UNIVERSITY OF ROCHESTER
AND RELATED ENTITIES

Consolidated Financial Statements

June 30, 2012 and 2011

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Report of Independent Auditors

To the Board of Trustees
University of Rochester:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of activities and of cash flows present fairly, in all material respects, the financial position of the University of Rochester (the "University") at June 30, 2012 and 2011, and the changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements 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 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, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1(i) to the consolidated financial statements, the University changed the manner in which it classifies accumulated total investment returns within net assets as a result of the adoption of ASC 958, Not-for-Profit Entities (formerly FASB Staff Position No. 117-1) at July 1, 2010.

PricewaterhouseCoopers LLP

Rochester, New York
October 16, 2012

PricewaterhouseCoopers LLP, 1100 Bausch & Lomb Place, Rochester, NY 14604
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UNIVERSITY OF ROCHESTER
AND RELATED ENTITIES
Consolidated Balance Sheet
As of June 30
(dollars in thousands)

Assets	**2012**	**2011**
Cash and cash equivalents	$ 326,227	$ 285,203
Operating investments, at market	209,016	209,393
Collateral held for securities lending	-	69,282
Accounts receivable, net	325,773	292,169
Inventories, prepaid expenses, and deferred charges	52,816	48,957
Contributions receivable, net	90,927	51,556
Notes receivable, net	48,347	48,006
Other assets	11,936	15,536
Investments held for long-term purposes	1,822,954	1,783,356
Property, plant, and equipment, net	1,561,957	1,453,775
Interest in net assets of foundation	12,330	13,743
Investments in perpetual trusts held by others	46,877	49,780
Total assets	$ 4,509,160	$ 4,320,756
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	$ 388,337	$ 305,494
Advanced receipt of sponsored research revenues	23,472	25,618
Deferred revenue	50,775	52,069
Third-party settlements payable, net	100,989	96,386
Securities lending liabilities	-	69,282
Accrued pension, post-retirement, and post-employment	386,472	308,073
Long-term debt	874,209	745,913
Asset retirement obligation	19,016	18,057
Refundable U.S. Government grants for student loans	16,223	16,004
Total liabilities	1,859,493	1,636,896
Net Assets:		
Unrestricted	1,745,673	1,818,709
Temporarily restricted	509,533	506,216
Permanently restricted	394,461	358,935
Total net assets	2,649,667	2,683,860
Total liabilities and net assets	$ 4,509,160	$ 4,320,756

See accompanying notes to consolidated financial statements.

UNIVERSITY OF ROCHESTER
AND RELATED ENTITIES
Consolidated Statement of Activities
Year Ended June 30, 2012
(dollars in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues:				
Tuition and fees	$ 360,695	$ -	$ -	$ 360,695
Less: scholarships and fellowships	(151,430)	-	-	(151,430)
Net tuition and fees	209,265	-	-	209,265
State and local appropriations	1,851	-	-	1,851
Grants and contracts	396,145	-	-	396,145
Gifts and pledges	25,747	49,738	36,320	111,805
Hospital and faculty practice patient care activities	1,860,382	-	-	1,860,382
Auxiliary enterprises	88,728	-	-	88,728
Interest income and appreciation of operating investments	5,537	-	-	5,537
Educational activities	28,540	-	-	28,540
Royalty income	34,431	-	-	34,431
Other sources	14,252	-	-	14,252
Long-term investment income and gains allocated to operations	88,390	-	-	88,390
Net assets released from restriction	53,701	(53,365)	(336)	-
Total operating revenues	2,806,969	(3,627)	35,984	2,839,326
Operating expenses:				
Salaries and wages	1,369,458	-	-	1,369,458
Fringe benefits	400,322	-	-	400,322
Total compensation	1,769,780	-	-	1,769,780
Supplies	350,767	-	-	350,767
Business and professional	190,815	-	-	190,815
Utilities	52,253	-	-	52,253
Maintenance and facilities costs	114,210	-	-	114,210
Depreciation	163,619	-	-	163,619
Interest	30,604	-	-	30,604
Other	59,881	-	-	59,881
Total operating expenses	2,731,929	-	-	2,731,929
Change in net assets from operating activities	75,040	(3,627)	35,984	107,397
Non-operating activities:				
Long-term investment activities:				
Investment income	10,036	2,569	(113)	12,492
Net appreciation (depreciation)	(12,466)	5,888	(1,816)	(8,394)
Total long-term investment activities	(2,430)	8,457	(1,929)	4,098
Long-term investment income and gains allocated for operations	(88,390)	-	-	(88,390)
Loss on extinguishment of debt	(636)	-	-	(636)
Other changes, net	(56,620)	262	1,315	(55,043)
Change in valuation of annuities	-	(1,775)	156	(1,619)
Change in net assets from non-operating activities	(148,076)	6,944	(458)	(141,590)
Change in net assets	(73,036)	3,317	35,526	(34,193)
Beginning net assets	1,818,709	506,216	358,935	2,683,860
Ending net assets	$ 1,745,673	$ 509,533	$ 394,461	$ 2,649,667

