# UNIVERSITY OF PITTSBURGH

# FINANCIAL REPORT
# FISCAL YEAR 2010

**KPMG LLP**
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# Independent Auditors' Report

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

We have audited the accompanying consolidated balance sheet of the University of Pittsburgh of the Commonwealth System of Higher Education (the University) as of June 30, 2010 and the related consolidated statements of activities and cash flows for the year then ended. These consolidated financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The accompanying consolidated financial statements of the University as of and for the year ended June 30, 2009, were audited by other auditors whose report thereon dated October 30, 2009, except for note 16, which was as of October 14, 2010, expressed an unqualified opinion on those statements.

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 of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2010 consolidated financial statements referred to above present fairly, in all material respects, the financial position of the University of Pittsburgh of the Commonwealth System of Higher Education as of June 30, 2010, and the changes in their net assets and their cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

October 14, 2010

KPMG LLP, is a Delaware limited liability partnership,
the U.S. member firm of KPMG International Cooperative
("KPMG International"), a Swiss entity.

University of Pittsburgh
Consolidated Balance Sheets
as of June 30, 2010 and 2009
*(in thousands of dollars)*

| | 2010 | 2009 |
|---|---|---|
| **CURRENT ASSETS:** | | |
| Cash and cash equivalents | $ 175,362 | $ 210,436 |
| Operating investments *(Note 4)* | 155,717 | 63,658 |
| Accounts and notes receivable, net *(Note 2)* | 160,344 | 167,169 |
| Contributions receivable, net *(Note 3)* | 18,902 | 23,600 |
| Investments held under securities lending program *(Note 4)* | 89,988 | 63,853 |
| Other assets | 14,020 | 13,061 |
| **TOTAL CURRENT ASSETS** | 614,333 | 541,777 |
| **NONCURRENT ASSETS:** | | |
| Endowment investments *(Note 4)* | 2,048,024 | 1,868,203 |
| Operating investments *(Note 4)* | 432,578 | 230,429 |
| Accounts and notes receivable, net *(Note 2)* | 57,151 | 61,260 |
| Contributions receivable, net *(Note 3)* | 36,061 | 47,215 |
| Deposits with bond trustees | 126,999 | 195,956 |
| Investments in foundations | 21,703 | 20,983 |
| Other assets | 8,245 | 6,363 |
| Property, plant, and equipment, net *(Note 6)* | 1,581,433 | 1,511,197 |
| **TOTAL NONCURRENT ASSETS** | 4,312,194 | 3,941,606 |
| **TOTAL ASSETS** | $ 4,926,527 | $ 4,483,383 |

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

University of Pittsburgh
Consolidated Balance Sheets
as of June 30, 2010 and 2009
*(in thousands of dollars)*

| | 2010 | 2009 |
|---|---|---|
| **CURRENT LIABILITIES:** | | |
| Accounts payable | $ 76,576 | $ 78,294 |
| Accrued payroll and related liabilities | 68,810 | 65,352 |
| Deferred student and other revenue | 30,725 | 28,110 |
| Advanced receipt of sponsored research funds | 85,983 | 89,294 |
| Short-term debt *(Note 8)* | 239,268 | 119,621 |
| Current maturities of long-term debt *(Note 8)* | 135,989 | 29,900 |
| Liability under securities lending program *(Note 4)* | 89,988 | 63,853 |
| Other liabilities | 34,945 | 27,530 |
| **TOTAL CURRENT LIABILITIES** | 762,284 | 501,954 |
| **NONCURRENT LIABILITIES:** | | |
| Pension and postretirement obligations *(Note 10)* | 292,806 | 264,041 |
| Other employee benefits | 14,226 | 14,270 |
| Refundable U.S. government student loans | 31,829 | 33,530 |
| Long-term debt *(Note 8)* | 805,943 | 937,721 |
| Conditional asset remediation obligation *(Note 7)* | 38,303 | 35,107 |
| Other liabilities | 94,452 | 97,073 |
| **TOTAL NONCURRENT LIABILITIES** | 1,277,559 | 1,381,742 |
| **TOTAL LIABILITIES** | 2,039,843 | 1,883,696 |
| **NET ASSETS:** | | |
| Unrestricted | 1,874,399 | 1,650,640 |
| Temporarily restricted | 474,590 | 429,873 |
| Permanently restricted | 537,695 | 519,174 |
| **TOTAL NET ASSETS** | 2,886,684 | 2,599,687 |
| **TOTAL LIABILITIES AND NET ASSETS** | $ 4,926,527 | $ 4,483,383 |

UNIVERSITY OF PITTSBURGH
CONSOLIDATED STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2010
COMPARED TO SUMMARY INFORMATION FOR THE YEAR ENDED JUNE 30, 2009
*(in thousands of dollars)*

| | 2010 | | | | |
|---|---|---|---|---|---|
| **REVENUES:** | Unrestricted | Temporarily Restricted | Permanently Restricted | Total | 2009 |
| Tuition and fees | $ 600,772 | $ - | $ - | $ 600,772 | $ 562,773 |
| Tuition discounts | (143,451) | - | - | (143,451) | (136,639) |
| Net tuition | 457,321 | - | - | 457,321 | 426,134 |
| Commonwealth appropriation | 185,407 | - | - | 185,407 | 177,902 |
| Commonwealth grants and contracts | 36,147 | - | - | 36,147 | 31,598 |
| Research grants and contracts | 693,363 | - | - | 693,363 | 653,925 |
| Research grants and contracts - ARRA | 43,662 | - | - | 43,662 | - |
| Gifts and contributions | 31,845 | 5,498 | 16,670 | 54,013 | 54,663 |
| Endowment earnings | 15,151 | - | 1,989 | 17,140 | 22,491 |
| Investment income | 14,558 | - | 173 | 14,731 | 13,452 |
| Sales and services, educational and other | 121,919 | - | - | 121,919 | 100,601 |
| Sales and services, auxiliary | 124,798 | - | - | 124,798 | 119,099 |
| Rental revenue | 19,360 | - | - | 19,360 | 18,867 |
| Other | 77,269 | - | - | 77,269 | 63,907 |
| Net assets released from restrictions | 15,831 | (15,831) | - | - | - |
| **Total revenues** | 1,836,631 | (10,333) | 18,832 | 1,845,130 | 1,682,639 |
| **EXPENSES:** | | | | | |
| Salaries and wages | 796,200 | - | - | 796,200 | 762,140 |
| Fringe benefits | 240,684 | - | - | 240,684 | 225,215 |
| Total compensation | 1,036,884 | - | - | 1,036,884 | 987,355 |
| Supplies | 118,325 | - | - | 118,325 | 106,271 |
| Business and professional | 265,163 | - | - | 265,163 | 250,870 |
| Utilities | 54,661 | - | - | 54,661 | 55,320 |
| Maintenance and facilities | 41,024 | - | - | 41,024 | 38,770 |
| Depreciation | 122,886 | - | - | 122,886 | 116,778 |
| Interest | 55,306 | - | - | 55,306 | 40,371 |
| Other | 62,246 | - | - | 62,246 | 61,887 |
| **Total expenses** | 1,756,495 | - | - | 1,756,495 | 1,657,622 |
| **Revenues less expenses** | 80,136 | (10,333) | 18,832 | 88,635 | 25,017 |
| **OTHER ACTIVITIES:** | | | | | |
| Realized gains (losses) on investments | 42,218 | 17,515 | (12) | 59,721 | (122,524) |
| Unrealized gains (losses) on investments | 108,563 | 37,535 | (299) | 145,799 | (433,120) |
| Pension and postretirement changes other than net periodic cost | (7,158) | - | - | (7,158) | (9,922) |
| **Total other activities** | 143,623 | 55,050 | (311) | 198,362 | (565,566) |
| **CHANGE IN NET ASSETS** | 223,759 | 44,717 | 18,521 | 286,997 | (540,549) |
| **NET ASSETS, BEGINNING OF YEAR** | 1,650,640 | 429,873 | 519,174 | 2,599,687 | 3,140,236 |
| **NET ASSETS, END OF YEAR** | $ 1,874,399 | $ 474,590 | $ 537,695 | $ 2,886,684 | $ 2,599,687 |

