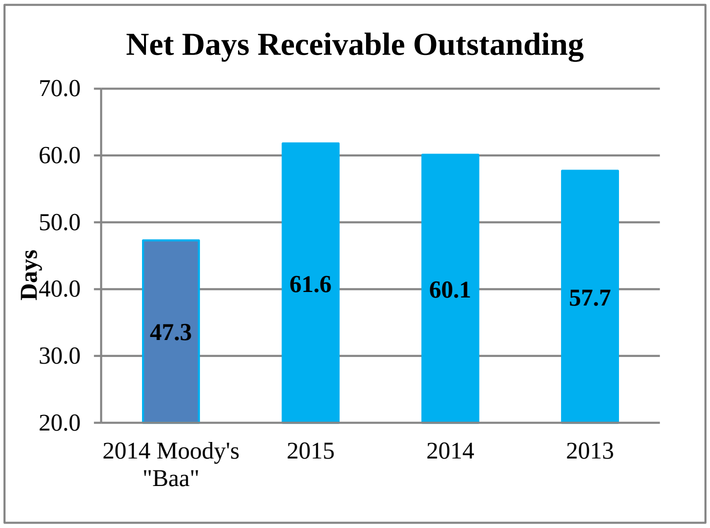
**Cash and cash equivalents** represent amounts invested in the King County Investment Pool (the KCIP) on behalf of Harborview. All amounts invested in the KCIP are available upon demand and, as such, are considered cash equivalents. Harborview's investment in the KCIP is split between cash and cash equivalents and assets whose use is limited in the statements of net position. Cash and cash equivalents increased $54.8 million in 2015 from $125.7 million at June 30, 2014 to $180.5 million at June 30, 2015 and increased $21.3 million in 2014 from $104.4 million at June 30, 2013 to $125.7 million at June 30, 2014.

Days cash on hand is utilized to evaluate an organization's continuing ability to meet its short-term operating needs. Days cash on hand, including board-designated assets whose use is limited, as of June 30, 2015, 2014, and 2013 are illustrated in the graph to the right.




Harborview's total days cash on hand, including board-designated assets whose use is limited, increased 24.4 days from 101.9 days at June 30, 2014 to 126.3 days at June 30, 2015 and increased 8.5 days from 93.4 days at June 30, 2013 to 101.9 days at June 30, 2014. The increase in 2015 was driven by Medicaid expansion and positive cash flow from operating activities. In addition, days cash on hand increase due to the receipt of CPE funds that will be settled and paid to the State in subsequent years.

**Net patient accounts receivable** was \$144.9 million as of June 30, 2015, compared to \$123.2 million at June 30, 2014. Net patient accounts receivable increased \$21.7 million and \$8.7 million during fiscal year 2015 and 2014, respectively. Harborview experienced a high revenue month for June 2015 which accounts for the increase in net patient accounts receivable. The increase in 2014 was due to the expansion of the Washington State Medicaid program, which resulted in an increase in Medicaid eligible patients and a decrease in self-pay patients.




Days receivable outstanding illustrates an organization's ability to convert net patient service revenue to cash. Days receivable outstanding as of June 30, 2015, 2014, and 2013 are provided in the graph included to the left.

Harborview's net days receivable outstanding increased 1.5 days from 60.1 days at June 30, 2014 to 61.6 days at June 30, 2015 and increased 2.4 days from 57.7 days at June 30, 2013 to 60.1 days at June 30, 2014. The increase in net days receivable outstanding during fiscal year 2015 is driven in part by the reduction of charity write-offs and the shift to managed care Medicaid payer plans, which has historically paid slower. The increase in fiscal year 2014 was driven by increased reimbursement time for Medicaid expansion claims and the Hospital Safety Net program funding being presented as other operating revenue in the form of grant revenue rather than net patient service as it has historically been presented.

As of June 30, 2015 and 2014, 39% of the gross patient accounts receivable balance is due from commercial payers, 56% and 55% is due from governmental payers Medicare and Medicaid, 3% and 5% is due from self-pay patients, and 2% and 1% from the Washington Health Benefit Exchange, respectively. On January 1, 2014, the Washington state Medicaid program was expanded to significantly increase the number of eligible Medicaid enrollees receiving benefits. Due to this expansion, Harborview has seen an increase in Medicaid gross patient accounts receivable and a decrease in self-pay gross accounts receivable at June 30, 2015, when compared to the previous fiscal year.

**Receivable from contractual agencies** consist of estimated receivables for cost report settlements. Receivable from contractual agencies decreased \$0.2 million from \$2.6 million as of June 30, 2014 to \$2.4 million as of June 30, 2015 as a result of a decrease in Medicare and Medicaid CPE report settlements and development in open Medicare cost report and CPE hold harmless estimates. During fiscal year 2014, receivables from contractual agencies decreased \$7.3 million as a result of decreases in Medicare and Medicaid CPE report settlements and development.

**Other current assets** include prepaid expenses and interest receivable. The increase in other current assets of \$4.0 million and \$5.6 million as of June 30, 2015 and 2014 relates to Harborview's current portion of prepaid IT expenses. The remaining balance of other current assets remained unchanged from the prior year.

### *Noncurrent Assets*

**Capital assets** net of accumulated depreciation, decreased $24.1 million during fiscal year 2015 from $331.4 million at June 30, 2014 to $307.3 million at June 30, 2015 and decreased $23.4 million during fiscal year 2014 from $354.8 million at June 30, 2013 to $331.4 million at June 30, 2014. The decrease in both years is primarily due to continued depreciation of depreciable assets offset by moderate capital spending.

Additional discussion regarding capital asset activity during the fiscal years can be found in the notes to the financial statements.

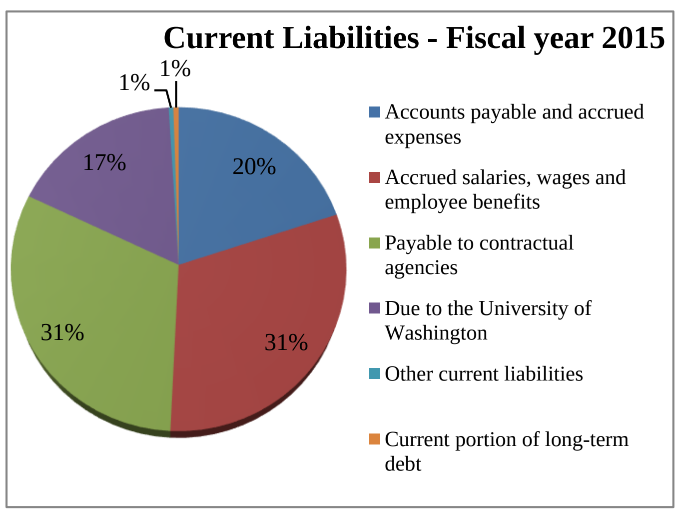
**Assets whose use is limited** (AWUL) includes board-designated, restricted investments and property held for future development. These investments include cash, long-term investments, and property held for future use. Board-designated cash and investments are used by Harborview to fund strategic initiatives, capital improvements, and to purchase equipment.

At June 30, 2015, total assets whose use is limited were $121.7 million, compared to $113.1 million at June 30, 2014, an increase of $8.6 million between years. The increase in assets in 2015 whose use is limited is a result of reduced capital expenditures and an increase in the funds set aside for the CPE hold harmless repayment to the State. Assets whose use is limited decreased $7.8 million during fiscal year 2013 due to funding of strategic initiatives and capital improvements.

**Other assets** consist of long-term prepaid expenses. Beginning in July 2013, UW Medicine ITS (a department of the UW) began recording enterprise-wide information technology (IT) capital assets that are purchased for use by UW Medicine entities. Previously, IT capital assets were recorded by Harborview. The long-term prepaid expense reflected in other assets of $14.0 million and $10.9 million at June 30, 2015 and 2014, respectively, entitles Harborview access to the enterprise-wide IT software and services.

### *Current Liabilities*

Current liabilities consist of accounts payable and other accrued liabilities that are expected to be paid within a year. Total current liabilities were $154.9 million at June 30, 2015, compared to $108.9 million at June 30, 2014. Fiscal year 2015 composition of current liabilities is illustrated in the chart to the right.



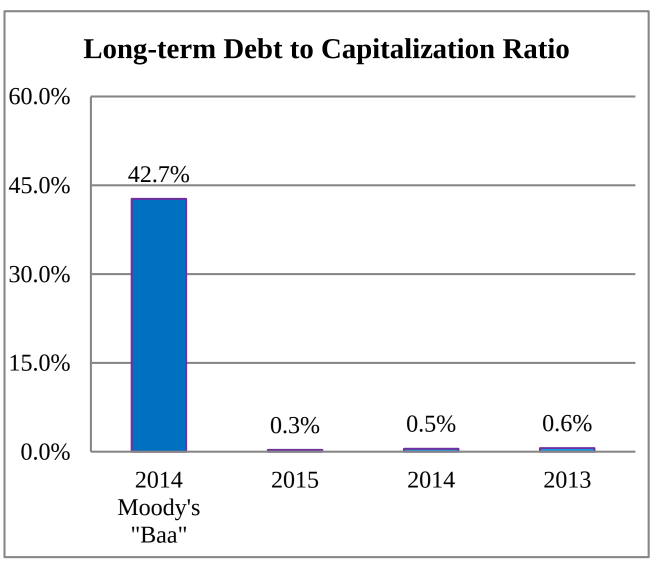

**Accounts payable and accrued expenses** increased $11.1 million from $19.8 million at June 30, 2014 to $30.9 million at June 30, 2015 and increased $1.8 million from $18.0 million at June 30, 2013 to $19.8 million at June 30, 2014. Changes in accounts payable and accrued expenses are primarily driven by timing of payments to vendors and employees.

**Accrued salaries, wages, and employee benefits** increased $5.6 million from $42.2 million at June 30, 2014 to $47.8 million at June 30, 2015 and increased $2.5 million from $44.7 million at June 30, 2013 to $42.2 million at June 30, 2014. Changes in accrued salaries, wages, and employee benefits are primarily driven by the number of employees, employee merit increases, and yearly estimate of the sick and vacation accrual.

**Payable to contractual agencies** consists of estimated reserves for Medicare cost report and Medicaid CPE settlements and amounts due as intergovernmental transfers to the Washington State Department of Social and Health Services. Payable to contractual agencies increased $22.1 million from $26.4 million at June 30, 2014 to $48.5 million at June 30, 2015 and increased $5.4 million from $21.0 million at June 30, 2013 to $26.4 million at June 30, 2014. The increase in fiscal year 2015 was driven by the development in open Medicare cost reports and Medicaid CPE hold harmless estimates. The decrease in fiscal year 2014 was driven by changes in Harborview's reserve methodology, settlement of Medicare and Medicaid CPE reports, and development in open Medicare cost report and CPE hold harmless estimates.

**Payable to the University of Washington (the University)** consists of amounts due for services provided to Harborview through the University for UW Medicine administrative and information technology support, as well as strategic funding to affiliates. Amounts due to the University increased $7.3 million from $19.0 million at June 30, 2014 to $26.3 million at June 30, 2015 and increased $12.5 million from $6.5 million at June 30, 2013 to $19.0 million at June 30, 2014. The increase in 2015 was a result of timing in settlement between Harborview and the University and Northwest Hospital. The increase in 2014 was driven by timing of invoices to the School of Medicine and to UW Medicine ITS for invoices related to operating expenses of the IT department.

***Noncurrent Liabilities***




Noncurrent liabilities consist of long-term debt and unearned rent.

**Long-term debt** as of June 30, 2015, 2014, and 2013 consists of bonds issued by King County.

Long-term debt to capitalization is a ratio used to evaluate capital structure of healthcare organizations. The graph to the left shows the long-term debt to capitalization ratio as of June 30 for 2015, 2014, and 2013 including a comparison to the stand-alone hospital median.

Historically, Harborview's significant construction projects have been funded through tax payer supported debt. As a policy, King County carries all tax payer supported debt and proceeds of debt are funded to Harborview through a voluntary nonexchange transaction. Debt carried by Harborview represents debt issued and supported through Harborview revenues. As a result of these policies, Harborview tends to report a significantly lower debt to capitalization ratio than other academic medical centers.

Additional discussion regarding long-term debt activity during the fiscal years can be found in the notes to the financial statements.

## Factors Affecting the Future

### *Strategic Collaborations*

In 2015, UW Medicine, Skagit Regional Health and Cascade Valley Hospital and Clinics entered into a Clinical Affiliation Agreement intended to create a long term and durable affiliation to integrate clinical programs to achieve the "Triple Aim" of better care for individuals, better health for populations, and lower per capita costs.