See accompanying notes to consolidated financial statements.

UNIVERSITY OF ROCHESTER
AND RELATED ENTITIES
Consolidated Statement of Activities
Year Ended June 30, 2011
(dollars in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues:				
Tuition and fees	$ 343,537	$ -	$ -	$ 343,537
Less: scholarships and fellowships	(142,321)	-	-	(142,321)
Net tuition and fees	201,216	-	-	201,216
State and local appropriations	1,875	-	-	1,875
Grants and contracts	438,022	-	-	438,022
Gifts and pledges	19,618	17,781	24,455	61,854
Hospital and faculty practice patient care activities	1,783,587	-	-	1,783,587
Auxiliary enterprises	79,653	-	-	79,653
Interest income and appreciation of operating investments	13,538	-	-	13,538
Educational activities	29,894	-	-	29,894
Royalty income	42,318	-	-	42,318
Other sources	13,758	(28)	-	13,730
Long-term investment income and gains allocated to operations	87,717	-	-	87,717
Net assets released from restriction	47,659	(47,659)	-	-
Total operating revenues	2,758,855	(29,906)	24,455	2,753,404
Operating expenses:				
Salaries and wages	1,306,985	-	-	1,306,985
Fringe benefits	367,618	-	-	367,618
Total compensation	1,674,603	-	-	1,674,603
Supplies	344,487	-	-	344,487
Business and professional	195,798	-	-	195,798
Utilities	53,918	-	-	53,918
Maintenance and facilities costs	112,914	-	-	112,914
Depreciation	158,441	-	-	158,441
Interest	29,344	-	-	29,344
Other	81,732	-	-	81,732
Total operating expenses	2,651,237	-	-	2,651,237
Change in net assets from operating activities	107,618	(29,906)	24,455	102,167
Non-operating activities:				
Long-term investment activities:				
Investment income	12,775	4,611	(126)	17,260
Net appreciation	140,635	115,119	7,273	263,027
Total long-term investment activities	153,410	119,730	7,147	280,287
Long-term investment income and gains allocated for operations	(87,717)	-	-	(87,717)
Other changes, net	7,909	(205)	3,157	10,861
Change in valuation of annuities	-	(2,753)	(752)	(3,505)
Change in net assets from non-operating activities	73,602	116,772	9,552	199,926
Change in net assets before cumulative effect of change in accounting principle	181,220	86,866	34,007	302,093
Cumulative effect of change in accounting principle	(239,778)	239,778	-	-
Change in net assets	(58,558)	326,644	34,007	302,093
Beginning net assets	1,877,267	179,572	324,928	2,381,767
Ending net assets	$ 1,818,709	$ 506,216	$ 358,935	$ 2,683,860

See accompanying notes to consolidated financial statements.