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

University of Pittsburgh
Consolidated Statement of Activities
For the Year Ended June 30, 2009
*(in thousands of dollars)*

| | 2009 | | | |
|---|---|---|---|---|
| **REVENUES:** | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| Tuition and fees | $ 562,773 | $ - | $ - | $ 562,773 |
| Tuition discounts | (136,639) | - | - | (136,639) |
| Net tuition | 426,134 | - | - | 426,134 |
| Commonwealth appropriation | 177,902 | - | - | 177,902 |
| Commonwealth grants and contracts | 31,598 | - | - | 31,598 |
| Research grants and contracts | 653,925 | - | - | 653,925 |
| Gifts and contributions | 29,785 | 7,999 | 16,879 | 54,663 |
| Endowment earnings | 20,765 | - | 1,726 | 22,491 |
| Investment income | 13,340 | - | 112 | 13,452 |
| Sales and services, educational and other | 100,601 | - | - | 100,601 |
| Sales and services, auxiliary | 119,099 | - | - | 119,099 |
| Rental revenue | 18,867 | - | - | 18,867 |
| Other | 63,907 | - | - | 63,907 |
| Net assets released from restrictions | 19,721 | (19,721) | - | - |
| **Total revenues** | 1,675,644 | (11,722) | 18,717 | 1,682,639 |
| **EXPENSES:** | | | | |
| Salaries and wages | 762,140 | - | - | 762,140 |
| Fringe benefits | 225,215 | - | - | 225,215 |
| Total compensation | 987,355 | - | - | 987,355 |
| Supplies | 106,271 | - | - | 106,271 |
| Business and professional | 250,870 | - | - | 250,870 |
| Utilities | 55,320 | - | - | 55,320 |
| Maintenance and facilities | 38,770 | - | - | 38,770 |
| Depreciation | 116,778 | - | - | 116,778 |
| Interest | 40,371 | - | - | 40,371 |
| Other | 61,887 | - | - | 61,887 |
| **Total expenses** | 1,657,622 | - | - | 1,657,622 |
| **Revenues less expenses** | 18,022 | (11,722) | 18,717 | 25,017 |
| **OTHER ACTIVITIES:** | | | | |
| Realized losses on investments | (47,494) | (74,934) | (96) | (122,524) |
| Unrealized losses on investments | (225,174) | (207,769) | (177) | (433,120) |
| Pension and postretirement changes other than net periodic cost | (9,922) | - | - | (9,922) |
| **Total other activities** | (282,590) | (282,703) | (273) | (565,566) |
| **CHANGE IN NET ASSETS** | (264,568) | (294,425) | 18,444 | (540,549) |
| **RECLASSIFICATION OF NET ASSETS** | - | (21,052) | 21,052 | - |
| **NET ASSETS, BEGINNING OF YEAR** | 1,915,208 | 745,350 | 479,678 | 3,140,236 |
| **NET ASSETS, END OF YEAR** | $ 1,650,640 | $ 429,873 | $ 519,174 | $ 2,599,687 |

University of Pittsburgh
Consolidated Statements of Cash Flows
For the Years Ended June 30, 2010 and 2009
*(in thousands of dollars)*

| | 2010 | 2009 |
|---|---|---|
| **CASH AND CASH EQUIVALENTS AT:** | | |
| End of year | $ 175,362 | $ 210,436 |
| Beginning of year | 210,436 | 36,999 |
| **CHANGE IN CASH AND CASH EQUIVALENTS** | $ (35,074) | $ 173,437 |
| **CASH FLOWS FROM OPERATING ACTIVITIES:** | | |
| Change in net assets | $ 286,997 | $ (540,549) |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation | 122,886 | 116,778 |
| Amortization | (3,694) | (1,776) |
| Loss on disposal of plant assets | 2,048 | 2,073 |
| Realized (gains) losses on investments | (59,721) | 122,524 |
| Unrealized (gains) losses on investments | (145,799) | 433,120 |
| Contributions restricted for long-term investment | (57,342) | (56,457) |
| Changes in operating assets and liabilities: | | |
| Accounts, notes, and contributions receivable, net | 27,745 | (4,491) |
| Other assets | (2,841) | (3,786) |
| Accounts payable | 252 | (1,873) |
| Pension and postretirement obligations | 29,481 | 29,760 |
| Conditional asset remediation obligation | 3,196 | (1,986) |
| Other accrued liabilities | 2,253 | 11,114 |
| Government student loans and deferred revenue | (2,397) | 8,812 |
| **Net cash provided by operating activities** | 203,064 | 113,263 |
| **CASH FLOWS FROM INVESTING ACTIVITIES:** | | |
| Expended for property, plant, and equipment - University | (159,023) | (179,771) |
| Expended for property, plant, and equipment - commonwealth | (36,147) | (31,598) |
| Change in accounts payable for property, plant, and equipment | (1,970) | 1,785 |
| Change in investments under securities lending program | (26,135) | 139,412 |
| Change in liability under securities lending program | 26,135 | (139,412) |
| Net purchases/sales of nonendowment investments | (92,154) | 11,102 |
| Purchases of endowment investments | (1,559,701) | (1,479,908) |
| Proceeds from sales/maturities of endowment investments | 1,387,626 | 1,548,474 |
| Change in investments in foundations | (720) | 2,834 |
| **Net cash used for investing activities** | (462,089) | (127,082) |
| **CASH FLOWS FROM FINANCING ACTIVITIES:** | | |
| Principal repayment of debt | (29,900) | (155,379) |
| Proceeds from issuance of debt | 127,552 | 459,377 |
| Change in deposits with bond trustees | 68,957 | (173,199) |
| Contributions restricted for long-term investment | 57,342 | 56,457 |
| **Net cash provided by financing activities** | 223,951 | 187,256 |
| **CHANGE IN CASH AND CASH EQUIVALENTS** | $ (35,074) | $ 173,437 |
| **Supplemental disclosure of cash flow information:** | | |
| **Cash paid for interest (excluding fees)** | $ 57,227 | $ 36,565 |
| **Noncash investing activity for property, plant, and equipment—accounts payable** | $ 27,869 | $ 29,839 |

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

## Note 1: Summary of Significant Accounting and Reporting Practices

**Organization**
Founded in 1787, the University of Pittsburgh of the Commonwealth System of Higher Education (the University) is an institution of higher education with a three-pronged mission to provide the highest-quality instruction for its students; engage in innovative research activities; and support the state and local community through public service programs. In its 223 year history, the University has evolved into an internationally recognized center of learning and research. The University's Oakland campus in the City of Pittsburgh is comprised of 16 schools and several academic centers educating more than 28,000 students in various undergraduate, graduate, and first professional programs. Four regional campuses with a total enrollment of over 7,000 students are located throughout western Pennsylvania.

**Relationship with the Commonwealth of Pennsylvania**
The University derives its corporate existence under the laws of the Commonwealth of Pennsylvania (the commonwealth) by reason of the act of the General Assembly of the commonwealth establishing an "Academy or Public School in the town of Pittsburgh" on February 28, 1787 and from the act of February 18, 1819 incorporating the "Western University of Pennsylvania." On July 11, 1908, the University's name was changed to the "University of Pittsburgh" by order of the Court of Common Pleas of Allegheny County. On July 28, 1966, the Pennsylvania State Legislature enacted the "University of Pittsburgh-Commonwealth Act" (the Act), which changed the name of the University to the "University of Pittsburgh – of the Commonwealth System of Higher Education" and established the University as an instrumentality of the commonwealth to serve as a state-related institution in the commonwealth system of higher education. The University is a Pennsylvania nonprofit corporation subject to the Nonprofit Corporation Law of 1988.

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

As a state-related institution, the University receives an annual operating appropriation from the commonwealth. The appropriation is subject to the commonwealth's annual budget process. There is no assurance that such appropriation will continue to be made, or will be made, at current levels or at levels requested by the University. The appropriation from the commonwealth was $185.4 million in 2010 and $177.9 million in 2009. In addition, in 2010 the University received $8.6 million from the commonwealth for 2009 stabilization, which is included in other revenues in the Consolidated Statement of Activities. Amounts received from the commonwealth are subject to an annual audit by the auditor general of the commonwealth.

In addition to the annual appropriation, the commonwealth also funds certain capital projects in support of the University's academic mission. Amounts funded by the commonwealth for capital projects were $36.1 million in 2010 and $31.6 million in 2009.

**Basis of Presentation**
The consolidated financial statements include the accounts of the University and the net assets of three regional campus foundations. These consolidated financial statements do not include the net assets or activities of the University of Pittsburgh Medical Center (UPMC) or the University of Pittsburgh Physicians (UPP) clinical practice plans, as they are separate legal entities not controlled by the University. The University does have the right to designate one-third of the members of the UPMC Governing Board and its Executive Committee. All significant intercompany balances and transactions have been eliminated in consolidation.

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

In accordance with GAAP, the University's net assets have been classified as either unrestricted, temporarily restricted, or permanently restricted based upon the existence or absence of donor-imposed restrictions. Unrestricted net assets are not subject to donor-imposed restrictions and are used for the general operating purposes of the University. This category also includes certain gifts and endowment earnings whose donor-imposed restrictions have been met within the fiscal year. Temporarily restricted net assets are subject to certain time or event restrictions by the donor. Upon satisfaction of these restrictions, the net assets are transferred to unrestricted. Temporarily restricted net assets at June 30, 2010 and 2009 consist of endowment balances ($441.0 million and $386.0 million, respectively); the net present value of unconditional promises to give ($27.6 million and $38.1 million, respectively), and split-interest agreements ($6.0 million and $5.8 million, respectively). Permanently restricted net assets are those subject to permanent donor-imposed restrictions and at June 30, 2010 and 2009 and consist of endowment balances ($499.2 million and $476.3 million, respectively); unconditional promises to give ($27.4 million and $32.7 million, respectively); and private loan funds ($11.1 million and $10.2 million, respectively). Reclassifications due to changes or clarifications in donor intentions are reflected accordingly in the Consolidated Statements of Activities.

Endowed gifts require that the original corpus of the gifts be maintained in perpetuity. The spending distributions from earnings generated by these gifts may be either expended or added to principal, in accordance with donor restrictions and gift policies.

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

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

Tuition discounts are recorded to the extent that either institutional financial aid or aid funded by gifts, endowment earnings, and research activities is awarded. Tuition discounts attributable to institutional funds in 2010 and 2009 are $121.9 million and $114.8 million, respectively. Tuition discounts attributable to restricted gifts, endowment earnings, and research activities in 2010 and 2009 are $21.6 million and $21.8 million, respectively.

Certain amounts for 2009 have been reclassified to conform to the current year presentation. The changes included (1) the recording of both a current asset and current liability for the securities lending program; (2) the reclassification of net purchases/sales of nonendowment investments from operating activities to investing activities on the Consolidated Statements of Cash Flows; and (3) the addition of property, plant, and equipment expenditures funded by the commonwealth into the amounts restricted for long-term investment in both operating and financing activities in the Consolidated Statements of Cash Flows.