In March 2014, UW Medicine and Capital Medical Center (Olympia, WA) signed an agreement selecting UW Medicine as the healthcare system of choice for complex tertiary and quaternary care for Capital Medical Center patients. This strategic collaboration, effective April 1, 2014 will provide Capital Medical Center patients prompt access to the highest level of care for advanced services while allowing the organizations to work together to continue improving the quality, safety, and cost-effectiveness of care in the South Sound.

### *UW Medicine Accountable Care Network*

In 2014, UW Medicine formed an Accountable Care Network (ACN) with other selected healthcare organizations and healthcare professionals in Western Washington to form a care delivery network to assume responsibility for the healthcare of contracted populations of patients to achieve the Triple Aim: improved healthcare experience for the individual, improved health of the population, and more affordable care.

The ACN has contracted with the Washington Health Care Authority (HCA) to participate in its new Puget Sound Accountable Care Program (ACP) for Public Employees Benefits Board (PEBB) members. The ACP will initially be offered to all PEBB members who reside in Snohomish, King, Kitsap, Pierce, and Thurston Counties, with possible statewide expansion in 2017. This new option will be available to PEBB members with coverage beginning January 1, 2016.

A subset of the network members have also agreed to participate with the ACN in a contract with Premera as part of its new Accountable Health System (AHS) product. As an AHS, the UW Medicine ACN will share in accountability for the quality and cost of healthcare for Premera members who select this plan. This product will be sold both on and off the Washington Health Exchange in select counties with coverage beginning on January 1, 2016.

The UW Medicine ACN also entered into an agreement to provide health care services to non-union employees of a large local employer with coverage that began January 1, 2015.

These arrangements provide an opportunity for shared savings between the ACN and the contracted entity based on achieving quality and financial benchmarks. If certain financial benchmarks are not attained, UW Medicine, along with its network members, are at risk for reductions in payment levels from the contracted entity based on the agreement.

### *Employee Costs*

Rising benefit costs, particularly for pensions and healthcare, continue to impact the University and Harborview. Employer pension funding rates for the Public Employees' Retirement System (PERS) pension plans were unchanged during fiscal year 2015, but will be increasing 19% to 11.0% of covered salary during fiscal year 2016. Likewise, although the monthly employer base rate paid by the University and Harborview for employee healthcare expenses decreased during fiscal year 2015, it will increase 27% to $840 per active employee during fiscal year 2016. Both rates are likely to continue increasing over the next few years.

### *Regulatory and Legislative Changes*

The following regulatory, legislative, and accounting activity will impact all entities in UW Medicine during fiscal year 2016 and beyond:

- ***International Classification of Diseases (ICD) v10*** – Code of Federal Regulations (45 CFR Part 162) requires healthcare providers to implement ICD-10 no later than October 1, 2015. ICD-10 represents a significant change in the standard healthcare coding system that will impact every system, process, and transaction that contains or uses a diagnosis code or inpatient procedure code. The implementation of ICD-10 will impact both healthcare providers and healthcare payers.

  UW Medicine has been undertaking activities related to the implementation of ICD-10 since the beginning of fiscal year 2012.

- ***Medicaid Expansion*** – On January 1, 2014, the Washington state Medicaid program was expanded to significantly increase the number of Medicaid enrollees receiving benefits. Due to the increased access to Medicaid coverage, Harborview has experienced a reduction in uninsured and underinsured patients and an increase in patients who qualify for Medicaid. The reduction of uninsured and underinsured patients is expected to have an impact on Medicare and Medicaid Disproportionate Share (DSH) reimbursement methodologies in the future. Harborview has experienced a change to their payer mix, which is anticipated to continue in 2016.

- ***Pay for Performance*** – The Affordable Care Act mandated programs that affect reimbursement through evaluation of the quality of care and cost of care provided to patients at the federal level, however, there are an increasing number of programs arising from state and private interests. These programs provide incentives (and/or penalties) for reporting performance data and on benchmarking performance against other providers regionally and nationally. The pay for performance programs will continue into the future and UW Medicine is examining performance to attain incentive dollars.

- ***Management Services Agreement*** – Harborview is managed and operated by the University of Washington (the University) under a management services agreement between the Board of Trustees (the Trustees) and the Board of Regents of the University. The agreement was set to expire on June 30, 2015, and to facilitate ongoing negotiations of a new agreement, the parties extended the agreement to the earlier of December 31, 2015 or the date that a new agreement is effective.

**HARBORVIEW MEDICAL CENTER**
(A Component Unit of King County)
(Operated by the University of Washington)

Statements of Net Position

June 30, 2015 and 2014

(Dollar amounts in thousands)

| **Assets** | | **2015** | **2014** |
|---|---|---|---|
| Current assets: | | | |
| Cash and cash equivalents | $ | 180,469 | 125,666 |
| Funds held by the University of Washington | | 3,577 | 2,177 |
| Patient accounts receivable, less allowance for uncollectible accounts of $30,777 in 2015 and $28,608 in 2014 | | 144,875 | 123,160 |
| Other receivables | | 25,957 | 16,669 |
| Supplies inventory | | 8,604 | 8,568 |
| Receivable from contractual agencies | | 2,430 | 2,591 |
| Other current assets | | 10,793 | 6,765 |
| Total current assets | | 376,705 | 285,596 |
| Noncurrent assets: | | | |
| Capital assets, net of accumulated depreciation | | 307,259 | 331,359 |
| Fund held by the University of Washington | | 600 | 600 |
| Assets whose use is limited | | 121,677 | 113,103 |
| Other assets | | 14,025 | 10,865 |
| Total noncurrent assets | | 443,561 | 455,927 |
| Total assets | $ | 820,266 | 741,523 |
| **Liabilities and Net Position** | | | |
| Current liabilities: | | | |
| Accounts payable and accrued expenses | $ | 30,857 | 19,829 |
| Accrued salaries, wages, and employee benefits | | 47,754 | 42,206 |
| Payable to the University of Washington | | 26,277 | 19,014 |
| Payable to contractual agencies | | 48,454 | 26,352 |
| Other current liabilities | | 704 | 704 |
| Current portion of long-term debt | | 805 | 755 |
| Total current liabilities | | 154,851 | 108,860 |
| Noncurrent liabilities: | | | |
| Unearned rent and other | | 13,698 | 14,669 |
| Long-term debt, net of current portion | | 801 | 2,327 |
| Total liabilities | | 169,350 | 125,856 |
| Net position: | | | |
| Net investment in capital assets | | 305,653 | 328,277 |
| Expendable, restricted | | 9,983 | 16,618 |
| Nonexpendable, restricted | | 2,527 | 3,709 |
| Unrestricted | | 332,753 | 267,063 |
| Total net position | | 650,916 | 615,667 |
| Total liabilities and net position | $ | 820,266 | 741,523 |

See accompanying notes to basic financial statements.

**HARBORVIEW MEDICAL CENTER**
(A Component Unit of King County)
(Operated by the University of Washington)

Statements of Revenues, Expenses, and Changes in Net Position

Years ended June 30, 2015 and 2014

(Dollar amounts in thousands)

| | | 2015 | 2014 |
|---|---|---|---|
| Operating revenues: | | | |
| Net patient service revenues (net of provision for uncollectible accounts of $26,741 in 2015 and $37,580 in 2014) | $ | 858,845 | 747,884 |
| State appropriation | | 6,171 | 6,125 |
| Other operating revenues | | 64,873 | 60,643 |
| Total operating revenues | | 929,889 | 814,652 |
| Operating expenses: | | | |
| Salaries and wages | | 343,507 | 327,085 |
| Employee benefits | | 101,072 | 103,156 |
| Purchased services | | 175,669 | 168,594 |
| Supplies and other expenses | | 208,523 | 173,644 |
| Depreciation | | 39,926 | 42,957 |
| Total operating expenses | | 868,697 | 815,436 |
| Income (loss) from operations | | 61,192 | (784) |
| Nonoperating revenues (expenses): | | | |
| Investment income, net | | 1,649 | 1,309 |
| Interest expense | | (212) | (161) |
| Donations | | 979 | 1,090 |
| Funding to affiliates | | (26,473) | (8,651) |
| Unrealized gain on investments, net | | 174 | 1,361 |
| Other, net | | (803) | (1,294) |
| Nonoperating expenses | | (24,686) | (6,346) |
| Income (loss) before capital contributions, additions to permanent endowments, and other | | 36,506 | (7,130) |
| Capital contributions, additions to permanent endowments, and other: | | | |
| Capital contributions and other | | (1,257) | 157 |
| Additions to permanent endowments | | — | 171 |
| Total capital contributions, additions to permanent endowments, and other | | (1,257) | 328 |
| Increase (decrease) in net position | | 35,249 | (6,802) |
| Net position – beginning of year | | 615,667 | 622,469 |
| Net position – end of year | $ | 650,916 | 615,667 |

See accompanying notes to basic financial statements.

**HARBORVIEW MEDICAL CENTER**
(A Component Unit of King County)
(Operated by the University of Washington)

Statements of Cash Flows

Years ended June 30, 2015 and 2014

(Dollar amounts in thousands)

| | | 2015 | 2014 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Cash received for patient service revenues and other | $ | 859,394 | 751,846 |
| Cash received for other services | | 60,320 | 72,364 |
| Cash paid to employees | | (439,031) | (432,764) |
| Cash paid to suppliers and others | | (382,983) | (343,379) |
| Net cash provided by operating activities | | 97,700 | 48,067 |
| Cash flows from noncapital financing activities: | | | |
| Donations and other income received | | 979 | 1,090 |
| Funding to affiliates | | (18,313) | (8,651) |
| Additions to permanent endowments | | — | 171 |
| Other | | (798) | (1,191) |
| Net cash used in noncapital financing activities | | (18,132) | (8,581) |
| Cash flows from capital and related financing activities: | | | |
| Principal payments on long-term debt | | (1,460) | (705) |
| Cash paid for interest | | (215) | (164) |
| Capital expenditures | | (15,082) | (20,912) |
| Capital contributions | | — | 158 |
| Net cash used in capital and related financing activities | | (16,757) | (21,623) |
| Cash flows from investing activities: | | | |
| Net (increase) decrease in assets whose use is limited | | (9,657) | 2,138 |
| Investment income, net | | 1,649 | 1,309 |
| Net cash (used in) provided by investing activities | | (8,008) | 3,447 |
| Increase in cash and cash equivalents | | 54,803 | 21,310 |
| Cash and cash equivalents, beginning of year | | 125,666 | 104,356 |
| Cash and cash equivalents, end of year | $ | 180,469 | 125,666 |
| Reconciliation of income (loss) from operations to net cash provided by operating activities: | | | |
| Income (loss) from operations | $ | 61,192 | (784) |
| Adjustments to reconcile income (loss) from operations to net cash provided by operating activities: | | | |
| Depreciation | | 39,926 | 42,957 |
| Provision for uncollectible accounts | | 26,741 | 37,580 |
| Net increase in current and other assets | | (66,207) | (49,786) |
| Net increase in current liabilities, except current portion of long-term debt | | 37,019 | 18,517 |
| Decrease in unearned revenue and unearned rent | | (971) | (417) |
| Net cash provided by operating activities | $ | 97,700 | 48,067 |
| Supplemental disclosures of cash flow information: | | | |
| Increase (decrease) in accounts payable for capital assets | $ | 762 | (1,321) |
| Donation gift in kind | | 245 | 289 |
| (Loss) gain on disposal of capital assets | | (18) | 116 |

See accompanying notes to basic financial statements.

## (1) Organization

Harborview Medical Center (Harborview) is a 413 licensed bed hospital operating in Seattle, Washington with extensive ambulatory services and is a discretely presented component unit of King County (the County). Harborview is managed by the University of Washington (the University) under a management contract between the Board of Trustees (the Trustees) and the Board of Regents of the University in accordance with policies established by the Trustees as provided for in the management contract. The first management contract originated on July 1, 1967, and has been revised and extended several times. The agreement was set to expire on June 30, 2015, and to facilitate ongoing negotiations of a new agreement, the parties extended the agreement to the earlier of December 31, 2015 or the date the new agreement is effective. The management contract recognizes the Trustees' desire to maintain Harborview as a means of meeting the County government's intent to provide the community with a resource for health services and the University's desire that Harborview be maintained as a continuing resource for education, training, and research. The Trustees during fiscal year 2015 were:



The general conditions within the management contract specify that the County will retain title to all real and personal properties acquired for the County with Medical Center capital or operating funds. However, Harborview retains the rights of ownership to these real and personal properties and records these assets on its books. The Trustees determine major institutional policies and retain control of programs and fiscal matters. The County retains ultimate control over capital programs and capital budgets for buildings and renovations. The Trustees agree to secure the University's recommendations on any changes to the above. The Trustees are accountable to the public and the County government for all financial aspects of Harborview's operation and agree to maintain a fiscal policy that keeps the essential operating program and expenditures within the limits of the operating income. In maintaining a balanced budget fiscal policy, the Trustees agree to adopt standards of patient care developed in cooperation with the University. The University provides for the rendering of medical, dental, and other professional services in Harborview and professional and hospital services by the University personnel and overall management services. A special account is maintained with the University to receive reimbursement payments from Harborview's operating account and to pay for the costs of all services and expenditures provided by the University.