UNIVERSITY OF ROCHESTER
AND RELATED ENTITIES
Consolidated Statement of Cash Flows
Years Ended June 30
(dollars in thousands)

Cash flows from operating activities:	**2012**	**2011**
Change in net assets	$ (34,193)	$ 302,093
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation expense	163,619	158,441
Net depreciation (appreciation) on long-term investment activities	8,394	(263,027)
Gifts of property, plant, equipment and other	(307)	(1,308)
Bond discount amortization	(1,294)	(762)
Loss on the extinguishment of debt	636	-
Provision for bad debts	10,668	25,718
Contributed securities	(13,452)	(10,504)
Loss on disposals of property, plant, and equipment	7,740	2,389
Contributions for long-term investments, net	(33,235)	(24,636)
(Increases) / decreases in:		
Operating investments	(746)	(7,840)
Accounts receivable, net	(44,272)	(10,054)
Inventories, prepaid expenses, and deferred charges	(3,338)	259
Contributions receivable, net	(37,782)	(5,376)
Other assets	3,362	(2,788)
Increases / (decreases) in:		
Accounts payable and accrued expenses	61,553	7,531
Advanced receipt of sponsored research revenues	(2,146)	2,489
Deferred revenues	(1,294)	562
Third-party settlements payable, net	4,603	3,819
Accrued pension, post-retirement, and post-employment	78,399	24,511
Net cash provided by operating activities	166,915	201,517
Cash flows from investing activities:		
Purchases of property, plant, and equipment	(268,986)	(206,424)
Purchases of investments	(509,988)	(621,295)
Proceeds from the sale of investments	492,165	676,248
Increase in investments in perpetual trusts held by others	(96)	(95)
(Increase) / decrease in notes receivable, net	(341)	157
Net cash used in investing activities	(287,246)	(151,409)
Cash flows from financing activities:		
Net borrowings on lines-of-credit	435	772
Principal repayments of long-term debt	(42,652)	(26,618)
Proceeds from issuance of long-term debt	171,929	-
Deferred financing costs	(1,811)	(1)
Increase in refundable U.S. Government grants for student loans	219	62
Contributions for long-term investments, net	33,235	24,636
Net cash provided by / (used in) financing activities	161,355	(1,149)
Net increase in cash and cash equivalents	41,024	48,959
Cash and cash equivalents, beginning of year	285,203	236,244
Cash and cash equivalents, end of year	$ 326,227	$ 285,203
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest on long-term debt	$ 30,288	$ 28,740
Non-cash investing and financing activities:		
Increase in construction related payables	$ 8,164	$ 4,407
Assets acquired under capital leases	$ 248	$ 342

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

(a) General

The University of Rochester (the University) is a private nonprofit institution of higher education based in Rochester, New York. The University provides education and training services, primarily for students at the undergraduate, graduate, and postdoctoral levels. It also performs research, training, and other services under grants, contracts, and similar agreements with sponsoring organizations, primarily departments and agencies of the United States Government; and provides health care services through Strong Memorial Hospital (Hospital), Strong Home Care Group, and the various entities included in Strong Partners Health System, Inc. (SPHS).

(b) Basis of Presentation

The accompanying consolidated financial statements include all of the integrated divisions of the University – The Schools of Arts, Sciences and Engineering, including the Hajim School of Engineering and Applied Sciences, Margaret Warner Graduate School of Education and Human Development, William E. Simon Graduate School of Business Administration, Eastman School of Music, Memorial Art Gallery, School of Medicine and Dentistry, Strong Memorial Hospital, School of Nursing, Eastman Institute for Oral Health, Health Sciences, and the University of Rochester Medical Faculty Group (URMFG). Included also are Strong Partners Health System, Inc. (and its affiliates), Eastman Dental Center Foundation, Inc., Strong Home Care Group (and its subsidiaries), Crittenden Boulevard Housing Company, Inc., Excell Partners, Inc., Rochester BioVenture Center, Inc., High Tech Rochester, Inc., UR Investment, LLC, eXtensible Catalog Organization, LLC, University of Rochester Real Estate Corporation, UR Equity Holdings, Inc., the Meliora Real Estate Corporation, and Spruce Risk Purchasing Group, LLC. All significant interorganizational balances and transactions have been eliminated.

The University is the sole member of SPHS, which is the sole member of Highland Hospital of Rochester (including its subsidiaries The Highland Foundation, Inc., Highland Facilities Development Corp., and the Medical Administrative Associates, Inc.); The Highlands Living Center, Inc.; Highland Community Development Corporation; and The Meadows at Westfall, Inc. Highland Hospital and its subsidiaries have debt outstanding which has been included in the University's consolidated financial statements; however, under the terms of the affiliation agreement with SPHS, the University has no legal obligation for the debt of Highland Hospital and affiliates.