**Cash and Cash Equivalents and Operating Investments**

Cash equivalents include investments with original maturities of three months or less and all assets invested in the University's short-term investment fund, which the University utilizes to fund daily cash needs. The fund currently invests in short-term Treasury securities and other short-term, highly-liquid investments, all of which can be liquidated within 7 days. All investments held in the fund must be rated A3/A-1 or better by Moody's Investor Service or A-/P-1 by Standard & Poors at the time of purchase. The fund is expected to generate a return approximating or exceeding the 3-month Treasury bill rate.

At June 30, 2010, $78.0 million is included in cash and cash equivalents and was used for the refunding of the 2007 PANTHER Notes on August 1, 2010 (refer to Note 8). Approximately $127.0 million of cash equivalents represent unspent bond proceeds and are reflected in the Consolidated Balance Sheets as deposits with bond trustees.

Cash and cash equivalents that are part of endowment investments are shown therewith as these funds are not used for operating needs. Current operating investments represent investments with original maturities greater than three months but less than 12 months. These current investments include obligations of the U.S. government and government agencies, bank certificates, commercial paper, corporate notes, and domestic equities. The noncurrent portion of operating investments are held for operating purposes, but have maturities greater than 12 months. Operating investments are reported at fair value generally based on quoted market prices.

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

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

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

**Derivative Financial Instruments**
The University records derivatives at fair value with changes in fair value reflected in the Consolidated Statements of Activities (see Note 9).

**Contributions**
The University records unconditional promises to give (which are agreements with donors involving nonreciprocal transfers of cash, other assets, or services) as either temporarily restricted or permanently restricted dependent upon the nature of the donor-imposed restrictions. Gifts whose restrictions are met in the same fiscal year as receipt are combined and reported with unrestricted gifts.

Unconditional promises to give made to the University are for the support of various schools and programs, including endowments for programs, faculty salaries, scholarships, and the renovation and expansion of physical facilities.

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

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

**Investments in Foundations**
The University's investments in foundations include the Bradford Educational Foundation, the Johnstown Educational Foundation, and the UPG (University of Pittsburgh at Greensburg) Foundation (the foundations). The purpose of the foundations is to receive, adminis-

ter, and distribute property exclusively for the benefit of each respective regional campus. Each foundation is governed by a board, with a majority of members being non-University employees. As such, the University does not exercise control of the foundations. However, due to the foundations being financially interrelated to the University, the University recognizes the net assets and its share of the annual change in net assets of the foundations.

**Property, Plant, and Equipment**
Property, plant, and equipment is recorded at cost, or if acquired by gift, at fair value at the date of the gift. Depreciation is calculated using the straight-line method. Useful lives generally range from 15 to 40 years for buildings and improvements and 5 to 10 years for furnishings and equipment. As assets are retired, sold, or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and gains or losses are recognized in the consolidated financial statements. Costs associated with the construction of new facilities and renovation and expansion of existing facilities are capitalized within construction in progress until such projects are placed in service. The University capitalizes software and related implementation costs and generally depreciates such assets over 5 to 10 years. Works of art, historical treasures, and similar assets include a variety of paintings, sculptures, photographs, antiques, and furnishings, as well as scholarly papers and archives. These assets are used for public exhibition, the preservation of artifacts and antiques for future generations, and scholarly research. Due to their nature, these assets are not depreciated. Library books, which include hard copy publications, periodicals, and electronic publications with rights to archival content, are depreciated over a period of 7 years. Maintenance and repairs are expensed as incurred.

**Insurance Liabilities**
The University is self-insured through an agreement with UPMC to provide medical coverage for its employees. A liability for estimated incurred but unreported claims of \$5.6 million and \$5.2 million has been recorded at June 30, 2010 and 2009, respectively, based upon management's analysis of claims history. This liability is reflected in accrued payroll and related liabilities in the Consolidated Balance Sheets.

The University is also self-insured for certain other activities, including workers' compensation, unemployment compensation, and litigation reserves. Liabilities have been established for these programs based on third-party administrators' estimates using the University's historical loss experience. The self-insurance accrual is subject to periodic adjustment by the University based on actual loss experience factors. Liabilities for these other self-insured obligations aggregated \$13.2 million as of June 30, 2010 and 2009, and are included in other employee benefits on the Consolidated Balance Sheets.

**Split-Interest Agreements**
Included in other noncurrent liabilities as of June 30, 2010 and 2009 is \$9.4 million of liabilities for split-interest agreements. These agreements with donors consist primarily of charitable gift annuities, pooled income funds, and irrevocable charitable remainder trusts for which the University serves as trustee. Assets are invested and payments are made to donors and/or other beneficiaries in accordance with the respective agreements.

**Research**
The University conducts sponsored research and development with various sponsors including agencies and departments of the federal government, the commonwealth, local government entities, companies, and foundations. Sponsored research activity in 2010 and 2009 is \$737.0 million and \$653.9 million, respectively, with approximately 63% of the funding awarded through the National Institutes of Health. Research grants and contracts - ARRA represents funding received through the American Recovery and Reinvestment Act of 2009. Most University research activity is incurred on a cost reimbursable basis with the University receiving funding after the related expenses have been incurred. Certain sponsors, however, provide research funding in advance of related expenses, and such funding is recorded as advanced receipt of sponsored research funds on the Consolidated Balance Sheets. Revenue on research awards is recognized as the related expenses are incurred.

The University incurs both direct and indirect costs in the conduct of its research. Recovery of indirect costs through federal awards is based upon predetermined rates negotiated with the Department of Health and Human

Services. Indirect cost recovery rates from nonfederal sources may vary. Funds received through federal sources are subject to audit each year in accordance with the Office of Management and Budget Circular A-133.

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

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

**Tax-exempt Status**
The University is exempt from federal income tax under Section 501(c)(3) of the United States Internal Revenue Code. Accordingly, no provision for income taxes has been reflected in the consolidated financial statements.

**New Accounting Standards**
In March 2008, the FASB issued new authoritative guidance that changes the disclosure requirements for derivative instruments and hedging activities. Entities are required to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how an entity accounts for derivative instruments and related hedged items, and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. The University adopted this new guidance for 2010 (see Note 9).

In December 2008, the FASB issued new authoritative guidance related to disclosure of pension and postretirement assets. This new guidance requires additional disclosures about plan assets including expanded disclosures on investment strategies, major categories of plan assets, the effect of fair value measurements using significant unobservable inputs on changes in plan assets, and significant concentrations of risk within plan assets. This new guidance is effective for the year ended June 30, 2010 (see Note 10).

In April 2009, the FASB issued a standard on *Mergers and Acquisitions for Not-for-Profit Entities.* This standard provides guidance on improving the quality of information in financial reports provided by a not-for-profit organization regarding business combinations with one or more other not-for-profit entities, businesses, or not-for-profit activities. Guidance will distinguish mergers (carryover method) from acquisitions (acquisition method), as well as improve accounting and reporting of goodwill and intangible assets after an acquisition. This standard is effective for the fiscal year ending June 30, 2011. The University is still evaluating the impact of this standard.

In September 2009, the FASB issued ASU 2009-12 (Topic 820), *Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. The guidance permits, as a practical expedient, an entity holding investments in certain entities that calculate NAV per share or its equivalent NAV to estimate the fair value of such investments on the basis of the reported NAV without adjustment. ASU 2009-12 requires additional disclosures regarding these investments. ASU 2009-12 was adopted by the University in 2010 and applies to indirect holdings in both privately and publicly traded assets via University interests in nonpublicly traded funds, including nonmarketable alternatives (e.g., private equity and venture capital), private real asset funds (e.g., real estate, energy, timber, and other natural resources), and marketable alternatives or hedge funds. The fair values estimated using NAV may differ significantly from the fair values that may be determined if a ready market were to exist for these funds (see Note 4).

**Subsequent Events**
The University has evaluated subsequent events through October 14, 2010, the date on which the consolidated financial statements were issued, and determined that there were no subsequent events requiring disclosure or adjustment to the consolidated financial statements.

## NOTE 2: ACCOUNTS AND NOTES RECEIVABLE, NET

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

| | 2010 | | 2009 | |
|---|---|---|---|---|
| | Current | Noncurrent | Current | Noncurrent |
| | *(in thousands of dollars)* | | | |
| Sponsored research receivables, net of allowance for doubtful accounts of $1,280 in 2010 and $1,444 in 2009 | $ 91,551 | $ - | $ 98,894 | $ - |
| Plant construction receivables | 17,829 | - | 12,367 | - |
| Hospitals and affiliated organizations, net of allowance for doubtful accounts of $945 in 2010 and $946 in 2009 | 11,429 | - | 20,802 | - |
| Student receivables, net of allowance for doubtful accounts of $1,799 in 2010 and 2009 | 8,748 | - | 7,964 | - |
| Student loan receivables, net of allowance for doubtful accounts of $1,447 in 2010 and $1,695 in 2009 | 6,653 | 41,063 | 6,155 | 46,102 |
| Accrued interest income receivables | 2,973 | - | 2,499 | - |
| Receivable on endowed funds held by third parties | 438 | 16,081 | 409 | 15,151 |
| Other, net of allowance for doubtful accounts of $193 in 2010 and $218 in 2009 | 20,723 | 7 | 18,079 | 7 |
| **Total accounts and notes receivable, net** | $ 160,344 | $ 57,151 | $ 167,169 | $ 61,260 |

## Note 3: Contributions Receivable, Net

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

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| Amounts due in: | | |
| Less than one year | $ 22,648 | $ 25,778 |
| One to five years | 35,654 | 47,662 |
| Greater than five years | 6,497 | 8,095 |
| Gross contributions receivable | 64,799 | 81,535 |
| Less: | | |
| Allowance for uncollectibles | (6,662) | (5,085) |
| Unamortized discounts | (3,174) | (5,635) |
| **Total contributions receivable, net** | $ 54,963 | $ 70,815 |
| Current | $ 18,902 | $ 23,600 |
| Noncurrent | 36,061 | 47,215 |
| **Total** | $ 54,963 | $ 70,815 |

The current yields for one- to 10-year U.S. Treasury notes are used to discount contributions receivable. Outstanding conditional promises to give to the University total $3.7 million and $4.8 million at June 30, 2010 and 2009, respectively, which are dependent upon the fulfillment of certain conditions and, therefore, are not included in the consolidated financial statements.