The Trustees and the University establish and maintain operational standards for all teaching and patient care designed to meet the requirements of such approval agencies as The Joint Commission. The Trustees control the use of all physical facilities and establish overall space use policies and guidelines in support of Harborview's programs. The University manages Harborview so as to retain its institutional identity in a manner which, to the extent of the funds available to Harborview, will achieve the aims of the Trustees to meet their community obligation and provide services to address the community's needs, as identified in


(Continued)

Harborview's mission statement. Additionally, the management contract requires the University "to provide hospital services, including management under the direction of a hospital administrator for the hospital, to provide for the rendering of medical services in connection with the hospital and to provide for the conduct of teaching and research activities by the University in connection with the hospital."

Harborview is a discretely presented component unit of King County and part of UW Medicine through the management contract that includes: UW Medical Center, Northwest Hospital & Medical Center (Northwest Hospital), Valley Medical Center (VMC), UW Physicians Network dba UW Neighborhood Clinics (UWNC), UW Physicians (UWP), the UW School of Medicine (the School) and Airlift Northwest (Airlift).

## (2) Summary of Significant Accounting Policies

### *(a) Accounting Standards*

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in the United States of America using the accrual basis of accounting. Harborview's financial statements and note disclosures are based on all applicable Government Accounting Standards Board (GASB) pronouncements and interpretations. Harborview uses proprietary fund accounting.

### *(b) Basis of Accounting*

Harborview's financial statements have been prepared using the accrual basis of accounting with the economic resources measurement focus. Under this method of accounting, revenues are recognized when earned and expenses are recorded when liabilities are incurred without regard to receipt or disbursement of cash.

### *(c) Use of Estimates*

The preparation of financial statements, in conformity with U.S. generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates in Harborview's financial statements include patient accounts receivable allowances, receivable from contractual agencies, payable to contractual agencies, and the fair value of investments.

### *(d) Cash and Cash Equivalents*

Cash and cash equivalents primarily comprise investments held in an external investment pool managed for Harborview by the County. These investments consist of pooled investment funds of money markets, U.S. agency securities, U.S. agency mortgage-backed securities, U.S. treasury securities, U.S. municipal securities, collateralized mortgaged obligations, and repurchase agreements and are carried at fair value.

The King County Investment Pool is not registered with the Securities and Exchange Commission (SEC) as an investment company. Oversight is provided by the King County Executive Finance Committee (EFC). All investments are subject to written policies and procedures adopted by the EFC. The EFC reviews pool performance monthly.

The King County Investment Pool allocates participants' shares using an amortized cost basis. Monthly income is distributed to participants based on their relative participation during the period. Income is calculated based on: (1) realized investment gains and losses; (2) interest income based on stated rates (both paid and accrued); and (3) the amortization of discounts and premiums on a straight-line basis. Income is reduced by the contractually agreed upon investment fee.

Harborview has unrestricted access to these investments at its discretion and without limitation, and as such, these investments are considered cash equivalents. Harborview has cash equivalents of $180.5 million and $125.7 million as of June 30, 2015 and 2014, respectively.

### *(e) Assets Whose Use is Limited*

Assets whose use is limited include designated unrestricted assets set aside by the Trustees for future capital and program purposes over which the Trustees retain control and may at their own discretion subsequently use for other purposes; investments restricted for use by creditors, grantors, or contributors external to Harborview; and investments restricted for capital purchases representing unspent bond proceeds, required capital funding by Harborview, and interest earnings thereon by the County. Investments are held in the King County Investment Pool, managed for Harborview by the County, and are carried at fair market value.

Disclosure requirements related to investment risk, credit risk, interest rate risk, foreign currency risk, and deposit risk are applicable to the primary government which, as it relates to Harborview, is the County.

### *(f) Inventories*

Inventories consist primarily of surgical, medical, and pharmaceutical supplies in organized stores at various locations across the Harborview. Inventories are recorded at the lower of cost (first-in, first-out (FIFO) or market.

### *(g) Capital Assets*

Capital assets, defined as purchases with a per item cost of $2,000 or greater and a useful life of at least two years, are stated at cost at acquisition or if acquired by gift, at fair market value at the date of the gift. Additions, replacements, major repairs, and renovations are capitalized. Maintenance and repairs are expensed. The cost of the capital assets sold or retired and the related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recorded.


(Continued)

The provision for depreciation is determined by the straight-line method, which allocates the cost of tangible property ratably over its estimated useful life. The estimated useful lives used by Harborview are as follows:

| | |
|---|---|
| Land improvements | 25 years |
| Buildings, renovations, and furnishings | 5–50 years |
| Fixed equipment | 5–25 years |
| Movable equipment | 3–20 years |
| Leasehold improvements | The shorter of the lease term or useful life |

Interest is capitalized on construction projects as a cost of the related project beginning with commencement of construction and ceases when the construction period ends and the related asset is placed in service. No interest was capitalized during 2015 and 2014.

For the year ended June 30, 2015, supplies and other expense includes approximately $9.2 million for the write-off of certain capital assets and restricted investments for which management determined carrying amounts were not recoverable.

***(h) Other Assets***

UW Medicine ITS (a department of the University) records enterprise-wide information technology (IT) capital assets that are purchased for use by UW Medicine entities. Previously, these capital assets were recorded at Harborview and UW Medical Center. Harborview provides advance funding to UW Medicine ITS which entitles Harborview access to the enterprise-wide IT software and services. The prepaid portion of this funding is reported within other current assets and other assets in the statements of net position. At June 30, 2015 and 2014, $8.6 million and $5.5 million, respectively, is recorded in other current assets and $14.0 and $10.9 million is recorded in other assets, respectively.

***(i) Compensated Absences***

University employees deployed at Harborview earn annual leave at rates based on length of service and sick leave at the rate of one day per month. Annual leave balances, which are limited to 240 hours, can be converted to monetary compensation upon employment termination. Sick leave balances, which are unlimited, can be converted to monetary compensation annually at 25% of the employees’ normal compensation rate for any balance that exceeds 480 hours or for any balance upon retirement or death. Harborview recognizes annual and sick leave liabilities when earned.

Annual leave accrued at June 30, 2015 and 2014 is $23.8 million and $21.6 million, respectively. Sick leave accrued as of June 30, 2015 and 2014 is $4.6 million and $1.5 million, respectively. Compensated absences are reported within the accrued salaries, wages, and employee benefits in the statements of net position.

### *(j) Receivable from/Payable to Contractual Agencies*

Harborview is reimbursed for Medicare inpatient, outpatient, psychiatric, and rehabilitation services, and for capital and medical education costs during the year either prospectively or at an interim rate. The difference between interim payments and the reimbursement computed based on the Medicare filed cost report results in an estimated receivable from or payable to Medicare at the end of each year. The Medicare program's administrative procedures preclude final determination of amounts receivable from or payable to Harborview until after the cost reports have been audited or otherwise reviewed and settled by Medicare.

Public hospitals located in the state of Washington designated by the Washington State legislature are reimbursed at the "full cost" of Medicaid inpatient covered services under the public hospital CPE payment method. See note 3(a) for discussion regarding this program.

The estimated settlement amounts for Medicare cost report and CPE payments that are not considered final are included in receivable from/payable to contractual agencies in the accompanying statements of net position.

### *(k) Classification of Revenues and Expenses*

Harborview's statements of revenues, expenses, and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues, such as patient service revenue, result from exchange transactions associated with providing healthcare services – Harborview's primary business. Exchange transactions are those in which each party to the transaction receives and gives up essentially equal values.

Operating expenses are all expenses, other than financing costs, incurred by Harborview to provide healthcare services to patients.

Nonoperating revenues and expenses are recorded for certain exchange and nonexchange transactions. This activity includes investment income, interest expense, intergovernmental transfer expense, and strategic funding to affiliates of UW Medicine.

### *(l) Net Patient Service Revenues*

Harborview has agreements with third-party payers that provide for payments to Harborview at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers.

Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. A summary of the payment arrangements with major third-party payers is as follows:

**Medicare**

Acute inpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge based on Medicare severity diagnosis-related groupings (MS-DRGs), as well as reimbursements related to capital costs. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Payments for Medicare outpatient services are provided based upon a prospective payment system known as ambulatory payment classifications (APC). APC payments are prospectively established and may be greater than or less than the primary government's actual charges for its services. The Medicare program utilizes the prospective payment system known as case mix group (CMG) for rehabilitation services reimbursement. As with MS-DRGs, CMG payments are prospectively established and may be greater than or less than Harborview's actual charges for its services. Psychiatric services are also paid prospectively using a federal per diem payment rate adjusted for comorbidity and various adjustment factors. Third-party settlements are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

**Medicaid**

Inpatient services rendered to Medicaid program beneficiaries are provided at prospectively determined rates per discharge. Outpatient services rendered are provided based upon the APC prospective payment system. See note 3(a) for discussion surrounding the Medicaid certified public expenditure program.

**Commercial**

Harborview also has entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to Harborview under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

**Exchange (HIX)**

Washington State health exchange (HIX) entered into agreements with certain commercial insurance plans to provide patients access to health care services. The basis for payment to Harborview under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

***(m) Accountable Care Network***

In 2014, UW Medicine entered into a risk contract with a large local employer and also formed an accountable care network (ACN) with certain other health care organizations and healthcare professionals to share financial and clinical responsibility for the healthcare of particular populations of patients. Harborview is a network member of the UW Medicine ACN and as such shares in risk contract surplus or deficits based on agreed upon contractual terms. Since its inception, the ACN has entered into various contracts which include provisions for shared risk as well as shared savings based on achieving certain quality and financial benchmarks. Harborview and the other network members share in the financial risk or savings. At June 30, 2015, Harborview has recorded a liability of $109,000 for its portion of the estimated liability related to these risk-sharing arrangements which is reflected in payable to the University of Washington in the accompanying statement of net position.

### *(n) Charity Care*

Harborview provides care without charge or at amounts less than established rates to patients who meet certain criteria under its charity care policy. Harborview maintains records to identify and monitor the level of charity care it provides. These records include charges foregone for services and supplies furnished under its charity care policy to the uninsured and the underinsured. Because Harborview does not pursue collection of amounts determined to qualify as charity care, these are not reported as net patient service revenue. The charges associated with charity care provided by the Hospital are approximately $60.0 million and $167.7 million, respectively, for the years ended June 30, 2015 and 2014.

Harborview estimates the cost of charity care using its Medicaid cost to charge ratio of 41.0% and 42.8% for the fiscal years ended June 30, 2015 and 2014, respectively. Applying Harborview's Medicaid cost to charge ratio of 41.0% to total charity of $60.0 million results in an estimated cost of charity care and uncompensated care of $24.6 million for the fiscal year ended June 30, 2015. Applying Harborview's Medicaid cost to charge ratio of 42.8% to total charity of $167.7 million results in an estimated cost of charity care and uncompensated care of $71.8 million for the fiscal year ended June 30, 2014.

### *(o) Federal Income Taxes*

Harborview, as a component of the State of Washington, is not subject to federal income taxes under Section 115 of the Internal Revenue Code, except for unrelated business income tax.

### *(p) Recently Adopted and New Accounting Pronouncements*

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions*, which is effective for the fiscal year beginning July 1, 2014. It requires governments providing defined benefit pensions to their employees to recognize the net pension liability for pension benefits on their statements of net position. Net position liability is measured as total pension liability, less the amount of the plan's fiduciary net position. Management evaluated the impact of this statement and determined that it is not applicable to Harborview as Harborview does not directly fund the employer contribution to the Department of Retirement System (DRS), which is funded by the University. Harborview is not part of the financial reporting entity of the University.

In February 2015, the GASB issued Statement No. 72 *Fair Value Measurement and Application*, which will be effective for the fiscal year ending June 30, 2016. This Statement provides guidance for determining a fair value measurement for financial reporting purposes. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. This Statement establishes a three level hierarchy of inputs to valuation techniques used to measure fair value and requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. Harborview is currently analyzing the impact of this statement.

In June 2015, the GASB issued Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Amendments to GASB Statement 68 will be effective for the fiscal year ending June 30, 2016 and the guidance for plans not within 68's scope will be effective for the fiscal year ending June 30, 2017. This Statement is intended to improve financial reporting of governments whose employees are provided with pensions that are not within the scope of Statement No. 68, improve the usefulness of information associated with governments that hold assets accumulated for purposes of providing defined benefit pensions not within the scope of Statement No. 68, and to clarify the application of certain provisions of Statements No. 67 and 68. Harborview is currently analyzing the impact of this statement.