The Eastman Dental Center Foundation, Inc. (the Foundation) was formed to hold and manage the investment assets of the former Eastman Dental Center, which was merged into the University during 1998. Income and assets of the Foundation are used to support oral health, education, and research projects at the University.

The University is the sole corporate member of Strong Home Care Group, which is the sole member of Visiting Nurse Service of Rochester and Monroe County, Inc. and Community Care of Rochester.

The University, through SPHS, Strong Memorial Hospital and URMFG, formed a Managed Care Organization (MCO) in October 1997 together with two community physician organizations: the Highland Physician Organization and the Rochester Community Physician Organization. The MCO has ceased operations related to member contracting activities and is in the process of finalizing its activities.

The University is the sole corporate member of Crittenden Boulevard Housing Company, Inc., which was formed to provide affordable housing facilities for graduate students and staff of the University.

The University is the sole corporate member of Excell Partners, Inc., which was formed to support early stage commercial development utilizing technologies created at the University of Rochester and other regional colleges and universities.

The University is the sole corporate member of Rochester BioVenture Center, Inc., which was formed to support the development of new businesses utilizing technologies created at the University and other regional colleges and universities, through the operation of incubator/research facilities in Monroe County, New York.

The University is the sole corporate member of High Tech Rochester, Inc. (HTR), which is a not-for-profit economic development organization that promotes the creation and growth of technology companies through support services and incubation facilities and provides consulting services for manufacturers.

The University is the sole member of University of Rochester Investment, LLC, which was formed for the purpose of holding certain University investments.

The University is the sole member of eXtensible Catalog Organization, LLC, which was formed to support the charitable and educational activities of the University through development of open-source library catalog software.

In December 2009, the University entered into a financing arrangement for the renovation of the Eastman Theatre enhanced by qualified investors in the New Markets Tax Credit (NMTC) program of the United States Treasury. The use of NMTCs is a program of the Community Development Financial Institutions Fund, a bureau of the United States Treasury. This transaction required the formation of a wholly-owned special purpose corporation known as the University of Rochester Real Estate Corporation.

In July 2010, UR Equity Holdings, Inc., a for-profit corporation, was formed for the purpose of holding the University's equity interests in startup companies.

In May 2011, the University became the sole corporate member of Meliora Real Estate Corporation, which was formed to support the charitable activities of the University of Rochester by providing financial and operational support to the University through the acquisition, holding and sale of real estate donated to the University and affiliates.

The University is the sole member of Spruce Risk Purchasing Group, LLC, which was formed in October, 2011 for the purpose of procuring insurance coverage for physicians and other healthcare providers affiliated with the University of Rochester Medical Center.

(c) Basis of Accounting

The consolidated financial statements of the University are prepared on the accrual basis of accounting and in conformity with generally accepted accounting principles in the United States of America.

<u>Classification of Net Assets</u>

The University reports its net assets and changes therein according to three classifications: permanently restricted, temporarily restricted, and unrestricted, based upon the existence or absence of donor-imposed restrictions.

<u>Permanently restricted</u> – Net assets subject to donor–imposed stipulations that they be maintained permanently by the University. In accordance with the guidance provided in the New York Prudent Management of Institutional Funds Act (NYPMIFA), the University's Board of Trustees, with consideration of the actions, reports, information, advice and counsel provided by its duly constituted committees and appointed officers of the University, has instructed the University to adopt a methodology designed to avoid spending below the historical dollar value of donor-restricted (true) endowment funds, absent explicit donor direction to the contrary. As a result, the University classifies as permanently restricted net assets the original gift value of true endowments plus any subsequent gifts and accumulations made in accordance with the directions of the applicable gift instruments. The

portion of true endowment funds that is not classified as permanently restricted net assets is classified as temporarily restricted net assets in accordance with accounting standards.

Temporarily restricted – Net assets subject to donor-imposed stipulations that may or will be met either by actions of the University and/or the passage of time. Investment income and gains and losses on permanently restricted net assets are reported as temporarily restricted until appropriated for expenditure in accordance with donor-imposed stipulations. Under NYPMIFA, the appropriation and spending of such income is subject to a standard of prudence, as more fully discussed under the accounting policy note on investments, note 1(i). When a donor restriction expires, that is, when a stipulated time restriction ends or spending restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restriction.