The University has been named as beneficiary in the wills of numerous donors totaling $87.6 million and $72.4 million at June 30, 2010 and 2009, respectively. These bequests are considered to be intentions to give and, therefore, are not included in the consolidated financial statements.

Note 4: Investments

Investments comprise the following at June 30:

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| Endowment investments: | | |
| Pooled | $ 2,024,149 | $ 1,844,880 |
| Nonpooled | 23,875 | 23,323 |
| Subtotal endowment investments | 2,048,024 | 1,868,203 |
| Current operating investments | 155,717 | 63,658 |
| Noncurrent operating investments | 432,578 | 230,429 |
| **Total investments** | $ 2,636,319 | $ 2,162,290 |
| Composition of endowment investments: | | |
| Cash and cash equivalents | $ 32,131 | $ 47,717 |
| Domestic equities | 279,102 | 277,347 |
| International equities | 399,581 | 332,245 |
| U.S. government and government agencies' securities, bank acceptances and certificates, and commercial paper | 114,361 | 124,055 |
| Corporate bonds and other obligations | 100,017 | 84,605 |
| Alternative investment funds and partnerships: | | |
| Marketable alternatives | 338,831 | 329,045 |
| Real assets | 341,372 | 311,581 |
| Private equities/venture capital | 407,779 | 326,758 |
| Other | 34,850 | 34,850 |
| **Total endowment investments** | $ 2,048,024 | $ 1,868,203 |
| Composition of current and noncurrent operating investments: | | |
| U.S. government and government agencies' securities, bank acceptances and certificates, and commercial paper | $ 504,884 | $ 236,826 |
| Corporate bonds and other obligations | 70,038 | 42,505 |
| Other | 13,373 | 14,756 |
| **Total current and noncurrent operating investments** | $ 588,295 | $ 294,087 |

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

The philosophies and policies employed in the management of the endowment are long-term by definition, as they are based on the expectation that the University will have an infinite life and will continue to provide financial support in perpetuity. Accordingly, the University's investment policy is intended to optimize long-term total return—income plus capital appreciation—relative to the level of risk taken.

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

The following table lists the University's investments as of June 30, 2010 for which NAV was employed to estimate fair value.

| Asset Class | Investment | Fair Value Determined using NAV | Unfunded Commitments |
|---|---|---|---|
| | | *(in thousands of dollars)* | |
| Domestic Equities | Long/Short Domestic Equity Fund | $ 47,804 | $ - |
| Emerging Markets Equities | Commingled Emerging Markets Fund | 53,535 | - |
| Fixed Income | High Yield Debt - Redeemable | 8,585 | - |
| Marketable Alternatives | Distressed Debt - Redeemable | 38,982 | - |
| | Distressed Debt - Nonredeemable | 80,566 | 4,000 |
| | Multi-Strategy/Arbitrage | 89,231 | - |
| | Long/Short Equity | 130,052 | - |
| | Total Marketable Alternatives | 338,831 | 4,000 |
| Nonmarketable Alternatives | Private Equity Funds | 255,866 | 192,742 |
| | Venture Capital Funds | 151,913 | 102,937 |
| | Total Nonmarketable Alternatives | 407,779 | 295,679 |
| Real Assets | Real Assets - Redeemable | 50,173 | - |
| | Private Real Estate Funds | 110,741 | 97,814 |
| | Private Energy Funds | 126,565 | 50,467 |
| | Private Timber Funds | 53,893 | 3,978 |
| | Total Real Assets | 341,372 | 152,259 |
| | **Total** | $ 1,197,906 | $ 451,938 |

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

**Long/Short Domestic Equity Fund**
The University's investment is an interest in a commingled fund that is fully redeemable without penalty as of any quarter-end with 60-day notice. The fund holds both long and short positions of publicly traded common equities.

**Commingled Emerging Markets Fund**
The University's investments are in two commingled funds managed by the same investment manager. Both funds hold publicly traded emerging market equities, with one holding mid and large cap stocks and the other holding small cap stocks. Both interests may be liquidated without penalty within 120 days of providing a month-end notice.

**High Yield Debt – Redeemable**
The University's investment is an interest in a commingled fund that is fully redeemable without penalty at any month-end with 10-day notice. The fund holds publicly traded high yield debt and bank loans.

**Distressed Debt – Redeemable**
The University's investments are in two commingled funds. Both funds are hedge funds that hold both long and short positions in mostly publicly traded, and some privately traded, distressed debt securities (i.e., the securities trade at significant discounts to their par value). The University's interest in one of the funds is redeemable without penalty on a quarterly basis with 90-day notice beginning April 1, 2012. The University's interest in the other fund may be redeemed without penalty in annual 20% increments (i.e., over a period of five years).

**Distressed Debt – Nonredeemable**
The University's investments are interests in a total of 11 commingled funds managed by four different investment managers. All of the funds hold distressed securities traded publicly and/or privately, and all have investment periods of three years or longer, during which committed capital may be called. The University's interests in the funds are reduced typically over multi-year periods as the managers return invested capital and distribute proceeds realized from underlying fund assets.

**Multi-Strategy/Arbitrage**
The University's investments are interests in four commingled funds. These funds are hedge funds that hold both long and short positions in equities, fixed income, and financial derivatives. The University's interests in three of the funds may be liquidated without penalty on an annual basis (in one case, beginning September 30, 2012) with 30-45 day notice. The University's interest in the fourth fund may be liquidated without penalty on a quarterly basis with 30-day notice.

**Long/Short Equity**
The University's investments are interests in eight commingled funds. These funds are hedge funds that hold both long and short positions in publicly traded global equities. The University's interests in all but one of the funds may be liquidated without penalty on a quarterly or monthly basis with 30-45 day notice; its interest in the other fund is redeemable without penalty with 60-day notice every three years for 80% of the assets and on a quarterly basis beginning April 1, 2011 for the remaining 20% of the assets.

**Private Equity Funds**
The University's investments are interests in 57 commingled funds. These funds are private equity funds that are invested in equity and equity-like securities of mostly nonpublicly traded companies over periods of typically three to five years, during which committed capital may be called. The University's interests in private equity funds are considered to be relatively illiquid in that they are not easily transferrable and typically achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds realized from underlying fund assets.

**Venture Capital Funds**
The University's investments are interests in 45 commingled funds. These funds are venture capital funds, a specialized type of private equity, and are invested in equity and equity-like securities of mostly nonpublicly traded, immature companies over periods of typically three to five years, during which committed capital may be called. The University's interests in venture capital funds are considered to be illiquid in that they are in riskier assets, they are not easily transferrable, and they typically can only achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds from the underlying fund assets.

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

**Private Real Estate Funds**
The University's investments are interests in 24 commingled funds. These funds are private real estate funds that are primarily invested in privately traded real estate-related properties and interests, including interests in companies engaged in real estate operations. These funds are invested over periods of typically three to five years, during which committed capital may be called. The University's interests in private real estate funds are considered to be relatively illiquid in that they are not easily transferrable and typically achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds realized from underlying fund assets.

**Private Energy Funds**
The University's investments are interests in 21 commingled funds. These funds are private energy funds that are primarily invested in privately traded energy-related properties and interests, including interests in oil and gas and other fossil fuel reserves, production, storage, and

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

**Private Timber Funds**

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

Through an agreement with its primary investment custodian, the University makes available its securities for loan to borrowers identified by the custodian. Collateral posted by the borrower for the benefit of the University is generally limited to cash, government securities, and irrevocable letters of credit. Both the custodian and the borrower have the right to terminate a loan at any time. In exchange for lending a security, the University receives a fee and continues earning applicable interest and dividends on the loaned security. As of June 30, 2010 and 2009, the University held $90.0 million and $63.9 million, respectively, of cash and cash equivalents as collateral deposits for securities on loan. Collateral held by the University is shown as an asset, and the obligation to return the collateral when the loan is terminated is presented as a liability in the Consolidated Balance Sheets. The total securities on loan had an estimated fair value of $87.0 million and $61.7 million at June 30, 2010 and 2009, respectively.

Operating investments are primarily managed by the University and used for general operating purposes.

## Note 5: Fair Value Measurements

In July 2008, the University adopted Accounting Standards Codification (ASC) 820, *Fair Value Measurements and Disclosures,* which establishes a single authoritative definition of fair value, sets a framework for measuring fair value, and requires additional disclosures about fair value measurements. In accordance with ASC 820, fair value is defined as the price that the University would receive upon selling an asset or the price paid to transfer a liability (exit price) in an orderly transaction between market participants in the principal or, in the absence of a principal market, most advantageous market at the measurement date.