In June 2015, the GASB issued Statement No. 74 *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which is effective for the fiscal year ending June 30, 2017. The objective of this Statement is to improve the usefulness of information about other postemployment benefits (OPEB) such as death benefits, life insurance, disability, and long-term care in financial reports of governments that provide them. This Statement replaces Statements No. 43, "Financial Reporting for Post-employment Benefit Plans Other Than Pension Plans, as amended." Harborview is currently analyzing the applicability of this statement.

In June 2015, the GASB issued Statement No. 75 *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which is effective for the fiscal year ending June 30, 2018. This Statement establishes standards of accounting and financial reporting for defined benefit OPEB and defined contribution OPEB that are provided to the employees of state and local governmental employers through OPEB plans that are administered through trusts or equivalent arrangements. This Statement also establishes standards of accounting and financial reporting for OPEB plans that are not administered through trusts or equivalent arrangements. Harborview is currently analyzing the impact of this statement.

In June 2015, the GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, which is effective for the fiscal year ending June 30, 2016. The objective of this Statement is to identify the hierarchy of generally accepted accounting principles (GAAP). This Statement reduces the GAAP hierarchy to two categories of authoritative GAAP and addresses the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. Harborview is currently analyzing the impact of this statement.

## (3) Net Patient Service Revenues

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. In 2015 and 2014, net patient service revenue includes approximately $7.8 million and $6.6 million of revenue, respectively, relating to prior years' net Medicare and Medicaid cost report settlements and revised estimates, including DSH reimbursement and the CPE Program.

The following are the components of net patient service revenues for the year ended June 30 (in thousands):

| | 2015 | 2014 |
|---|---|---|
| Gross patient service revenues | $ 2,099,327 | 1,916,945 |
| Less adjustments to patient service revenues: | | |
| Charity care | (59,964) | (167,681) |
| Contractual discounts | (1,153,777) | (963,800) |
| Provision for uncollectible accounts | (26,741) | (37,580) |
| Total adjustments to patient service revenues | (1,240,482) | (1,169,061) |
| Net patient service revenues | $ 858,845 | 747,884 |

Harborview grants credit without collateral to its patients, most of whom are local residents and insured under third-party payer agreements. The mix of gross patient charges and receivables from significant third-party payers for the years ended June 30, 2015 and 2014 is as follows:

| | Patient service charges | Accounts receivable |
|---|---|---|
| 2015: | | |
| Medicare | 30% | 25% |
| Medicaid | 33 | 31 |
| Commercial and other | 33 | 39 |
| Self-pay | 3 | 3 |
| Exchange (HIX) | 1 | 2 |
| Total | 100% | 100% |
| 2014: | | |
| Medicare | 29% | 25% |
| Medicaid | 30 | 30 |
| Commercial and other | 33 | 39 |
| Self-pay | 7 | 5 |
| Exchange (HIX) | 1 | 1 |
| Total | 100% | 100% |

***(a) Medicaid Certified Public Expenditure Reimbursement***

Public hospitals located in the state of Washington designated by the Washington State legislature are reimbursed at the “full cost” of Medicaid inpatient covered services under the public hospital CPE payment method.

“Full cost” payments are determined using the respective hospital’s Medicaid ratio of cost to charges to determine the cost for covered medically necessary services. The costs will be certified as actual expenditures by the hospital and the State claims federal match on the amount of the related certified public expenditures. Per the Centers for Medicare and Medicaid Services (CMS) approved Medicaid State Plan, participating hospitals receive only the federal match portion of the allowable costs. Harborview received $71.1 million and $76.0 million in claims payments under this program for the years ended June 30, 2015 and 2014, respectively.

In addition, Harborview receives the federal match portion of Disproportionate Share (DSH) payments, which are the lesser of qualifying uncompensated care cost or the hospital’s specific limit. Harborview received $40.9 million and $42.4 million in DSH funding under this program for the years ended June 30, 2015 and 2014, respectively.

Since the inception of the program, the Washington State Legislature (the State) has provided, through an annual budget proviso, a “hold harmless” provision for hospitals participating in the CPE program. Through this proviso, hospitals participating in the CPE program will receive no less in combined state and federal payments than they would have received under the previous payment methodology. In addition, the hold harmless provision ensures that participating hospitals receive DSH payments as specified in the legislation.

In the event of a shortfall between CPE program payments and the amount determined under the hold harmless provision, the difference is paid to the hospitals as a grant from state-only funds. Harborview received $13.5 million and $9.2 million in state grants for the years ended June 30, 2015 and 2014, respectively. Claims payments, DSH payments, and state grant funds are included in net patient service revenues in the statements of revenues, expenses, and changes in net position.

CPE payments are subject to retrospective determination of actual costs once Harborview's Medicare Cost Report is audited. CPE program payments are not considered final until retrospective cost reconciliation is complete, after Harborview receives its Medicare Notice of Program Reimbursements (NPR) for the corresponding cost reporting year. To date, the 2006 CPE program year has had a final settlement.

Interim state grant payments are retrospectively reconciled to "hold harmless" after actual claims are repriced using the applicable DRG payment methodology. This process takes place approximately 12 months after the end of the fiscal year and results in either a payable to, or receivable from, the state Medicaid Program.

Harborview has estimated the expected final settlement amounts based on the difference between CPE payments received and the estimated hold harmless amount. For the years ended June 30, 2015 and 2014, net patient service revenue includes approximately $(0.3) million and $4.5 million, respectively, of (decreases) increases relating to the prior year's estimate and settlements.

As of June 30, 2015, Harborview has an estimated payable of $42.1 million and an estimated receivable of $0.4 million for the CPE program, which are included in payable to contractual agencies and receivable from contractual agencies, respectively in the statements of net position. As of June 30, 2014, Harborview has an estimated payable of $26.4 million and an estimated receivable of $2.6 million for the CPE program, which are included in payable to contractual agencies and receivable from contractual agencies, respectively in the statements of net position.

***(b) Professional Services Supplemental Payment (PSSP) and Provider Access Payment (PAP) Program***

The professional services supplemental payment (PSSP) and provider access payment (PAP) program are programs managed by the Washington State Health Care Authority (WSHCA) benefiting certain public hospitals. CMS approved the PAP program in August 2014 for services on and after July 1, 2014.

Under the program, UW Medical Center, Harborview, VMC, UWP, and Children's University Medical Group (CUMG) receive supplemental Medicaid payments for the physician and other professional services for which they bill. These supplemental payments equal the difference between the standard Medicaid reimbursement and the upper payment limit allowable by federal law. UW Medical Center and Harborview provide the nonfederal share of the supplemental payments that are used to obtain the matching federal funds.

Harborview recorded $11.9 million and $4.2 million for the years ended June 30, 2015 and 2014, respectively, in intergovernmental transfers (IGT) to WSHCA related to professional claims paid in those fiscal years, which is included as a nonoperating expense in the statements of revenue, expenses, and changes in net position.

WSHCA uses the federal match funds to make professional services supplemental payments to UW Medicine entities for PSSP and through the Medicaid managed care plans for PAP. Harborview recognized $2.0 million and $0.2 million in supplemental payments for the years ended June 30, 2015 and 2014, respectively. These payments are included in net patient service revenues in the statements of revenue, expenses, and changes in net position.

There is no requirement that UWP and CUMG PSSP and PAP payments be returned to Harborview and UW Medical Center as a condition for making the IGT's. PSSP and PAP funds are combined with other revenues used by the School for the central support of faculty costs. Thus, the School requires less funding from Harborview and UW Medical Center. The faculty support is reduced by $20.7 million and $7.9 million in fiscal years 2015 and 2014, respectively. This reduction is included as an offset to purchased services in the statements of revenue, expenses, and changes in net position.

### *(c) Hospital Safety Net Program*

The Hospital Safety Net Assessment Act (HSNA) uses local funds obtained through an assessment levied on Prospective Payment System (PPS) hospitals and federal matching funds to increase Medicaid payments to hospitals. Under this program, PPS program hospitals are assessed a fee on all non-Medicare patient days. Under the original HSNA program, HSNA funds were used to prevent the significant budget cuts proposed during the 2009 session of the state legislature. The original legislation expired on June 30, 2013.

In its 2013 session, the Washington State legislature passed a new assessment program that was similar to the original program as they will use federal matching funds to increase Medicaid hospital payments. Under the new HSNA program, PPS hospitals receive supplemental Medicaid payments, Critical Access Hospitals receive disproportionate share payments, and CPE hospitals receive state grants. The safety net assessment was subject to approval by the Center for Medicare and Medicaid Services before it took effect. CMS approved this program in 2014. The program has an expiration date of June 30, 2017.

Harborview is exempt from the assessment as the hospital is operated by an agency of the state government and also participates in the CPE program.

Harborview recognized grant funding of $7.6 million and $7.6 million for the years ended June 30, 2015 and 2014, respectively, which is recorded in other operating revenue in the statements of revenues, expenses, and changes in net position.

### *(d) Meaningful Use Incentives*

The American Recovery and Reinvestment Act of 2009 (ARRA) established incentive payments to eligible professionals and hospitals participating in Medicare and Medicaid programs that adopt certified electronic health records but only if the technology is being used in a "meaningful" way that supports the ultimate goals of improving quality, safety, and efficiency of care. "Meaningful use" is defined with specific quality performance metrics for eligible healthcare professionals and hospitals and certain thresholds must be met and maintained to receive payment.

Harborview recognized meaningful use incentives of $6.0 million and $6.0 million for the years ended June 30, 2015 and 2014, respectively, which are included in other operating revenues in the statements of revenue, expenses, and changes in net position.

### *(e) Other Federal and State Funding*

As a regional trauma center, Harborview is eligible for additional State funding in both 2015 and 2014 through the Trauma Enhancement program. Participating hospitals receive a pro-rata share of the pool appropriated for this program based on their portion of total inpatient and outpatient Medicaid claims submitted. Harborview received $8.5 million and $5.8 million for the years ended June 30, 2015 and 2014. In addition to the funding received through the Trauma Enhancement program, Harborview received State sponsored trauma grants in the amount of $1.7 million and $1.9 million for the years ended June 30, 2015 and 2014, respectively. Funds from both programs are included in net patient service revenues in the statements of revenues, expenses, and changes in net position.

## (4) State Appropriation

An appropriation is made by the State to the University on a biennial basis. Harborview is designated as a division of the major program "hospitals" included within the total appropriation. This appropriation is specifically designated by the State for the training of future healthcare professionals and to upgrade the skills of current practitioners. Due to the nature of the designation, these amounts are included in other operating revenues in the accompanying statements of revenues, expenses, and changes in net position. Harborview recognized $6.2 million and $6.1 million for the years ended June 30, 2015 and 2014, respectively.

## (5) Capital Assets

The activity in Harborview's capital asset and related accumulated depreciation accounts for the years ended June 30, 2015 and 2014 is set forth below (in thousands):

| | Balance June 30, 2014 | Additions | Transfers | Retirements | Balance June 30, 2015 |
|---|---|---|---|---|---|
| Capital assets, not being depreciated: | | | | | |
| Land | $ 1,586 | — | — | — | 1,586 |
| Construction in process | 14,860 | 7,440 | (9,647) | — | 12,653 |
| Total capital assets, not being depreciated | 16,446 | 7,440 | (9,647) | — | 14,239 |
| Capital assets, being depreciated: | | | | | |
| Land improvements | 5,519 | — | 65 | — | 5,584 |
| Buildings, renovations and furnishings | 407,089 | — | 6,501 | — | 413,590 |
| Fixed equipment | 143,351 | — | 542 | — | 143,893 |
| Movable equipment | 274,538 | 8,404 | 2,539 | (1,199) | 284,282 |
| Leasehold improvements | 9,555 | — | — | — | 9,555 |
| Total capital assets, being depreciated | 840,052 | 8,404 | 9,647 | (1,199) | 856,904 |
| Total capital assets at historical cost | 856,498 | 15,844 | — | (1,199) | 871,143 |
| Less accumulated depreciation for: | | | | | |
| Land improvements | (2,312) | (316) | — | — | (2,628) |
| Buildings, renovations and | | | — | — | |
| furnishings | (174,899) | (13,501) | — | — | (188,400) |
| Fixed equipment | (119,588) | (5,139) | — | — | (124,727) |
| Movable equipment | (224,725) | (20,419) | — | 1,181 | (243,963) |
| Leasehold improvements | (3,615) | (551) | — | — | (4,166) |
| Total accumulated depreciation | (525,139) | (39,926) | — | 1,181 | (563,884) |
| Total capital assets, net | $ 331,359 | (24,082) | — | (18) | 307,259 |

| | Balance June 30, 2013 | Additions | Transfers | Retirements | Balance June 30, 2014 |
|---|---|---|---|---|---|
| Capital assets, not being depreciated: | | | | | |
| Land | $ 1,586 | — | — | — | 1,586 |
| Construction in process | 13,344 | 13,502 | (11,986) | — | 14,860 |
| Total capital assets, not being depreciated | 14,930 | 13,502 | (11,986) | — | 16,446 |
| Capital assets, being depreciated: | | | | | |
| Land improvements | 5,338 | — | 181 | — | 5,519 |
| Buildings, renovations and furnishings | 400,699 | — | 6,390 | — | 407,089 |
| Fixed equipment | 143,105 | — | 246 | — | 143,351 |
| Movable equipment | 265,915 | 6,089 | 4,770 | (2,236) | 274,538 |
| Leasehold improvements | 9,156 | — | 399 | — | 9,555 |
| Total capital assets, being depreciated | 824,213 | 6,089 | 11,986 | (2,236) | 840,052 |
| Total capital assets at historical cost | 839,143 | 19,591 | — | (2,236) | 856,498 |
| Less accumulated depreciation for: | | | | | |
| Land improvements | (1,997) | (315) | — | — | (2,312) |
| Buildings, renovations and furnishings | (161,522) | (13,377) | — | — | (174,899) |
| Fixed equipment | (114,152) | (5,436) | — | — | (119,588) |
| Movable equipment | (203,646) | (23,199) | — | 2,120 | (224,725) |
| Leasehold improvements | (2,985) | (630) | — | — | (3,615) |
| Total accumulated depreciation | (484,302) | (42,957) | — | 2,120 | (525,139) |
| Total capital assets, net | $ 354,841 | (23,366) | — | (116) | 331,359 |

Capital assets, net include intangible assets, net of accumulated depreciation of $0.7 million and $5.8 million as of June 30, 2015 and 2014, respectively.