Unrestricted – Net assets that are not subject to donor-imposed stipulations and that are generally available for support of the University's activities with certain limitations, as follows:

- Uses of certain unrestricted net assets are committed through contractual agreements. Such amounts primarily consist of required trusteed balances under long-term debt agreements and matching funds under student loan programs of the federal government. In addition, grants and contracts for the performances of certain services or functions are reported in the unrestricted net asset category.

- Many of the funds, which are unrestricted for accounting purposes, carry internal designations to specific divisions of the University, and therefore are not treated operationally as unrestricted funds.

- The Board of Trustees, through voluntary resolutions, has set aside portions of the University's unrestricted net assets to function as endowment, for property, plant and equipment purposes, and for other specific operating purposes.

Revenues from sources other than contributions are generally reported as increases in unrestricted net assets. Contributions are reported as increases in the appropriate category of net assets, except those contributions whose imposed restrictions are met in the same fiscal year they are received, are included in unrestricted revenues.

Expenses are reported as decreases in unrestricted net assets. Expiration of temporary restrictions recognized on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as releases from temporarily restricted net assets to unrestricted net assets. Temporary restrictions on gifts to acquire long-lived assets are considered met in the period in which the assets are placed in service.

(d) Income Taxes

The University and the majority of its affiliates are not-for-profit organizations as described in section 501(c)(3) of the Internal Revenue Code and are generally exempt from income taxes on related income pursuant to Section 501(a) of the Code.

(e) Operations

The statements of activities present the changes in net assets of the University from operating activities and from non-operating activities. Operating revenues and expenses relate primarily to educational and training programs, research activities and hospital and patient care activities provided by the University and its related entities.

Utilization of investment income and gains on long-term investments held for endowment and similar purposes under the University's total return spending policy, as discussed in note 1(i), is considered operating revenue.

Non-operating activities consist primarily of investment income and appreciation from long-term investments in excess of amounts utilized for operations. Other changes, net consists primarily of adjustments in pension, post-retirement, and post-employment obligations based on actuarially determined liabilities.

(f) Cash and Cash Equivalents and Operating Investments

Cash and cash equivalents include amounts on deposit with financial institutions; short-term investments with maturities of three months or less at the time of purchase and other highly liquid investments, primarily cash management funds, except that such instruments purchased with endowment and annuity and life income assets on deposit with trustees are classified as investments.

Operating investments include all other current investments with original maturities greater than three months and are used to support operations. These current investments include obligations of the U.S. Treasury, U.S. Government and other government agencies, and corporate and foreign bonds. Included also are internal operating funds invested in the University's long term investment pool however, they may be liquidated upon demand at any time.

(g) Inventories

Inventories, primarily medical supplies, are valued at the lower of cost, which is determined by the first-in, first-out method, or market.

(h) Contributions

Contributions, including unconditional promises, or pledges, are recognized as revenues in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value at the date of the gift. Contributions to be received after one year are discounted, at a range of 2% to 4%, to their present value. Amortization of the discount is recorded as additional contribution revenue and used in accordance with donor-imposed restrictions, if any, on the contributions. Allowance is made for uncollectible contributions based upon management's judgment and analysis of the creditworthiness of the donors, past collection experience and other relevant factors.

(i) Investments and Spending Policy

The University's investments are comprised of the assets of the University's endowment and other investments held for general operating purposes. The University reports those investments at fair value as described further in note 12.

The Board of Trustees interprets NYPMIFA to allow for the spending of income and gains on investments of permanently restricted net assets in a manner that is prudent, considering such factors as the duration and preservation of the endowment fund, the purposes of the institution and the endowment fund, general economic conditions including the potential effect of inflation or deflation, the expected total return of the fund, other resources of the University, the needs of the University and the fund to make distributions and preserve capital, and the University's investment policy.