The principal market is the market in which the reporting entity would sell the asset or transfer the liability with the greatest volume and level of activity for the asset or liability. The most advantageous market is the market in which the reporting entity would maximize the amount received for an asset or minimize the amount paid to transfer a liability.

ASC 820 established a three-tier hierarchy, based on inputs to fair value measurements for disclosure purposes. Inputs may be observable or unobservable and refer broadly to the assumptions that market participants would use in pricing an asset or liability, including assumptions about risk.

The three-tier hierarchy of inputs is summarized in the three broad levels below:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets that the University has the ability to access at the measurement date. This level of the fair value hierarchy provides the most reliable evidence of fair value and is used to measure fair value whenever available. Instruments valued by Level 1 measures primarily consist of directly held securities that are actively traded in public markets.

- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs include quoted prices for similar investments in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable; and inputs that are derived from observable market data by correlation or other means. Instruments valued by Level 2 measures include University holdings in certain structured debt obligations, University interests in certain commingled investment funds, interest rate swap agreements, and other thinly-traded instruments.

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

University fund investments for which NAV is used to estimate fair value are classified as either Level 2 or 3 assets in the fair value hierarchy, depending on the fair value tier in which the underlying fund assets would fall and the University's ability to redeem its interest in the fund. If the underlying fund assets are publicly traded securities for which there exists a broad, active market, and the University's interest can be redeemed without penalty within the near term, the University's interest in the fund is classified as a Level 2 investment. If the underlying fund assets are privately traded and/or the University's interest cannot be redeemed without penalty generally within 90 days, the University's interest in the fund is classified as a Level 3 investment. The classification of investments in the fair value hierarchy is not necessarily an indication of the risks, liquidity, or degree of difficulty in determining fair value.

The following table summarizes the inputs used as of June 30, 2010 in valuing the University assets and liabilities carried at fair value:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | *(in thousands of dollars)* | | | |
| Assets | | | | |
| Endowment investments: | | | | |
| Cash and cash equivalents | $ 23,802 | $ 8,329 | $ - | $ 32,131 |
| Domestic equities | 188,353 | 90,749 | - | 279,102 |
| International equities | 335,165 | 54,318 | 10,098 | 399,581 |
| U.S. government, corporate bonds, and other obligations | 145,419 | 58,164 | 10,795 | 214,378 |
| Marketable alternatives | - | 128,805 | 210,026 | 338,831 |
| Real assets | - | 48,735 | 292,637 | 341,372 |
| Private equities | - | - | 407,779 | 407,779 |
| Other | - | - | 34,850 | 34,850 |
| Operating investments: | | | | |
| U.S. government, corporate bonds, and other obligations | 545,449 | 29,473 | - | 574,922 |
| Other | 792 | - | 12,581 | 13,373 |
| Deposits with bond trustees | 92,163 | 34,836 | - | 126,999 |
| **Total assets** | $ 1,331,143 | $ 453,409 | $ 978,766 | $ 2,763,318 |
| Liabilities | | | | |
| **Interest rate swaps** | $ - | $ 60,927 | $ - | $ 60,927 |

The following table summarizes the inputs used as of June 30, 2009 in valuing the University assets and liabilities carried at fair value:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | *(in thousands of dollars)* | | | |
| Assets | | | | |
| Endowment investments: | | | | |
| Cash and cash equivalents | $ 290 | $ 47,427 | $ - | $ 47,717 |
| Domestic equities | 114,540 | 162,807 | - | 277,347 |
| International equities | 282,201 | 35,228 | 14,816 | 332,245 |
| U.S. government, corporate bonds, and other obligations | 158,337 | 45,998 | 4,325 | 208,660 |
| Marketable alternatives | - | 87,773 | 241,272 | 329,045 |
| Real assets | - | 42,460 | 269,121 | 311,581 |
| Private equities | - | - | 326,758 | 326,758 |
| Other | - | - | 34,850 | 34,850 |
| Operating investments: | | | | |
| U.S. government, corporate bonds, and other obligations | 258,483 | 20,848 | - | 279,331 |
| Other | 3,240 | - | 11,516 | 14,756 |
| Deposits with bond trustees | 100,000 | 95,956 | - | 195,956 |
| **Total assets** | $ 917,091 | $ 538,497 | $ 902,658 | $ 2,358,246 |
| Liabilities | | | | |
| **Interest rate swaps** | $ - | $ 55,688 | $ - | $ 55,688 |

The following tables summarize the change in the Level 3 activity for the years ended June 30, 2010 and 2009:

2010

*(in thousands of dollars)*

| | International Equities | U.S. Government Corporate and Other | Marketable Alternatives | Real Assets | Private Equities | Other | Total |
|---|---|---|---|---|---|---|---|
| Balance - June 30, 2009 | $ 14,816 | $ 4,325 | $ 241,272 | $ 269,121 | $ 326,758 | $ 46,366 | $ 902,658 |
| Capital calls/purchases | 6,530 | 6,344 | 22,698 | 48,312 | 68,960 | 1,203 | 154,047 |
| Distributions/sales | (4,241) | (296) | (45,488) | (26,545) | (31,566) | (215) | (108,351) |
| Transfers in (out) | (9,806) | - | (55,650) | - | - | - | (65,456) |
| Realized gains | 586 | - | - | - | - | - | 586 |
| Unrealized gains | 2,213 | 422 | 47,194 | 1,749 | 43,627 | 77 | 95,282 |
| **Balance - June 30, 2010** | $ 10,098 | $ 10,795 | $ 210,026 | $ 292,637 | $ 407,779 | $ 47,431 | $ 978,766 |

2009

*(in thousands of dollars)*

| | International Equities | U.S. Government Corporate and Other | Marketable Alternatives | Real Assets | Private Equities | Other | Total |
|---|---|---|---|---|---|---|---|
| Balance - June 30, 2008 | $ 16,895 | $ 4,589 | $ 203,577 | $ 268,262 | $ 342,792 | $ 12,981 | $ 849,096 |
| Capital calls/purchases | 6,388 | 60 | 70,250 | 51,340 | 68,427 | 934 | 197,399 |
| Distributions/sales | (4,106) | (296) | (14,545) | (22,502) | (10,500) | (588) | (52,537) |
| Transfers in (out) | (101) | - | - | - | - | 69,701 | 69,600 |
| Realized losses | (2,485) | - | - | - | - | - | (2,485) |
| Unrealized losses | (1,775) | (28) | (18,010) | (27,979) | (73,961) | (36,662) | (158,415) |
| **Balance - June 30, 2009** | $ 14,816 | $ 4,325 | $ 241,272 | $ 269,121 | $ 326,758 | $ 46,366 | $ 902,658 |

Gains and losses (realized and unrealized) for Level 3 activity are reported in other activities in the Consolidated Statements of Activities. The unrealized gains (losses) related to investments held as of June 30, 2010 and 2009 were $95.3 million and $(158.3) million, respectively.

## Note 6: Property, Plant, and Equipment, Net

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

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| Land | $ 51,255 | $ 48,130 |
| Buildings and improvements | 2,127,243 | 2,014,815 |
| Equipment | 578,005 | 553,063 |
| Library books | 216,969 | 206,399 |
| Works of art, historical treasures, and similar assets | 14,668 | 14,572 |
| Construction in progress | 263,879 | 241,840 |
| Subtotal | 3,252,019 | 3,078,819 |
| Less: Accumulated depreciation | (1,670,586) | (1,567,622) |
| **Total property, plant, and equipment, net** | $ 1,581,433 | $ 1,511,197 |

In 2010, the University expended $195.2 million for property, plant, and equipment, of which $36.1 million was funded by the commonwealth. The combined additions included $31.7 million for renovations to Benedum Hall; $30.6 million for operating equipment; $17.4 million for the Petersen Sports Complex; $12.3 million for continued renovations to the Chevron Science Center; $10.6 million for library acquisitions; $6.8 million for continued renovations at the Falk School; $4.2 million for the Johnstown Campus Recreation Building addition; $3.8 million for construction of a new dorm at the Bradford Campus; $3.0 million for the Salk Hall addition; $2.9 million for continued renovations to the University Club; $2.2 million for the renovation of Fisher Hall at the Bradford Campus; $2.1 million for renovations to 7500 Thomas Boulevard; $2.1 million for the South Loop Steam distribution; and $2.0 million for the Allen Hall Mid-Campus Emergency Research Generator.

In 2009, the University expended $211.4 million for property, plant, and equipment, of which $31.6 million was funded by the commonwealth. The combined additions included $37.5 million for renovations to Benedum Hall; $22.7 million for operating equipment; $13.3 million for renovations at the University Club; $13.2 million for the acquisition and development of the property for the Petersen Sports Complex; $11.3 million for renovations and an addition at the Falk School; $10.3 million for library acquisitions; $9.3 million for an addition and renovations to the Chevron Science Center; $8.7 million for the Langley Hall mechanical systems and infrastructure upgrades; $6.0 million for renovations to Amos Hall; $4.4 million for the construction of the Van de Graaff Building 3rd Floor Laser Lab; $3.5 million for renovations to Ruskin Hall; and $3.4 million for the Plum Borough animal facility renovation.

The amount capitalized in property, plant, and equipment related to expenditures by the commonwealth on behalf of the University totals $439.5 million at June 30, 2010. Formal title to this property passes to the University upon completion of each project. The net book value of these items is $184.3 million at June 30, 2010.