## (6) Board-Designated and Restricted Assets

### *(a) Assets Whose Use is Limited*

Assets whose use is limited consist of the following, as of June 30 (in thousands):

| | | 2015 | 2014 |
|---|---|---|---|
| Board-designated assets: | | | |
| Pooled investments managed by King County | $ | 80,851 | 64,423 |
| Receivables and other | | 191 | 170 |
| Property held for future use, at cost, less accumulated depreciation | | 2,718 | 2,718 |
| Total board-designated assets | | 83,760 | 67,311 |
| Management-designated assets | | 25,574 | 25,423 |
| Restricted cash and investments: | | | |
| Investments restricted for capital by King County | | 5,590 | 11,686 |
| Investments restricted by donor | | 6,753 | 8,683 |
| Total restricted assets | | 12,343 | 20,369 |
| Total assets whose use is limited | $ | 121,677 | 113,103 |

### *(b) Board-Designated Assets*

Certain assets listed above have been designated by the Trustees for specific purposes. These assets comprise cash, cash equivalents, and other. The assets by designated purpose are as follows as of June 30 (in thousands):

| | | 2015 | 2014 |
|---|---|---|---|
| Commuter service fund | $ | 12,148 | 10,632 |
| Self-insurance fund | | 1,188 | 1,181 |
| Walter Scott Brown property | | 2,718 | 2,718 |
| Equipment fund | | 8,365 | 16,665 |
| Building repair and replacement fund | | 25,645 | 21,142 |
| Planned capital and program reserves | | 33,696 | 14,973 |
| Total | $ | 83,760 | 67,311 |

### *(c) Investments Restricted for Capital and by Donor*

Investments restricted for capital comprise investments held in the King County Investment Pool, managed for Harborview by the County and are $5.6 million and $11.6 million for the years ended June 30, 2015 and 2014, respectively. These investments represent unspent bond proceeds, required capital funding, and accumulated interest earnings. Use of these investments is restricted by the County for designated capital projects.

Investments restricted by donor represent assets whose use is restricted by grantors or contributors external to Harborview and are $6.8 million and $8.7 million as of June 30, 2015 and 2014, respectively. These investments consist of pooled investment funds of money markets, U.S. agency securities, U.S. agency mortgage-backed securities, U.S. treasury, U.S. municipal, and collateralized mortgaged obligations, and are carried at market value.

## (7) Noncurrent Liabilities

Long-term debt, reported as part of noncurrent liabilities, consists of the following as of June 30 (in thousands):

| | | 2015 | 2014 |
|---|---|---|---|
| 2006A Limited Tax General Obligation Refunding Bonds of King County, 5.0%; annual principal payments ranging from $515 to $655 through 2017, including premium of $7 as of June 30, 2015 | $ | 1,196 | 2,002 |
| 2010A Limited Tax General Obligation Refunding Bonds of King County, 3.0% to 5.0%, annual principal payments ranging from $115 to $150 through 2018 | | 410 | 1,080 |
| Total long-term debt | | 1,606 | 3,082 |
| Less current portion | | (805) | (755) |
| Total long-term debt, net of current portion | $ | 801 | 2,327 |

### *(a) Long-term Debt Overview*

King County issues debt on behalf of Harborview to meet capital needs. The County is the obligor of the debt and is responsible for meeting the associated debt covenant requirements. Harborview carries its obligation to the County as long-term debt on its statements of net position and makes payments to the County to cover debt service costs. The following is a summary of current outstanding obligations issued on behalf of Harborview.

**Series 2006 Bond Issue**

The 2006A Limited Tax General Obligation (LTGO) Refunding Bonds were issued on December 14, 2006 for the purpose of advance refunding and defeasing the Limited Tax General Obligation Refunding Bonds, 1996A and 1997G. The net proceeds were used to purchase U.S. government securities that were deposited with an escrow agent to provide for all future debt service payments on the refunded bonds. The bonds were deemed defeased upon deposit with the escrow agent.



(Continued)

**Series 2010 Bond Issue**

The 2010A Limited Tax General Obligation (LTGO) Refunding Bonds were issued on October 18, 2010 for the purpose of advance refunding and defeasing the Limited Tax General Obligation Refunding Bonds, 2001. The net proceeds were used to purchase U.S. government securities that were deposited with an escrow agent to provide for all future debt service payments on the refunded bonds. The bonds were deemed defeased upon deposit with the escrow agent.

### *(b) Long-Term Debt Maturities*

The following schedule shows debt service requirements for the next five years and thereafter, as of June 30, 2015, using the fixed interest rates, for both principal and interest (in thousands):

| | Principal | Interest | Total |
|---|---|---|---|
| 2016 | $ 805 | 68 | 873 |
| 2017 | 660 | 35 | 695 |
| 2018 | 115 | 5 | 120 |
| 2019 | — | — | — |
| 2020 | — | — | — |
| 2021–2023 | — | — | — |
| Total payments | 1,580 | 108 | 1,688 |
| Less current portion | (805) | (68) | (873) |
| Add unamortized premiums and loss on refunding, net | 26 | — | 26 |
| Long-term debt, net of current portions | $ 801 | 40 | 841 |

### *(c) Changes in Noncurrent Liabilities*

Changes in noncurrent liabilities during the fiscal years ended June 30, 2015 and 2014 are summarized below (in thousands):

| | Balance June 30, 2014 | Increases | Decreases | Balance June 30, 2015 | Due within one year |
|---|---|---|---|---|---|
| 2006A LTGO Bonds | $ 2,002 | — | (806) | 1,196 | 655 |
| 2010A LTGO Bonds | 1,080 | — | (670) | 410 | 150 |
| Unearned rent and other | 15,373 | — | (971) | 14,402 | 704 |
| Total noncurrent liabilities | $ 18,455 | — | (2,447) | 16,008 | 1,509 |

| | | Balance June 30, 2013 | Increases | Decreases | Balance June 30, 2014 | Due within one year |
|---|---|---|---|---|---|---|
| 2006A LTGO Bonds | $ | 2,592 | — | (590) | 2,002 | 610 |
| 2010A LTGO Bonds | | 1,210 | — | (130) | 1,080 | 145 |
| Unearned rent and other | | 15,790 | 287 | (704) | 15,373 | 704 |
| Total noncurrent liabilities | $ | 19,592 | 287 | (1,424) | 18,455 | 1,459 |

## (8) Risk Management

Harborview is exposed to risk of loss related to professional and general liability, employee medical, dental and pharmaceutical claims, and injuries to employees. Harborview participates in risk pools managed by the University to mitigate risk of loss related to these exposures.

### *(a) Professional and General Liability*

The University's professional liability program currently includes self-insured and commercial reinsurance coverage components. Harborview's annual funding to the professional liability program is determined by the University administration using information from an annual actuarial study. The actuary used a discount rate of 5.5% for both 2015 and 2014 in recognition of the expected earnings of the self-insurance fund and other factors. In addition to the University, the participants in the professional liability program include Harborview, UWP, CUMG, UWNC, School of Dentistry, Airlift, Northwest Hospital, and UW Medical Center. The various participants in the program contribute to the self-insurance fund and share in the expenses of the Health Sciences Risk Management Office.

Harborview's contribution to the professional liability program was $3.4 million and $3.2 million in 2015 and 2014, respectively, recorded in supplies and other expense on the statements of revenues, expenses, and changes in net position.

### *(b) Employee Medical and Workers' Compensation*

The University pools employee benefit costs, including employee medical and workers' compensation, for all University employees. Departments, divisions, and affiliated organizations with employees covered under the University benefit programs are charged a single benefit rate, based on employee salary class.

Harborview, as an affiliated organization with University employees deployed at Harborview are covered under the University benefit programs, participates in the benefit pool. See further discussion in note 9.

## (9) Benefit Costs

Benefit costs are pooled centrally for all University employees. Annually the University reviews total employee benefit costs and prepares standard benefit load rates by employment classification. Departments, divisions, agencies, component units, and affiliated parties of the University that have University employees qualifying for employee benefit coverage are charged a cost allocation using the determined benefit load rate and budgeted salary dollars by employment classification. All funding of obligations are on a pay-as-you-go basis. At the end of the reporting period, the cost allocation is compared to actual benefit costs and differences between actual and budgeted costs are included as a component of the benefit load rates charged in the following year.

Employee benefits covered under the benefit pool include the following:

- Workers' compensation
- Unemployment compensation
- Employee medical, dental, and vision
- Retirement and other postretirement benefit plans
- Social security
- Medicare
- Separation leave

During the fiscal years ended June 30, 2015 and 2014, Harborview incurred and paid $101.1 million and $103.2 million to the University for the employee benefits listed above, which is recorded as employee benefits in the statements of revenues, expenses, and changes in net position.

### Retirement and Other Postretirement Benefit Plans

Harborview personnel are employees of the University. All of the employees of the University participate in the following state and University sponsored retirement and other postretirement benefit plans:

**Washington Public Employees Retirement System (PERS)** – PERS is a cost sharing, multiple-employer, defined-benefit pension plan administered by the state of Washington Department of Retirement Systems. There are three separate plans covered under PERS. PERS Plan 1 provides retirement and disability benefits and minimum benefit increases beginning at age 66 to eligible nonacademic plan members hired prior to October 1, 1977. PERS Plans 2 and 3 provide retirement and disability benefits and a cost-of-living allowance to eligible nonacademic plan members hired on or after October 1, 1977. In addition, PERS Plan 3 has a defined-contribution component, which is fully funded by employee contributions. The authority to establish and amend benefit provisions resides with the legislature. The Department of Retirement Systems issues a publicly available financial report that includes financial statements and required supplementary information for PERS. The report may be obtained by writing to the Department of Retirement Systems, P.O. Box 48380, Olympia, WA 98504-8380, or visiting http://www.drs.wa.gov/administration/.

The Office of the State Actuary, using funding methods prescribed by statute, determines actuarially required contribution rates for PERS. Funding obligations are measured at the University level and the University allocates expense to departments, divisions, agencies, and component units through the benefit load.

Based on the University's benefit load apportionment Harborview incurred and paid \$25.7 million and \$22.6 million in fiscal years 2015 and 2014, respectively, related to annual PERS funding, which is recorded in employee benefits on the statements of revenues, expenses, and changes in net position.

**University of Washington Retirement Plan (UWRP)** – UWRP is a defined contribution plan administered by the University. All faculty and professional staff are eligible to participate in the plan. Contributions to UWRP are invested by participants in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations. Benefits from fund sponsors are available upon separation or retirement at the member's option. RCW 28B.10.400 et. Seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

Funding is determined by employee age and ranges from 5% to 10% of employee salary. Funding obligations are calculated at the University level and the University allocates expense to department, divisions, agencies, and component units through the benefit load.

Based on the University's benefit load apportionment Harborview incurred and paid \$4.7 million and \$4.5 million in fiscal years 2015 and 2014, respectively, related to annual UWRP funding, which is recorded in employee benefits on the statements of revenues, expenses, and changes in net position.

**University of Washington Supplemental Retirement Plan (the 401(a) Plan) –** The 401(a) Plan provides for a supplemental payment component which guarantees a minimum retirement benefit based upon a one-time calculation at each eligible participant's retirement date. The University makes direct payment to qualifying retirees when the retirement benefits provided by UWRP do not meet the benefit goals.