Investment of the University's net assets held for endowment and similar purposes is based upon a total return policy, and the utilization of its endowment resources for current operating and capital needs is related to this policy. Although NYPMIFA does not preclude the University from spending below the original gift value of permanently restricted funds, the University's policy is to spend no more than a stated percentage of fair value of its investment portfolio over time. Accordingly, during fiscal year 2012, the Board of Trustees authorized the use of total return (income and appreciation) from its endowment resources at an aggregate rate of 5.9% (5.9% during fiscal year 2011) of the average fair value of its consolidated investment portfolio for the most recent five years. To the extent that the total return requirement for the current year is not fulfilled by interest and dividends, the University utilizes the appreciation of its endowment and similar net assets for operating purposes. To the extent that the total return requirement for the current year is exceeded by interest and dividends, the University reinvests the excess in its net assets held for endowment and similar purposes.

The University, in compliance with NYPMIFA, notified available donors who had established endowments prior to September 17, 2010, of the new law, and offered these donors the option of requiring the University to maintain historical dollar value for their endowment funds. A minority of donors requested this option; for those who did, the University has designed procedures to ensure that the University maintains historical dollar value.

Investment securities are exposed to various risks, such as interest rates, market, economic conditions, world affairs, and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in value could occur in the near term and such changes could materially affect the amounts reported in the investments and investment activity of the University.

In prior years, the University participated in securities lending activities. All loans where callable at any time and were fully collateralized. Investments that were loaned to another institution were included in investments held for long-term purposes on the consolidated balance sheet. Cash received as collateral on the securities lending transactions was reported as collateral held for securities lending on the consolidated balance sheet. Since the collateral had to be returned in the future, a corresponding liability was reported on the consolidated balance sheet. During fiscal year 2012, the University decided to no longer participate in securities lending activities.

(j) Property, Plant, and Equipment

Property, plant, and equipment are stated at cost or at estimated fair value if acquired by gift, less accumulated depreciation and amortization. Buildings used for research activities are componentized as site improvements, buildings, building services, and fixed equipment. Depreciation of research building components is recorded using the straight-line method over the useful lives of the components ranging from 4 to 50 years. Depreciation of non-research buildings, equipment and library books, and amortization of leasehold and land improvements are computed using the straight-line method over the estimated useful lives of the assets. Land and museum collections are not subject to depreciation. Estimated useful lives for non-research assets are as follows:

	Years
Building	40
Building and leasehold improvements	20
Land improvements	20
Equipment	4 to 15
Library books	10

The University reports gifts of property, plant, and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as temporarily restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the University reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

(k) Museum Collections

The University capitalizes museum collections. If purchased, collection items are capitalized at cost, and if donated, at their appraised or fair value on the accession date (the date on which the item is accepted by the Board of Trustees). There is no depreciation recorded on collection items.

(l) Split Interest Agreements and Perpetual Trusts

The University's split interest agreements with donors consist primarily of gift annuities, unitrusts, charitable remainder annuity trusts, and life income agreements. Assets held under these agreements are included in investments held for long-term purposes and investments in perpetual trusts held by others. For fiscal years 2012 and 2011, the fair values for split interest agreements assets are $78,750 and $81,119, respectively. Generally, contribution revenues are recognized at the dates the agreements are established and liabilities are recorded for the present value of the estimated future payments to be made to the beneficiaries. The liabilities are adjusted during the term of the trusts for changes in the value of the assets, accretion of the discount and other changes in the estimates of future benefits. The University is also the beneficiary of certain perpetual trusts held and administered by others. The present values of the estimated future cash receipts, which are measured by the fair value of the assets contributed to the trust, are recognized as assets and contribution revenues at the dates the trusts are established. The carrying value of the assets is adjusted for changes in the fair value of the trust assets for both split interest agreements and perpetual trusts.

(m) Refundable U.S. Government Grants for Student Loans

Funds provided by the United States Government under the Federal Perkins, Nursing and Health Professions Student Loan programs are loaned to qualified students and may be re-loaned after cash collections. These funds are ultimately refundable to the government and are recognized as a liability in the accompanying consolidated balance sheet.

(n) Grants and Contracts

Revenue from grants and contracts, primarily for research and training programs, is generally recognized as earned, that is, as the related costs are incurred under the grant or contract agreements. Amounts received in advance are reported as advance receipt of sponsored research revenues.