## NOTE 7: CONDITIONAL ASSET REMEDIATION OBLIGATION

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

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

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| Balance - beginning of year | $ 37,107 | $ 39,093 |
| Accretion/ change in assumptions | 4,873 | (1,521) |
| Liabilities settled | (1,677) | (465) |
| **Balance - end of year** | $ 40,303 | $ 37,107 |
| Current liabilities | $ 2,000 | $ 2,000 |
| Noncurrent liabilities | 38,303 | 35,107 |
| **Total** | $ 40,303 | $ 37,107 |

| | Years Remaining to Maturity | FY 2010 Effective Interest Rates | Outstanding Principal (in thousands of dollars) 2010 | 2009 |
|---|---|---|---|---|
| Variable-rate bonds: | | | | |
| Series 2007-B Bonds | 31 | 0.25%-0.75% | $ 44,621 | $ 104,621 |
| Series 2005-B Bonds | 28 | 0.23%-0.40% | 45,000 | 45,000 |
| Series 2005-C Bonds | 25 | 0.22%-0.50% | 30,000 | 30,000 |
| Series 2005-A Bonds | | | - | 35,000 |
| Series 2002-B Bonds | | | - | 14,500 |
| Series 2000-A/B/C Bonds | | | - | 124,400 |
| Total variable-rate bonds | | | 119,621 | 353,521 |
| Term-rate bonds: | | | | |
| Series 2005-A Bonds | 29 | 5.00% | 40,000 | 40,000 |
| Series 2002-B Bonds | 26 | 5.00% | 15,000 | 15,000 |
| Total term-rate bonds | | | 55,000 | 55,000 |
| Fixed-rate bonds and notes payable: | | | | |
| Series 2009-A/B Bonds | 21 | 1.10%-5.10% | 428,520 | 428,520 |
| Series 2007-B Bonds | 18 | 4.28%-4.69% | 60,000 | - |
| Series 2005-A Bonds | 20 | 4.69%-4.83% | 35,000 | - |
| Series 2002-A Bonds | 13 | 1.93%-4.31% | 40,000 | 40,000 |
| Series 2002-B Bonds | 17 | 4.53%-4.74% | 14,500 | - |
| Series 2000-A/B/C Bonds | 25 | 4.00%-5.07% | 154,800 | 60,300 |
| Series 2007 PANTHER Notes, due August 1, 2010 | | 3.85% | 118,000 | 118,000 |
| Series 2010 PANTHER Notes, due May 31, 2011 | | 0.47% | 118,000 | - |
| Noninterest-bearing promissory note | | | 171 | 171 |
| Total fixed-rate bonds and notes payable | | | 968,991 | 646,991 |
| Unamortized premium | | | 37,588 | 31,730 |
| **Total bonds and notes payable** | | | $ 1,181,200 | $ 1,087,242 |

Interest costs incurred in 2010 and 2009 were $55.3 million and $40.4 million, respectively. Included in these amounts is capitalized interest associated with various construction projects. Capitalized interest for 2010 and 2009 was $4.4 million and $2.5 million, respectively.

In March 2009, the University issued $428.5 million of tax-exempt Capital Project and Refunding Bonds and generated $24.0 million of net premium proceeds. The Series 2009-A Bonds were issued in the amount of $143.5 million for the purpose of refunding the outstanding Series 2007-A Bonds on April 6, 2009. The Series 2009-B Bonds were issued in the amount of $285.0 million for the purpose of financing various capital projects.

Between December 2008 and August 2009, the University converted all of its variable rate demand bonds (VRDBs) in weekly mode into a fixed-rate, term-rate, or commercial paper (CP) mode. In July 2009, the University converted (a) $104.6 million of Series 2007-B Bonds in weekly mode to fixed-rate or CP mode; (b) $14.5 million of Series 2002-B Bonds in CP mode to fixed-rate mode; and (c) $124.4 million of Series 2000 Bonds in weekly or CP mode to fixed-rate mode. In August 2009, the University converted $35.0 million of Series 2005-A Bonds in CP mode to fixed-rate mode.

Liquidity support for the $119.6 million of outstanding VRDBs in CP mode is provided by the University. In the event the University receives notice of an optional tender on its VRDBs in CP mode, the purchase price of the bonds will be paid from the remarketing of such bonds. However, if the remarketing proceeds are insufficient, the University will have a current obligation to purchase the tendered bonds. To provide a secondary source of liquidity for this type of event, the University has a $100.0 million unsecured standby liquidity agreement with a financial institution that matures in September 2013. During 2010, no draws were made under the liquidity agreement.

In May 2010, the University issued its Pitt Asset Notes - Tax Exempt Higher Education Series of 2010 (PANTHERS of 2010) in the amount of $118.0 million. Of this amount, $78.0 million was used to partially refund the $118.0 million of PANTHERS of 2007 that matured on August 1, 2010, and $40.0 million is for the purpose of financing capital equipment expenditures. The PANTHERS of 2010 mature on May 31, 2011.

In August 2007, the University issued its Pitt Asset Notes - Tax Exempt Higher Education Series of 2007 (PANTHERS of 2007) in the amount of $118.0 million. Of this amount, $61.0 million was used to partially refund the $78.0 million of PANTHERS of 2006 that matured on August 24, 2007, and $57.0 million was used to finance capital equipment expenditures.

The fair value (as determined primarily by quoted market prices) of total bonds and notes payable is $1,264.5 million and $1,111.4 million at June 30, 2010 and 2009, respectively.

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

| | |
|---|---|
| 2011 | $ 254.1 |
| 2012 | $ 17.5 |
| 2013 | $ 30.0 |
| 2014 | $ 30.4 |
| 2015 | $ 35.0 |

The foregoing does not include $119.6 million of VRDBs in CP mode, all of which have final maturity dates between 2035 and 2041. These bonds bear short-term rates that are fixed over staggered periods of approximately 90 days each and are remarketed at the expiry of each rate period.

The University entered into three general unsecured credit facilities, aggregating $175.0 million, during 2009. These facilities were renewed in 2010 with the same aggregate available amount of $175.0 million. No draws were made under the facilities during 2010.

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

Derivative instruments are carried at fair value and included in the Consolidated Balance Sheets. Gains and losses from derivative instruments are reported in the Consolidated Statements of Activities. The University may be exposed to financial loss should a derivative counterparty fail to perform pursuant to the instrument. In the case of exchange-traded derivatives, the counterparty is the exchange itself. In the case of "over-the-counter" derivatives, the counterparty is typically a financial institution. Counterparty risks are mitigated by using creditworthy counterparties, settling positions periodically, and requiring collateral to be posted at predetermined levels of exposure.

Not including University derivative instruments held by various alternative investment funds, University financial assets invested in derivative instruments had a fair value of $136.7 million and $126.2 million as of June 30, 2010 and 2009, respectively, which are included in endowment investments on the Consolidated Balance Sheets.

The University liability arising from variable-to-fixed interest rate swap agreements associated with certain University debt obligations had a fair value of $60.9 million and $55.7 million as of June 30, 2010 and 2009, respectively, and are included in other liabilities on the Consolidated Balance Sheets. The fair value represents the estimated amount the University would be required to pay to terminate these agreements as of fiscal year end. The University recorded unrealized losses in the Consolidated Statements of Activities in the amounts of $5.2 million in 2010 and $39.8 million in 2009 due to changes in fair value of the swaps.

The aggregate notional amount of the swap agreements associated with University debt was $448.6 million and $659.2 million as of June 30, 2010 and 2009, respectively. These swaps were entered into for the sole purpose of hedging the interest payable on the University's Series 2000, 2002, 2005, and 2007 VRDBs. As such, the notional amounts and maturity dates of the swap agreements precisely matched the VRDBs they were intended to hedge. As the VRDBs have been subsequently modified or refinanced, the University has terminated or amended various swap agreements to achieve closer alignment with the current debt obligations. In this regard, the University terminated swap agreements having a total notional amount of $180.7 million during 2010. The variable interest rates received by the University under the swap agreements are either 67% or 70% of one- or three-month LIBOR, while the fixed rates paid by the University range from 3.18% to 5.14%. Net swap payments made or received by the University are reported in interest expense in the Consolidated Statements of Activities. No collateral was called or posted during 2010 with respect to these swap agreements. Furthermore, the University does not anticipate ever posting collateral pursuant to these swap agreements since the collateral thresholds applicable to the University are infinite at the University's current credit ratings.

## Note 10: Pension Plans and Other Benefits

The University provides retirement benefits under contributory or noncontributory plans to substantially all employees. The University's contributory plan provides for participation in the Teachers Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF) and in investment funds of the Vanguard Group. The plan is fully funded and requires three years of service for vesting of the University contribution. Employees hired before January 1, 1995 were immediately vested. University contributions to this plan in 2010 and 2009 were $66.2 million and $65.7 million, respectively.

The noncontributory plan is a defined benefit pension plan that covers employees who do not participate in the contributory plan. The plan provides for vesting after five years with pension benefits accruing at 2.1% of base salary or the Social Security wage base, whichever is lower. Pension benefits are payable upon normal retirement at age 65 or early retirement at age 55, in accordance with the conditions and pension eligibility criteria described in the plan. University contributions to this plan in 2010 and 2009 were $3.2 million and $2.8 million, respectively.