The University receives an independent actuarial valuation to determine funding needs for the supplemental payment component of UWRP. The funding obligation is determined at the University level and the University allocates expense to departments, divisions, agencies, and component units through the benefit load.

Based on the University's benefit load apportionment Harborview incurred and paid \$0.8 million and \$1.6 million in fiscal years 2015 and 2014, respectively, related to annual 401(a) Plan funding, which is recorded in employee benefits on the statements of revenues, expenses, and changes in net position.



(Continued)

**Other Post-Employment Benefits (OPEB)** – All University employees, including medical center employees, are eligible for participation in healthcare and life insurance programs administered by the WSHCA. Harborview retirees may elect coverage through state health and life insurance plans, for which they pay less than the full cost of the benefits based on their age and other demographic factors.

The Office of the State Actuary determines total OPEB obligations at the State level using individual state employee data, including age, retirement eligibility, and length of service. Information to support actuarial calculations at the division, department, or component unit level is not available. The State is ultimately responsible for the obligation; therefore, the annual required contribution (ARC) is not recorded at the University or its departments, divisions, agencies, or component units.

## (10) Related Parties

Harborview has engaged in a number of transactions with related parties. When economic benefits are either provided or received by Harborview, these transactions are recorded as operating revenues or expenses, respectively, by Harborview. Harborview records cash transfers between Harborview and related parties that are not the result of economic benefits as nonoperating expenses within the statements of revenues, expenses, and changes in net position.

### *(a) University of Washington*

University divisions provide various levels of support to Harborview. The following is a summary of services purchased.

**UW School of Medicine**

Harborview purchases a variety of clinical and administrative services from the School. For example, Harborview purchases laboratory services from the School and Harborview pays a portion of residents and faculty salaries for clinical and administrative support at Harborview. Harborview also transfers a portion of its Medicare reimbursement for medical education to the School in support of teaching costs. The amounts paid for these services are shown below (see (d)).

**UW Medicine Central Costs**

UW Medicine provides services to UW Medical Center such as advancement, compliance, telemedicine, community relations staffing, medical staff oversight, marketing, and other administrative services related to UW Medicine. The amounts paid by UW Medical Center for these services are shown below (see (d)).

**University of Washington Consolidated Laundry**

The University of Washington Consolidated Laundry (the Laundry) provides laundry services to Harborview, UW Medical Center, the Veteran’s Administration, Swedish Edmonds, Skagit Valley Hospital, UW, Northwest Hospital, and UWNC.

Harborview purchases laundry services from the Laundry and the amounts purchased are shown below (see (d)).

**UW Physicians Network dba UW Neighborhood Clinics**

Under an annual agreement between the involved UW Medicine entities, Harborview provides strategic support of approximately 20% of the UWNC's annual operating loss and capital funding needs for fiscal years 2015 and 2014. Funding from Harborview to UWNC was $6.4 million and $4.4 million for fiscal years 2015 and 2014, respectively, and is recorded as funding to affiliates in the statements of revenues, expenses, and changes in net position.

**Other Divisions of the University**

In addition to the divisions and transactions identified above, Harborview purchases information technology services, general and professional liability insurance, printing, accounting, temporary staffing, and other administrative and operational services. The amounts for these transactions are shown below (see (d)).

***(b) UW Medicine/Northwest dba Northwest Hospital and Medical Center***

In 2015, Harborview provided strategic support to Northwest Hospital for operating purposes. Funding from Harborview to Northwest Hospital was $8.2 million for the year ended June 30, 2015 and is recorded as funding to affiliates in the statements of revenues, expenses, and changes in net position and as a payable to the University in the statements of net position.

***(c) King County***

The County holds all investment funds on behalf of Harborview. The County also processes all payments to vendors outside of the University divisions. Additional detail describing Harborview's position within the County is provided in note 1.

Harborview has agreed to provide space and services on behalf of the County for certain grants and contracts, for which Harborview receives rental income and grant revenue from the County. Additionally, Harborview has long-term debt contracts with the County in the form of General Obligation Bonds. The terms of these agreements are described in more detail in note 7.

***(d) Summary of Related-Party Transactions (in thousands):***

| Revenue (expense) transactions | | 2015 | 2014 |
|---|---|---|---|
| Services and supplies purchased from the University and its departments and affiliates: | | | |
| The School | $ | (66,838) | (52,898) |
| Central Costs | | (9,888) | (8,737) |
| The Laundry | | (3,015) | (3,072) |
| UW Medical Center | | (2,696) | (1,564) |
| UWP | | (1,156) | (1,026) |
| UW Medicine ITS | | (55,087) | (51,655) |
| Other University divisions and departments | | (21,473) | (6,230) |
| Services provided to the University and its departments and affiliates: | | | |
| The School | | 8,103 | 7,195 |
| UW Medical Center | | 2,423 | 1,731 |
| Services provided to King County | | 708 | 723 |

Harborview had net amounts (due to) due from related parties for various transactions, which are included in funds held by the University, patient accounts receivable, other receivables, other current assets, accrued salaries, wages and employee benefits, payable to the University, and long-term debt in the accompanying statements of net position. The net amounts (due to) due from related parties as of June 30, 2015 and 2014 are as follows (in thousands):

| Net receivable (payable) | | 2015 | 2014 |
|---|---|---|---|
| The University and its departments and affiliates: | | | |
| The School | $ | 2,880 | (976) |
| UWP | | 1,553 | 1,334 |
| UW Medical Center | | 937 | 359 |
| Airlift | | 2,200 | 2,061 |
| Other University divisions and departments | | (29,209) | (35,156) |
| King County | | 131 | 86 |
| Northwest Hospital | | (7,090) | — |

## (11) Commitments and Contingencies

***(a) Operating Leases***

Harborview leases certain medical office space and equipment under operating lease arrangements. Total rental expense in years ended June 30, 2015 and 2014 for all operating leases was $17.4 million and $17.8 million, respectively, which is recorded in supplies and other expenses in the statement of revenues, expenses, and change in net position.

The following schedule shows future minimum lease payments by fiscal year as of June 30, 2015 (in thousands):

| | | |
|---|---|---|
| 2016 | $ | 1,054 |
| 2017 | | 515 |
| 2018 | | 206 |
| 2019 | | 66 |
| 2020 | | — |
| 2021–2025 | | — |
| | $ | 1,841 |

### *(b) Purchase Commitments*

Harborview has current commitments at June 30, 2015 of $21.7 million related to various construction projects, and equipment purchases. Harborview intends to use its unrestricted funds for these commitments.

### *(c) Regulatory Environment*

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, governmental healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government agencies are actively conducting investigations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs, together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that Harborview is in compliance with the fraud and abuse regulations as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions known or unasserted at this time.

### *(d) Litigation*

Harborview is involved in litigation arising in the normal course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect to Harborview's future financial position or results of operations.

### *(e) Collective Bargaining Agreements*

Harborview has a total of approximately 4,476 employees. Of this total, approximately 78% are covered by collective bargaining agreements as of June 30, 2015 and 2014. Nurses are represented by the Service Employees International Union (SEIU) and other healthcare and support workers are represented by the SEIU and Washington Federation of State Employees (WFSE). All collective bargaining agreements expired on June 30, 2015. Harborview's management and SEIU continue to negotiate the terms of a new agreement, and during the interim period, SEIU members continue to work under the terms of the expired agreement. SEIU and WFSE collective bargaining agreements were signed and expire on June 30, 2017.

### *(f) Patricia Bracelin Steel Building*

The Patricia Bracelin Steel building (PSB) is a five-story building containing 156,800 square feet of office space with related parking. The building is primarily occupied by Harborview. Prior to December 2012, the County leased PSB from Broadway Office Properties (BOP) and instructed Harborview, through County Ordinance, to budget funds, annually, to make rental payments under the lease. The lease agreement with BOP provided the County an option to terminate the lease agreement and purchase the building for total outstanding principal on monthly rent payments beginning on or after December 1, 2012.

In December 2012, the County exercised its option to purchase the building from BOP. To fund the purchase of the building, the County issued Limited Tax General Obligation (LTGO) debt. The County has instructed Harborview to budget funds, annually, to be used to fund payments due under the LTGO debt. As the financial obligations of the LTGO debt remains the responsibility of the County, Harborview accounts for these payments as rental expense. Rental expense was approximately $2.8 million for the years ended June 30, 2015 and 2014, respectively.

### *(g) Ninth and Jefferson Building*

The Ninth & Jefferson Building, a 14-story medical office building with approximately 440,000 square feet, including 13,300 square feet of retail space, and five levels of underground parking, is located at 908 Jefferson Street in Seattle. The building was completed in January 2010 and several Medical Center departments now occupy the building.

In 2006, the Trustees passed a resolution in support of the Ninth & Jefferson Building under the 63-20 financing model. The building owner and lessor is Ninth & Jefferson Building Properties; however, the land upon which the building is constructed is owned by the County and leased to Ninth & Jefferson Building Properties under a ground lease. The County has entered into a lease with Ninth & Jefferson Building Properties for the building with a 30-year term. The lease qualifies for capital lease treatment and as such, the building asset and related lease obligation are recorded by the County based upon the terms of the agreement.

The County Council has directed the Trustees to budget funds, annually, to make the rental payments due under the lease. As the financial obligations of the lease remain the responsibility of the County, Harborview accounts for these rental payments as rental expense. Lease expense was approximately $12.7 million for the years ended June 30, 2015 and 2014, respectively. If Harborview continues to occupy this space, annual lease expense will not differ significantly from the amount recognized in 2015.

**UNIVERSITY OF WASHINGTON**
**METROPOLITAN TRACT**

FINANCIAL REPORT

JUNE 30, 2015

# C O N T E N T S

petersonsullivan LLP
Certified Public Accountants
& Advisors

**INDEPENDENT AUDITORS' REPORT**

To the Board of Regents
University of Washington
Seattle, Washington

We have audited the accompanying financial statements of the University of Washington Metropolitan Tract, which comprise the statement of assets, liabilities, and net position as of June 30, 2015, and the related statements of revenues, expenses, and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements.

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

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

**Auditor's Responsibility**

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

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

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

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**Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington Metropolitan Tract as of June 30, 2015, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States.

**Supplementary Information**

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the University of Washington Metropolitan Tract as a whole. The details of property on page 17 are presented for the purposes of additional analysis and are not a required part of the basic financial statements.

The details of property on page 17 are the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Peterson Sullivan LLP

October 20, 2015

**UNIVERSITY OF WASHINGTON**
**METROPOLITAN TRACT**

STATEMENT OF ASSETS, LIABILITIES, AND NET POSITION

June 30, 2015

| | |
|---|---|
| ASSETS | |
| Current Assets | |
| Cash held in trust | $ 8,968,177 |
| Funds held by the University | 26,508,196 |
| Security deposits - residential | 52,385 |
| Due from Fairmont Olympic Hotel | 791,502 |
| Accounts receivable, net of allowance of $6,302 | 1,008,272 |
| Other current assets | 368,167 |
| Total current assets | 37,696,699 |
| Property, net | 129,851,245 |
| Straight-line rent adjustment | 3,299,789 |
| Other assets | 25,155 |
| Total assets | $ 170,872,888 |
| LIABILITIES | |
| Current Liabilities | |
| Accounts payable and accrued expenses | $ 2,948,748 |
| Leasehold excise tax payable | 2,066,940 |
| Security deposits - residential | 52,385 |
| Unearned rent revenue | 1,308,032 |
| Current portion of long-term debt | 3,580,000 |
| Total current liabilities | 9,956,105 |
| Security Deposits - commercial | 1,251,708 |
| Long-Term Debt, net of discount and current portion | 38,518,719 |
| Total liabilities | 49,726,532 |
| NET POSITION | |
| Invested in capital assets, net of related debt | 87,752,526 |
| Unrestricted | 33,393,830 |
| Total net position | 121,146,356 |
| Total liabilities and net position | $ 170,872,888 |

See Notes to Financial Statements

**UNIVERSITY OF WASHINGTON**
**METROPOLITAN TRACT**

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

For the Year Ended June 30, 2015

| | |
|---|---|
| Operating Revenues | |
| Office rent | $ 32,009,764 |
| Hotel rent | 5,289,862 |
| Retail rent | 4,664,007 |
| Parking | 3,512,667 |
| Residential rent | 1,907,094 |
| Rainier Square rent | 641,467 |
| Other rent | 408,480 |
| Other income | 143,391 |
| Total operating revenues | 48,576,732 |
| Operating Expenses | |
| Property operating expenses | 8,054,635 |
| General and administrative | 6,578,909 |
| Taxes | 5,600,807 |
| Property management | 1,389,911 |
| Total operating expenses | 21,624,262 |
| Operating income before depreciation and amortization | 26,952,470 |
| Depreciation | 10,781,955 |
| Amortization | 75,464 |
| **Net operating income** | **16,095,051** |
| Other Revenues (Expenses) | |
| Interest income | 240,814 |
| Interest expense | (385,627) |
| Total other expenses | (144,813) |
| **Net income** | **15,950,238** |
| Transfers | |
| Transfers from UW Real Estate Office | 626,448 |
| Distribution to University Building Fund | (8,000,000) |
| Total transfers | (7,373,552) |
| Change in net position | 8,576,686 |
| Total net position, beginning of year | 112,569,670 |
| Total net position, end of year | $ 121,146,356 |