The University uses a measurement date of June 30 for plan assets and the benefit obligations. The table below sets forth the defined benefit plan's net periodic pension cost, projected benefit obligation, and funded status as reported at June 30:

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| **Net periodic pension cost:** | | |
| Service cost | $ 2,915 | $ 2,911 |
| Interest cost | 3,181 | 2,954 |
| Expected return on plan assets | (2,915) | (3,513) |
| Actuarial loss | 217 | - |
| Amortization of prior service credit | (224) | (224) |
| **Net periodic pension cost** | $ 3,174 | $ 2,128 |
| **Funded status:** | | |
| Projected benefit obligation—beginning of year | $ 45,995 | $ 44,279 |
| Service cost | 2,915 | 2,911 |
| Interest cost | 3,181 | 2,954 |
| Actuarial loss (gain) | 1,613 | (3,660) |
| Pension benefits paid to participants | (551) | (489) |
| **Projected benefit obligation—end of year** | $ 53,153 | $ 45,995 |
| Fair value of plan assets—beginning of year | $ 34,851 | $ 41,846 |
| Actual return on plan assets | 3,717 | (9,271) |
| Actual plan contributions | 3,174 | 2,765 |
| Pension benefits paid to participants | (551) | (489) |
| **Fair value of plan assets—end of year** | $ 41,191 | $ 34,851 |
| **Funded status - liability recognized on Consolidated Balance Sheets:** | | |
| **Pension and postretirement obligations** | $ (11,962) | $ (11,144) |
| **Accumulated benefit obligation** | $ 50,899 | $ 43,438 |
| **Estimated 2011 employer contribution to the defined benefit plan:** | $ 3,012 | |

Assets related to the University's noncontributory defined benefit pension plan are segregated in a trust and invested in a balanced fund managed by a third-party investment manager. The fair value of these assets as of June 30, 2010 and 2009 is $41.2 million and $34.9 million, respectively. The fund is invested in domestic and international equities and fixed income securities using the S&P 500 Index as a benchmark for domestic equities, the MSCI EAFE Index for international equities, and the Barclays Intermediate Government/Credit Bond Index for the fixed income securities. The specific investment objective is to meet or exceed the investment policy benchmark over the long term.

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

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

| | Target Asset Allocation |
|---|---|
| Domestic Equity | 35% |
| International Equity | 35% |
| Fixed Income | 30% |

The actual asset allocation as of June 30, 2010 and 2009 is 60% and 75%, respectively, for combined equities and 40% and 25%, respectively, for fixed income securities.

The fair value of the University's pension plan assets at June 30, 2010, by asset category, is as follows:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | | *(in thousands of dollars)* | | |
| **Asset Category** | | | | |
| Equity Securities: | | | | |
| Stock Index | $ - | $ 11,400 | $ - | $ 11,400 |
| Small Cap | - | 1,362 | - | 1,362 |
| International | - | 11,793 | - | 11,793 |
| Debt Securities | - | 12,662 | - | 12,662 |
| Cash and Equivalents | - | 3,974 | - | 3,974 |
| **Total** | $ - | $ 41,191 | $ - | $ 41,191 |

The fair value of the University's pension plan assets at June 30, 2009, by asset category, is as follows:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | | *(in thousands of dollars)* | | |
| **Asset Category** | | | | |
| Equity Securities: | | | | |
| Stock Index | $ - | $ 18,564 | $ - | $ 18,564 |
| International | - | 7,557 | - | 7,557 |
| Debt Securities | 3,047 | 1,492 | - | 4,539 |
| Cash and Equivalents | - | 4,191 | - | 4,191 |
| **Total** | $ 3,047 | $ 31,804 | $ - | $ 34,851 |

The University also provides postretirement medical and life insurance benefits to eligible employees and their spouses upon retirement through a contributory benefit plan. The University uses a measurement date of June 30 for plan assets and the benefit obligation. The table below sets forth the University's net periodic postretirement benefit cost, accumulated postretirement benefit obligation, and funded status at June 30:

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| **Net periodic postretirement benefit cost:** | | |
| Service cost | $ 14,058 | $ 13,152 |
| Interest cost | 18,027 | 15,995 |
| Amortization of prior service credit | (3,965) | (3,965) |
| Amortization of transition obligation | 3,031 | 3,031 |
| Recognized actuarial loss | 1,280 | 1,444 |
| **Net periodic postretirement benefit cost** | $ 32,431 | $ 29,657 |
| **Funded status:** | | |
| Accumulated benefit obligation — beginning of year | $ 262,988 | $ 241,939 |
| Service cost | 14,058 | 13,152 |
| Interest cost | 18,027 | 15,995 |
| Actuarial loss | 6,669 | 820 |
| Postretirement benefits paid to participants | (10,091) | (8,918) |
| **Accumulated benefit obligation — end of year** | $ 291,651 | $ 262,988 |
| **Funded status - liability recognized on Consolidated Balance Sheets** | $ (291,651) | $ (262,988) |
| **Amounts recognized in the Consolidated Balance Sheets consist of:** | | |
| Accrued payroll and related liabilities | $ (10,807) | $ (10,091) |
| Pension and postretirement obligations | (280,844) | (252,897) |
| **Liability recognized on Consolidated Balance Sheets** | $ (291,651) | $ (262,988) |

A one percentage point change in assumed healthcare cost trend rates would have the following effects:

| | Increase | | (Decrease) | |
|---|---|---|---|---|
| | *(in millions of dollars)* | | | |
| | Revised Amount | Percent Change | Revised Amount | Percent Change |
| Service and interest cost (medical component only) | $ 33.5 | 15.9% | $ 25.0 | 13.4% |
| Total periodic benefit cost | $ 39.5 | 21.9% | $ 26.5 | 18.2% |
| Accumulated benefit obligation for healthcare benefits | $ 293.8 | 12.8% | $ 232.9 | 10.6% |
| Total accumulated benefit obligation | $ 324.9 | 11.4% | $ 263.9 | 9.5% |

Though funding is not required, the University has elected to fund the medical and life insurance portions of its liability via a quasi-endowment, which is managed by the University's external endowment fund managers. The fair value of these investments at June 30, 2010 and 2009 is $178.0 million and $149.5 million, respectively, and is included in endowment investments in the Consolidated Balance Sheets as detailed in Note 4.

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

| | Defined Benefit Plan | | Postretirement Plan | |
|---|---|---|---|---|
| | 2010 | 2009 | 2010 | 2009 |
| **Weighted-average assumptions used to determine the benefit obligation (liability) at June 30:** | | | | |
| Discount rate | 6.0% | 7.0% | 5.75% | 7.0% |
| Expected long-term return on plan assets | 8.0% | 8.5% | - | - |
| Rate of compensation increase: | | | | |
| 2009 | - | - | - | - |
| 2010 - 2011 | 2.5% | 2.0% | - | - |
| 2012 - 2014 | 3.0% | 4.0% | - | - |
| 2015 and thereafter | 3.0% | 5.0% | - | - |
| Assumed healthcare trend cost: | | | | |
| Initial trend - pre-age 65 retirees | - | - | 9.0% | 9.0% |
| Initial trend - post-age 65 retirees | - | - | 15.0% | 20.0% |
| Ultimate trend | - | - | 5.0% | 5.0% |
| Year to reach ultimate | - | - | 2015 | 2014 |
| **Weighted-average assumptions used to determine the net periodic cost (expense) for the years ended June 30:** | | | | |
| Discount Rate | 7.0% | 6.75% | 7.00% | 6.75% |
| Rate of compensation increase | 5.0% | 5.0% | - | - |
| Expected long-term return on plan assets | 8.5% | 8.5% | - | - |
| Assumed health care trend cost: | | | | |
| Initial trend - pre-age 65 retirees | - | - | 9.0% | 9.0% |
| Initial trend - post-age 65 retirees | - | - | 20.0% | 15.0% |
| Ultimate trend | - | - | 5.0% | 5.0% |
| Year to reach ultimate | - | - | 2014 | 2013 |

| **Estimated future benefit payments:** | Defined Benefit Plan | Postretirement Plan |
|---|---|---|
| 2011 | $ 1,088 | $ 10,807 |
| 2012 | $ 1,192 | $ 13,006 |
| 2013 | $ 1,313 | $ 14,625 |
| 2014 | $ 1,450 | $ 16,295 |
| 2015 | $ 1,626 | $ 17,661 |
| 2016-2020 | $ 11,562 | $ 107,182 |

Authoritative accounting guidance provides information on the net asset classification of donor-restricted endowment funds for not-for-profit organizations that are subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA), including enhanced disclosures related to an organization's endowment funds regardless of whether the organization is located in a state that is subject to UPMIFA. The enhanced disclosures relate to net asset classification and changes in endowment net assets and have been incorporated in the tables below.

The commonwealth has not adopted UPMIFA and, instead, enacted in December 1998 Pennsylvania Act 141 (codified as Title 15 of the Pennsylvania Consolidated Statutes §5548(c) and referred to herein as "Title 15") to govern the investment of restricted funds held in trust by Pennsylvania nonprofit corporations. Title 15 permits Pennsylvania nonprofit corporations to elect a "total return" approach for determining income distributions from restricted funds held in trust, whereby "income" is defined as a stipulated percentage of the value of the assets held; the stipulated percent must be determined at least annually and may be no less than 2% nor more than 7%, and the value of the assets held must be averaged over a period of three or more preceding years. A resolution to elect a "total return" approach for determining endowment income distributions was passed by the University's Board of Trustees on October 21, 1999. The University's endowment income distribution is determined annually using a stipulated percentage of 4.25% of the endowment's three-year average fair value, provided that such distribution is not less than the amount distributed in the previous year. As a result of the University's floor on income distributions, the income distribution for 2010 was approximately 4.41% of the endowment's three-year average fair value.

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

The University's endowment net assets as of June 30 are as follows:

| | 2010 | | | |
|---|---|---|---|---|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| | *(in thousands of dollars)* | | | |
| Donor-restricted endowment funds | $ - | $ 440,996 | $ 499,173 | $ 940,169 |
| Quasi-endowment funds | 1,079,802 | - | - | 1,079,802 |
| **Total endowment net assets** | $ 1,079,802 | $ 440,996 | $ 499,173 | $ 2,019,971 |

| | 2009 | | | |
|---|---|---|---|---|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| | *(in thousands of dollars)* | | | |
| Donor-restricted endowment funds | $ - | $ 386,026 | $ 476,252 | $ 862,278 |
| Quasi-endowment funds | 967,054 | - | - | 967,054 |
| **Total endowment net assets** | $ 967,054 | $ 386,026 | $ 476,252 | $ 1,829,332 |

The change in endowment net assets for the years ended June 30 are as follows:

| | 2010 | | | |
|---|---|---|---|---|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| | *(in thousands of dollars)* | | | |
| Endowment net assets - beginning of year | $ 967,054 | $ 386,026 | $ 476,252 | $ 1,829,332 |
| Endowment return: | | | | |
| Endowment earnings | 15,498 | - | 1,642 | 17,140 |
| Net gains | 162,982 | 54,970 | - | 217,952 |
| Total endowment return | 178,480 | 54,970 | 1,642 | 235,092 |
| Gifts | 571 | - | 21,279 | 21,850 |
| Net distributions | (81,269) | - | - | (81,269) |
| Net transfers | 14,966 | - | - | 14,966 |
| **Endowment net assets - end of year** | $ 1,079,802 | $ 440,996 | $ 499,173 | $ 2,019,971 |

| | 2009 | | | |
|---|---|---|---|---|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| | *(in thousands of dollars)* | | | |
| Endowment net assets - beginning of year | $ 1,214,881 | $ 669,135 | $ 454,641 | $ 2,338,657 |
| Endowment return: | | | | |
| Endowment earnings | 21,025 | - | 1,466 | 22,491 |
| Net losses | (239,083) | (283,109) | (121) | (522,313) |
| Total endowment return | (218,058) | (283,109) | 1,345 | (499,822) |
| Gifts | 538 | - | 20,266 | 20,804 |
| Net distributions | (79,355) | - | - | (79,355) |
| Net transfers | 49,048 | - | - | 49,048 |
| **Endowment net assets - end of year** | $ 967,054 | $ 386,026 | $ 476,252 | $ 1,829,332 |

Nearly 99 percent of the University's endowment funds are collectively managed in a broadly diversified pool of assets called the consolidated investment pool. The Investment Committee of the Board of Trustees provides advice to University management, including the approval of endowment investment guidelines, objectives, and policies, and it is responsible for reviewing the selection of investment advisors and investment performance.

The asset allocation policy is established with the intent of optimizing long-term portfolio returns while minimizing market and manager risks. It reflects a desire for portfolio diversification by incorporating allocations across several broad asset classes, including: domestic equity, international equity, and emerging markets equity; fixed income; real assets; marketable alternatives; and nonmarketable alternatives.

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

## Note 12: Functional Expenses

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

| | 2010 | 2009 |
|---|---|---|
| | *(in thousands of dollars)* | |
| Instruction | $ 461,399 | $ 452,310 |
| Research | 607,123 | 549,390 |
| Public service | 97,690 | 91,433 |
| Academic support | 137,603 | 131,909 |
| Libraries | 51,897 | 51,896 |
| Student services | 114,830 | 114,659 |
| Institutional support | 168,435 | 154,888 |
| Auxiliary enterprises | 117,518 | 111,137 |
| **Total functional expenses** | $ 1,756,495 | $ 1,657,622 |

## Note 13: Related Parties

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

Certain University SOM faculty and staff provide clinical services through their University appointments to UPMC, UPP, and affiliated hospitals. The University invoices these entities monthly for reimbursement of the clinical portion of the associated compensation costs. SOM faculty members having both a University academic appointment and separate, external UPP clinical responsibilities participate in the University/UPP common paymaster arrangement for purposes of determining appropriate FICA taxation. In addition to the reimbursable compensation costs, the University also engages in other transactions with these entities, which include providing certain facilities-related services, telephone, mailing, printing, and various other services, which are reimbursed at cost. Receivables due from UPMC and UPP for compensation and other costs total $8.4 million and $9.3 million as of June 30, 2010 and 2009, respectively.

In 1998, the University signed a 10-year agreement with UPMC that included financial commitments designed to further the two entities' commitment to their interrelated teaching, research, clinical care, and community service missions. As part of the agreement, UPMC provides $12.5 million annually in funding for the SOM. UPMC also provides additional funding up to $2.5 million annually on a matching basis. The match is on a one-to-two basis with UPMC matching $1 for every $2 provided by the University to support health sciences programs. The University has received this match each year since the inception of the agreement. This agreement was amended in 2007 under essentially the same terms, except for a provision to provide an additional $10.0 million per year in 2007, increased annually by $0.5 million from 2008 through 2016. The agreement was further amended in 2009 to include additional financial support from UPMC through the Children's Hospital of Pittsburgh of UPMC (CHP) to the University of $7.5 million annually related to an agreement detailing the transfer of certain pediatric research programs from CHP to the University. This transfer standardizes procedures, eliminates duplication of services, improves efficiency, reduces costs, and enhances recruitment efforts for pediatric programs.

UPMC also provided $12.3 million and $11.9 million in 2010 and 2009, respectively, of contractual dean's tax, which represents additional support for the academic and research activities of the SOM.

The University is involved in certain rental arrangements where the University acts as both lessor or lessee with UPMC and its affiliates. Rental revenue from UPMC and affiliates totals $10.7 million and $10.4 million for the years ended June 30, 2010 and 2009, respectively. Rent expense paid to UPMC and affiliates totals $22.8 million and $16.3 million for the years ended June 30, 2010 and 2009, respectively.

UPMC serves as the provider of health insurance coverage to all eligible University employees who enroll in the plan. The University is self-insured for these costs and reimburses UPMC for actual claims cost. Health insurance expense including administrative fees totaled $85.9 million and $82.1 million in 2010 and 2009, respectively, and is reported as expense on the Consolidated Statements of Activities.

In 2003, the University and UPMC created the Medical and Health Sciences Foundation (MHSF), a separate 501(c)(3) organization. The mission of MHSF is to create a unified fundraising organization for the University's schools of the health sciences and UPMC. The arrangement calls for the cost of MHSF to be split evenly between the University and UPMC. In 2010 and 2009, UPMC's share of total operating costs for MHSF totaled $3.5 million and $3.6 million, respectively. All gifts generated by MHSF are credited to the University or UPMC based upon donor wishes.

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

A lease arrangement exists between the University and the commonwealth for the Western Psychiatric Institute and Clinic (WPIC). Since 1949, the University has managed WPIC under an agreement between the University and the commonwealth whereby the University rents for a consideration of $1 per year the land, building, equipment, and other items that are used by WPIC. The agreement provides for continuing terms of 10 years each; however, this agreement is cancelable by either party on one year's written notice. In 1992, the University subleased to UPMC the land, building, equipment, and other items subject to the current lease arrangement between the commonwealth and the University. This sublease arrangement continued to be in effect during 2010 and 2009. Included in property, plant, and equipment is $191.1 million and $187.7 million at June 30, 2010 and June 30, 2009, respectively, related to the land, buildings, and equipment used by WPIC. Accumulated depreciation related to these assets totals $148.4 million and $143.5 million at June 30, 2010 and June 30, 2009, respectively.

The University also has an arrangement with WPIC whereby certain research-related costs incurred by WPIC clinical staff (primarily compensation) are charged to University research grants via an electronic billing each month. Payments on these billings total $29.4 million in 2010 and $29.1 million in 2009 and are recorded as expenses in the Consolidated Statements of Activities. All billings are recorded at cost and amounts are reimbursed to WPIC on a monthly basis.

## Note 14: Commitments and Contingencies

At June 30, 2010 and 2009, the University has outstanding contractual commitments of $62.8 million and $61.4 million, respectively, for property, plant, and equipment expenditures.

The University engages in various leasing activities as both a lessor and lessee. Rental revenue from operating leases is $19.4 million and $18.9 million in 2010 and 2009, respectively. Rental expense for operating leases is $41.8 million in 2010 and $30.4 million in 2009. Minimum future rental revenue and expense under operating leases that have initial or remaining noncancelable lease terms for the years ended June 30 are as follows:

| | Rental Revenue | Rental Expense |
|---|---|---|
| | *(in thousands of dollars)* | |
| 2011 | $ 16,651 | $ 33,029 |
| 2012 | $ 5,447 | $ 26,562 |
| 2013 | $ 4,176 | $ 23,703 |
| 2014 | $ 2,958 | $ 22,043 |
| 2015 | $ 2,359 | $ 21,050 |
| Thereafter | $ 12,479 | $ 167,766 |

Various legal proceedings involving, among other things, allegations of securities fraud and other securities law violations have been initiated against one of the University's investment advisers, Westridge Capital Management, Inc. and its related entities (Westridge). In connection with these proceedings, restraining orders have been granted, assets of Westridge and other named defendants have been frozen, and a receiver has been appointed and is currently overseeing the affairs of Westridge. The University's interest with Westridge is a senior promissory note and is reported in the University's endowment assets on the Consolidated Balance Sheets.

Based upon management's assessment of the receiver's findings, the fair value as of June 30, 2010 and 2009 of the University's investment in Westridge is reported on the Consolidated Balance Sheets at $34.9 million. In 2009, the University recognized an impairment loss of $34.9 million. As of June 30, 2010, there are uncertainties as to the timing and amount of the University's ultimate recovery from this investment.

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

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

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

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