See Notes to Financial Statements

**UNIVERSITY OF WASHINGTON**
**METROPOLITAN TRACT**

STATEMENT OF CASH FLOWS

For the Year Ended June 30, 2015

| | |
|---|---|
| Cash Flows From Operating Activities | |
| Cash received from tenants | $ 50,277,102 |
| Payments made to vendors | (10,207,449) |
| Payments made to employees | (2,967,674) |
| Payments for leasehold excise taxes | (4,608,437) |
| Net cash flows from operating activities | 32,493,542 |
| Cash Flows From Capital and Related Financing Activities | |
| Improvements made to long-lived assets | (43,586,472) |
| Payments to University Treasury Department | (8,500,000) |
| Borrowing on University Treasury Department | 42,098,719 |
| Interest expense | (385,627) |
| Net cash flows from capital and related financing activities | (10,373,380) |
| Cash Flows From Noncapital Financing Activities | |
| Funds received from UW Real Estate Office | 626,448 |
| Distribution to University Building Fund | (8,000,000) |
| Net cash flows from noncapital financing activities | (7,373,552) |
| Cash Flow From Investing Activity | |
| Interest received | 240,814 |
| **Net change in cash** | **14,987,424** |
| Cash, beginning of year | 20,488,949 |
| Cash, end of year | $ 35,476,373 |

Cash in the statement of cash flows is reported in the statement of assets, liabilities, and net position as follows:

| | |
|---|---|
| Cash held in trust | $ 8,968,177 |
| Funds held by the University | 26,508,196 |
| Total | $ 35,476,373 |

See Notes to Financial Statements

**UNIVERSITY OF WASHINGTON**
**METROPOLITAN TRACT**

STATEMENT OF CASH FLOWS
(Continued)
For the Year Ended June 30, 2015

| | | |
|---|---|---|
| Reconciliation of Net Operating Income to Net | | |
| Cash Flows From Operating Activities | | |
| Net operating income | $ | 16,095,051 |
| Adjustments to reconcile net operating income to net | | |
| cash flows from operating activities | | |
| Depreciation | | 10,781,955 |
| Amortization | | 75,464 |
| Changes in operating assets and liabilities | | |
| Due from Unico Properties LLC | | 2,476,076 |
| Due from Fairmont Olympic Hotel | | (64,908) |
| Accounts receivable | | (1,008,272) |
| Straight-line rent adjustment | | (376,533) |
| Security deposits | | (52,385) |
| Other assets | | (114,704) |
| Due to Unico Properties LLC | | (1,016,775) |
| Leasehold excise tax payable | | 992,370 |
| Unearned rent revenue | | 726,392 |
| Other current liabilities | | 2,823,554 |
| Security deposits payable | | 1,156,257 |
| Net cash flows from operating activities | $ | 32,493,542 |

See Notes to Financial Statements

## NOTES TO FINANCIAL STATEMENTS

### Note 1. Metropolitan Tract Ownership and Operation

The University of Washington Metropolitan Tract ("the Metropolitan Tract"), located in downtown Seattle, comprises approximately 11 acres of developed property, including office space, retail space, residential apartments, parking, and a luxury hotel. This land was the original site of the University of Washington ("the University") from 1861 until 1895, when the University moved to its present location on Lake Washington. Since the early 1900s, the Metropolitan Tract had been leased by the University to entities responsible for developing and operating the property. As discussed below, the University took a more active management role in October 2014.

On July 18, 1953, the University leased a significant portion of the office, retail, and parking facilities to Unico Properties, LLC ("Unico") under a master lease agreement ("the Unico Lease"). In 2004, the Unico Lease was amended to exclude the Cobb Building, and a new lease for that building was signed with Unico ("the Cobb Lease"). In 1995, the University assumed a sublease for a portion of the Rainier Tower, one of the Unico-controlled buildings on the Metropolitan Tract, and directly controlled approximately 380,000 square feet of office space referred to as the Rainier Tower Sublease.

The Unico Lease expired on October 31, 2014, and control of the properties transferred to the University. The University and Unico entered into an agreement that addressed "end of lease" issues that were not addressed in the original Unico Lease ("the Transition Agreement"), including the assignment of leases, pro-rata revenue and calculations, and transfer of personal property essential to the buildings.

In addition, the following events occurred simultaneously with the Unico Lease expiration:

- The University terminated the lease with Unico for the Cobb Building and paid a termination price of $33.4 million. The termination price paid was calculated based on a formula provided in the Cobb Lease and represented the value of the leasehold improvement.

- Ownership of the Palomar Garage property transferred to the University as agreed to in the Unico Lease.

- On May 15, 2014, the University entered into an agreement with WRC Fourth Avenue LLC ("WRC"), an entity controlled by Wright Runstad, to undertake activities relating to the redevelopment of the site currently referred to as the Rainier Square ("the Predevelopment Agreement"). In connection with this agreement, which commenced on November 1, 2014, and expires upon the completion of certain development milestones, the University entered into a property management agreement for the Rainier Tower and the Interim Agreement for operation of the Rainier Square. Upon satisfaction of the Predevelopment Agreement, the University plans to lease the site to Wright Runstad for a term of 80 years.

- The Interim Agreement provides Wright Runstad with significant control over the management and operation of the Rainier Square Building in exchange for a fixed rent schedule for up to seven years.

- The University contracted with Unico to perform leasing for all of the properties in the Metropolitan Tract and provide certain management duties for all of the properties, except the Rainier Square, the Rainer Tower (as noted above), and the Fairmont Olympic Hotel. Unico subcontracted the management of the residential portion of the Cobb Building to Blanton Turner.

On January 18, 1980, the Board of Regents entered into a lease ("the Hotel Lease") with the Olympic Hotel property, which expires in 2040. The hotel was operated as the Four Seasons Olympic Hotel until July 31, 2003. On August 1, 2003, the remaining lease term was assigned to LHCS Hotel Holding (2002), LLC. The hotel was renamed the Fairmont Olympic Hotel and managed by Fairmont Hotels and Resorts, Inc.

On September 18, 2007, Legacy REIT, a publicly traded Canadian real estate investment trust and parent company of LHCS Hotel Holding (2002), LLC, was purchased by Cadbridge Investors, LP, a limited partnership majority owned by Cadim (a division of the Caisse de depot et placement du Quebec). The tenant under the Hotel Lease remained the same, and the management of the hotel by Fairmont Hotels and Resorts, Inc. did not change.

On June 1, 2015, the University consented to the assignment of the Hotel Lease from LHCS Hotel Holding (2002) LLC to IC/RCDP Seattle Hotel, LLC and the simultaneous sublease of the premises to IC/RCDP Seattle Hotel TRS, LLC ("IC/RCDP Seattle"). The new tenant, IC/RCDP Seattle, is two-thirds owned by Cadim and one-third owned by RCDP Seattle Hotel JV, LLC.

The Hotel Lease contains a termination clause that allows the tenant to terminate the lease in 2020, 2025, 2030, or 2035, if notification is provided 36 months prior to termination.

The Metropolitan Tract is managed by the University under the authority of state law, which contains certain restrictions on the disposal of property and use of income. These restrictions include a prohibition on the sale of land and a limitation that lease terms extend no more than 80 years.

## Note 2. Summary of Significant Accounting Policies

### Basis of Accounting

These financial statements present only a selected portion of the activities of the University. As such, they are not intended to and do not present either the financial position, results of operations, or changes in net position of the University. The financial statements have been prepared in accordance with governmental accounting principles generally accepted in the United States. The financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned and expenses are recorded when an obligation has been incurred.

Significant revenue recognition and related expense policies are as follows:

- Office, retail, and residential revenues are recognized (on a straight-line basis) each month based on tenant leases in place. Prior to November 1, 2014, with the exception of the Rainier Tower Sublease, all rent revenue was recognized when earned based on the terms of the Unico Lease. There were no residential revenues during this period, as these relate solely to the Cobb building, which was transferred back to the Metropolitan Tract on November 1, 2014.

- Hotel Rent comprises minimum monthly payments as calculated under the Hotel Lease, in addition to a percentage of tenant revenues as calculated at the end of the year. The management of the Metropolitan Tract estimates and accrues the percentage rent for the period from January to June of 2015. There have been no significant adjustments from the estimated amount recognized and actual amounts calculated at the end of each lease year.

- Parking revenues are recognized based on tenant leases in place or as spaces are occupied. Prior to November 1, 2014, these were recognized based on contractual payments with Unico.

- Rainier Square rent revenues are recognized on a monthly basis as outlined by the Interim Agreement. Revenues prior to the agreement for Rainier Square were recognized as part of office and retail rent based on the Unico Lease.

- Direct operating expenses related to the properties, including utilities, repairs and maintenance, and security and janitorial costs, are reported as property operating expenses.

- Expenses incurred in the management of the property, including contractual payments, are reported as property management.

- All other indirect expenses not related to the direct operating or property management are recorded as general and administrative.

- Non-operating revenue and expenses are activities that are not related to rental activities, including interest income and expense.

During the fiscal year ended June 30, 2015, the University implemented Governmental Accounting Standards Board Statement No. 68 (Accounting and Financial Reporting for Pensions). This new standard did not have any significant effect on the financial statements of the Metropolitan Tract for the year ended June 30, 2015.

**Cash Held in Trust**

Cash held in trust represents operating cash held in financial institutions for various properties on behalf of the University. Cash balances held in the trust and other cash balances may exceed federally insured limits during the year.

**Funds Held by the University**

Funds held by the University are funds invested in pooled investments with the University. The University combines most short-term available cash balances from various departments into the invested funds pool, which is primarily composed of U.S. government and agency securities, mortgage rated investments, and asset backed securities, as well as units in the Consolidated Endowment Fund ("CEF"), which is a diversified investment fund. The underlying investments in CEF include emerging market equity securities, developed market equity securities and fixed income securities.

The University annually allocates investment earnings to the departments with qualifying funds in the invested funds pool based on relative amount invested at a rate determined and approved by the University. For the years ended June 30, 2015 and 2014, the rate determined by the University was 2.0%. Principal amounts invested in the pooled invested are guaranteed by the University.

**Security Deposits – Residential**

Security deposits – residential consists of amounts collected by the University from residential tenants in the Cobb Building as security in the event of a lease default. These deposits are required to be retained and segregated from the University's operating cash. There are no such requirements for security deposits received by commercial tenants.

**Accounts Receivable**

Accounts receivables are due from tenants for rent and other reimbursements. The University considers all accounts greater than 90 days old to be past due and uses the allowance method for recognizing bad debts. When an account is deemed uncollectible, it is generally written off against the allowance. These receivables are generally unsecured and do not bear interest. At June 30, 2015, the balance of allowance for uncollectible accounts amounted to $6,302.

**Due from Fairmont Olympic Hotel**

This amount represents a receivable from the Fairmont Olympic Hotel for leasehold improvement taxes payable to the State of Washington and the percentage rent due for January to June 2015. A corresponding payable for the leasehold improvement taxes is included in leasehold excise tax payable.

**Straight-Line Rent Adjustment**

Many commercial and residential leases contain fixed escalations of the minimum annual lease payment during the original term of the lease. Therefore, rental income is recognized on the straight-line basis over the lease term. The difference between rental income recognized and the amount currently receivable is recorded as a straight-line rent adjustment.

**Property and Depreciation**

Land and buildings are recorded at the appraised values as of November 1, 1954, with subsequent additions at cost, when the assets are placed in service. Tenant and building improvements that have not yet been placed in service as of year-end are recorded as construction in progress and are expected to be completed within the next year. Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets as follows:

| | |
|---|---|
| Buildings | 50 - 60 years |
| Modernizations | 20 years |
| Tenant improvements | The lease term |

The University reviews long-lived assets for impairment whenever events or changes in circumstances have indicated that the carrying amount of the assets might not be recoverable. There were no such impairments during the year ended June 30, 2015.

**Leasehold Excise Tax Payable**

Leasehold excise tax is payable on a quarterly basis to the State of Washington. The current liability represents taxes collected on rent during April to June of 2015, as well as accruals related to percentage rent that is expected to be collected under the Hotel Lease from January to June of 2015, but will not be determined until the end of calendar year 2015.

**Net Position**

The University's net position is presented as net investment in capital assets, with the remainder considered unrestricted net position. Capital assets consist of land, building, building improvements, furniture, fixtures and equipment, and construction in progress. The related debt is debt issued to support the acquisition and construction of capital assets. Unrestricted assets include assets that have no restrictions placed on them, as well as assets that have been internally restricted, if any.

**Unearned Rent Revenue**

Tenant rent payments received in advance are deferred until the period to which the payments relate.

**Fair Value of Financial Instruments**

The Metropolitan Tract's financial instruments consist primarily of cash held in trust, funds held by the University, receivables, payables, and long-term debt. The carrying amounts of cash held in trust, funds held by the University, receivables, and payables approximate their respective estimated fair value due to their short-term nature. The carrying amount of the long-term debt approximates the fair value because the interest rate on these loans does not vary materially from the market rate for similar debt instruments.

**Transfer from UW Real Estate Office**

This represents funds that were transferred from the UW Real Estate Office to the Metropolitan Tract.

**Distribution to University Building Fund**

During the year ended June 30, 2015, $8,000,000 was distributed from the Metropolitan Tract to the University Building Fund. The distribution is determined annually based on cash available after consideration of future operating and capital expenses and adequate reserves.

**Property Management**

Property management expenses represent fees paid to Unico, Wright Runstad, and Blanton Turner for services rendered on the properties. The fees are based on a percentage of tenant rent recognized at each property. Total fees paid to Unico and Wright Runstad were $273,755 and $213,154, respectively, for the year ended June 30, 2015. Blanton Turner serves as a sub-contractor to Unico under the University's property management agreement with Unico.

**Lease Commissions**

Lease commissions are costs paid to commercial real estate brokers that facilitate the execution of tenant leases. These commissions are expensed as incurred.

**Income Taxes**

As part of the University, the Metropolitan Tract is exempt from federal income taxes, unless it earns unrelated business income.

**Use of Estimates**

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

## Subsequent Events

Management of the University has evaluated subsequent events through the date these financial statements were available to be issued, which was October 20, 2015.

## Note 3. Property

Property activity for the year ended June 30, 2015, is summarized as follows:

| | Balance at June 30, 2014 | Additions | Transfers | Balance at June 30, 2015 |
|---|---|---|---|---|
| Property, not being depreciated: | | | | |
| Land | $ 9,974,594 | $ - | $ - | $ 9,974,594 |
| Construction in progress | 4,600,204 | 4,387,580 | (4,600,205) | 4,387,579 |
| Total property not being depreciated | 14,574,798 | 4,387,580 | (4,600,205) | 14,362,173 |
| Property, being depreciated: | | | | |
| Land improvements | 793,423 | | | 793,423 |
| Buildings | 95,503,891 | | | 95,503,891 |
| Tenant improvements | 55,067,124 | 4,177,459 | 1,775,931 | 61,020,514 |
| Modernizations | 86,449,962 | 34,911,078 | 2,824,274 | 124,185,314 |
| Furniture, fixtures, and equipment | | 110,355 | | 110,355 |
| Total property being depreciated | 237,814,400 | 39,198,892 | 4,600,205 | 281,613,497 |
| Less accumulated depreciation: | | | | |
| Land improvements | 793,423 | | | 793,423 |
| Buildings | 69,839,540 | 1,316,650 | | 71,156,190 |
| Tenant improvements | 40,311,296 | 4,431,095 | | 44,742,391 |
| Modernizations | 44,398,211 | 5,024,961 | | 49,423,172 |
| Furniture, fixtures, and equipment | | 9,249 | | 9,249 |
| Total accumulated depreciation | 155,342,470 | 10,781,955 | | 166,124,425 |
| Property, net | $ 97,046,728 | $ 32,804,517 | $ - | $ 129,851,245 |

There were no significant disposals of property in fiscal year 2015.

## Note 4. Long-Term Debt

In March 2015, a short-term loan of $8,500,000 from the University was replaced by a long-term loan from the University that was financed through the issuance of taxable serial bonds. The loan balance as of June 30, 2015, was $8,535,000. The debt has an effective interest rate of 0.86% and a maturity date of December 2017. Also, in March 2015, the University issued general revenue bonds, and the Metropolitan Tract received $33.4 million in financing from the University's Treasury Department through the issuance of the general revenue bonds. The loan balance as of June 30, 2015, was $33,563,719. The effective interest rate over the 30-year term of the loan is 3.49% and the loan matures in December 2044. Both loans are unsecured, but are expected to be repaid through revenues generated by the Metropolitan Tract properties.

Long-term liability activity for the year ended June 30, 2015, is summarized as follows:

| | Balance at June 30, 2014 | Additions | Reduction | Balance at June 30, 2015 |
|---|---|---|---|---|
| Long-term debt | $ - | $ 42,098,719 | $ - | $ 42,098,719 |
| Current portion | | | | (3,580,000) |
| Non-current portion | $ - | | | $ 38,518,719 |

The following is a summary of future payments (principal and interest) to be paid to the University for the years ending June 30:

| | Principal | Interest | Total |
|---|---|---|---|
| 2016 | $ 3,580,000 | $ 1,098,331 | $ 4,678,331 |
| 2017 | 3,600,000 | 1,079,278 | 4,679,278 |
| 2018 | 3,630,000 | 1,051,745 | 4,681,745 |
| 2019 | 770,000 | 1,029,744 | 1,799,744 |
| 2020 | 785,000 | 1,017,216 | 1,802,216 |
| 2021 - 2025 | 4,190,000 | 4,815,750 | 9,005,750 |
| 2026 - 2030 | 4,855,000 | 4,161,240 | 9,016,240 |
| 2031 - 2035 | 5,720,000 | 3,287,478 | 9,007,478 |
| 2036 - 2040 | 6,830,000 | 2,173,692 | 9,003,692 |
| 2041 - 2045 | 8,138,719 | 783,951 | 8,922,670 |
| | $ 42,098,719 | $ 20,498,425 | $ 62,597,144 |

**Note 5. Future Minimum Rent**

The base rental income on the Fairmont Olympic Hotel is subject to change on an annual basis, as set forth in the lease. At the end of each lease year, the annual rent is adjusted for a percentage of revenues, not below an annual minimum of $1,260,000.

Minimum future rental income under the Hotel Lease are as follows for the years ending June 30:

| | |
|---|---|
| 2016 | $ 1,260,000 |
| 2017 | 1,260,000 |
| 2018 | 1,260,000 |
| 2019 | 1,260,000 |
| 2020 | 1,260,000 |
| Thereafter | 24,360,000 |
| | $ 30,660,000 |

Minimum future rental income under the Interim Agreement for the Rainier Square property are as follows for the years ending June 30:

| | | |
|---|---|---|
| 2016 | $ | 962,200 |
| 2017 | | 858,867 |
| 2018 | | 703,867 |
| 2019 | | 548,867 |
| 2020 | | 497,200 |
| Thereafter | | 165,733 |
| | $ | 3,736,734 |

Minimum future rental income under non-cancelable lease agreements with various commercial (office and retail) and residential tenants are as follows for the years ending June 30:

| | | |
|---|---|---|
| 2016 | $ | 40,515,650 |
| 2017 | | 35,828,383 |
| 2018 | | 34,980,557 |
| 2019 | | 25,401,044 |
| 2020 | | 21,096,598 |
| Thereafter | | 80,870,001 |
| | $ | 238,692,233 |

**Note 6. Commitments to Unico for Rainier Tower Sublease**

In 1995, the University assumed a sublease for a portion of the Rainier Tower Building, one of the Unico-controlled buildings on the Metropolitan Tract, and directly controlled approximately 380,000 square feet of office space referred to as the Rainier Tower Sublease ("Sublease"). As of October 31, 2014, the University directly controls the entire Rainier Tower Building; however, the Sublease remains in place until October 31, 2017. Unico managed the Sublease until October 31, 2014, when responsibilities were transferred to Wright Runstad.

Rent expense related to the Rainier Tower Sublease prior to November 1, 2014, was $2,480,353.

**Note 7. Cobb Building**

In July 2004, the University amended the existing Unico Lease (see Note 1) to exclude the Cobb Building. At the same time, the University entered into a new 45-year lease with Unico. The Cobb Lease provided for Unico to implement a $38.5 million redevelopment and conversion of the Cobb Building from obsolete medical office space to 92 rental residential units. In accordance with the new lease agreement, the University invested a total of approximately $7.9 million in the development. The Cobb Lease also included lease buyout rights in 2014, 2024, and 2034. On September 20, 2013, the University exercised its option to terminate its lease with Unico for the Cobb Building (and take possession of the leasehold improvements) effective October 31, 2015. The termination price of $33.4 million was calculated based on terms established in the Cobb Lease.

**Note 8. Palomar Garage**

In 1964, Unico purchased the property adjacent to the Cobb Building on the west side of the block. The acquisition of the property and the subsequent construction of the Palomar Garage structure were agreed to between Unico and the University, and the property was conveyed to the University at no cost on November 1, 2014.

**Note 9. Related Party Transactions**

Unico leased office space on the Metropolitan Tract to University departments during fiscal year 2015. The total rent-related amounts paid to Unico by University departments was $718,598 for the period ended October 31, 2014, which were subjected to the percentage rent received by the University. After the Unico Lease expired, the rent-related amounts paid by the University departments were reported as office rent, which amounted to $1,665,822 for the period from November 1, 2014, to June 30, 2015. The leases with University departments expire at various dates up through 2020.

**Note 10. Rainier Square Redevelopment**

As described in Note 1, the terms of the Predevelopment Agreement with WRC required WRC to place $2,500,000 into escrow. Release of the funds in escrow depends on the performance of certain development milestones carried out between WRC and the City of Seattle ("the City"). In November 2014, WRC filed a master use permit application ("MUP Application") with the City, triggering the release of $1.5 million from escrow. The remaining funds in escrow will be released in equal installments of $500,000 upon the City's approval of the MUP Application and issuance of a master use permit. The University will receive all or a portion of the remaining funds in the event that WRC does not secure a master use permit by June 30, 2017.

# SUPPLEMENTARY INFORMATION

**UNIVERSITY OF WASHINGTON METROPOLITAN TRACT**

DETAILS OF PROPERTY

June 30, 2015

| | Cobb Building | Skinner Building | Puget Sound Plaza | IBM Building | Rainier Tower * | Financial Center | Olympic Hotel | Olympic Garage | 2015 Total |
|---|---|---|---|---|---|---|---|---|---|
| Buildings, tenant improvements, and modernizations | | | | | | | | | |
| Buildings | $ 751,994 | $ 2,037,004 | $ 9,113,065 | $ 8,412,874 | $ 42,878,840 | $ 16,983,859 | $ 12,535,102 | $ 2,791,153 | $ 95,503,891 |
| Tenant improvements | | 7,855,042 | 10,040,864 | 9,987,838 | 21,966,146 | 11,170,624 | | | 61,020,514 |
| Modernizations | 43,207,399 | 18,342,015 | 16,620,572 | 13,732,739 | 18,959,411 | 13,323,178 | | | 124,185,314 |
| Construction in progress | | 205,924 | 2,289,643 | 255,184 | 112,105 | 1,524,723 | | | 4,387,579 |
| Furniture, fixtures, and equipment | | 2,738 | 10,950 | 30,196 | 21,900 | 44,571 | | | 110,355 |
| | 43,959,393 | 28,442,723 | 38,075,094 | 32,418,831 | 83,938,402 | 43,046,955 | 12,535,102 | 2,791,153 | 285,207,653 |
| Less accumulated depreciation and amortization | | | | | | | | | |
| Buildings | 751,994 | 2,037,004 | 8,366,318 | 8,412,874 | 27,513,921 | 12,030,232 | 9,671,376 | 2,372,471 | 71,156,190 |
| Tenant improvements | | 5,776,023 | 7,897,948 | 7,048,690 | 15,382,021 | 8,637,709 | | | 44,742,391 |
| Modernizations | 4,721,101 | 10,310,547 | 9,689,710 | 7,711,181 | 9,515,559 | 7,475,074 | | | 49,423,172 |
| Furniture, fixtures, and equipment | | 182 | 731 | 2,420 | 1,095 | 4,821 | | | 9,249 |
| | 5,473,095 | 18,123,756 | 25,954,707 | 23,175,165 | 52,412,596 | 28,147,836 | 9,671,376 | 2,372,471 | 165,331,002 |
| Net investment | $ 38,486,298 | $ 10,318,967 | $ 12,120,387 | $ 9,243,666 | $ 31,525,806 | $ 14,899,119 | $ 2,863,726 | $ 418,682 | 119,876,651 |
| Land | | | | | | | | | 9,974,594 |
| Land improvements | | | | | | | | | 793,423 |
| Less accumulated depreciation | | | | | | | | | (793,423) |
| Net land and land improvements | | | | | | | | | 9,974,594 |
| Net investment including land and land improvements | | | | | | | | | $ 129,851,245 |

* Includes Rainier Square