Grants and contracts awarded to the University are subject to audit by the various sponsoring agencies. Indirect costs recovered on grants and contracts are recorded at rates established by the University with the federal government, or predetermined by the non-federal sponsor. Indirect cost rates for government grants and contracts are subject to audit, and subsequent final settlements are recorded as current period adjustments. Management believes the impact of any future settlements to be immaterial to the consolidated financial statements.

(o) Benefit Plans

The University provides certain health care and life insurance benefits to retired employees and spouses under a defined benefit plan. Benefits include basic medical and major medical coverage. Certain categories of retirees receive dental coverage and group life insurance. Such post-retirement benefits are accounted for as a form of deferred compensation over the estimated service lives of employees.

Post-employment benefits include benefits provided to former or inactive employees after employment but before retirement. For the University, such benefits include workers' compensation benefits, short-term disability benefits, and benefits provided under various other programs.

(p) Hospital and Faculty Practice Patient Care Activities

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare

Under the Medicare program, the Hospital receives reimbursement under a prospective payment system

(PPS) for inpatient services. Under the hospital inpatient PPS, fixed payment amounts per inpatient discharge are established based on the patient's assigned diagnosis related group (DRG). When the estimated cost of treatment for certain patients is higher than the average, providers typically will receive additional "outlier" payments. The Hospital also receives reimbursement under a prospective payment system for certain medical outpatient services, based on service groups, called ambulatory payment classifications (APCs). Other outpatient services are based upon a fee schedule and/or actual costs. The Hospital's Medicare cost reports are subject to audit by the fiscal intermediary. Such audits have been done through December 31, 2005.

Medicaid and Other Third-Party Payors

The New York Health Care Reform Act of 1996 (HCRA), as amended, governs payments to hospitals in New York State (NYS).

Under HCRA, Medicaid, workers compensation, and no-fault payors payment rates are promulgated by the New York State Department of Health (DOH). Fixed payment amounts per inpatient discharge are established based on the patient's assigned case mix intensity similar to a Medicare DRG. All other third-party payors, principally Blue Cross, other private insurance companies, Health Maintenance Organizations (HMOs), Preferred Provider Organizations (PPOs) and other managed care plans, negotiate payment rates directly with the hospitals. Such arrangements vary from DRG-based payment systems, to per diems, case rates and percentage of billed charges. If such rates are not negotiated, then the payors are billed at the Hospital's established charges. Effective December 1, 2009, NYS implemented inpatient reimbursement reform. The reform updated the data utilized to calculate payment rates utilizing All Patient Refined DRGs (APR-DRGs). APR-DRGs used revised service intensity weights (SIWs) to adjust each APR-DRG for patient acuity. Similar type outpatient reforms were implemented effective December 1, 2008 by connecting outpatient payments to Ambulatory Payment Groups (APGs) which use outpatient SIWs based on types of service and resource consumption.

In addition, under HCRA, all non-Medicare payors are required to make surcharge payments for the subsidization of indigent care and other health care initiatives. The percentage amounts of the surcharge vary by payor and apply to a broader array of health care services. Also, certain payors are required to provide additional funds through surcharges on payments to hospitals for inpatient services or through voluntary election to pay a covered lives assessment directly to the DOH.

Revenue from Blue Cross and Preferred Care accounted for approximately 28% and 6%, respectively, of the Hospital's net patient service revenue for the year ended June 30, 2012, and 27% and 7%, respectively, for the year ended June 30, 2011.

Revenue from Medicare and Medicaid programs accounted for approximately 32% and 18%, respectively, of the Hospital's net patient revenue for the fiscal year ended June 30, 2012, and 32% and 17%, respectively, for the year ended June 30, 2011. Laws and regulation governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by material amounts in the near term. The Hospital believes that it is in compliance, in all material respects, with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. Compliance with such laws and regulations can be subject to future government review and interpretation. Non-compliance with such laws and regulations could result in repayments of amounts improperly reimbursed, substantial monetary fines, civil and criminal penalties and exclusion from the Medicare and Medicaid programs.

Both federal and NYS regulations provide for certain adjustments to current and prior years' payment rates and indigent care pool distributions based on industry-wide and hospital-specific data. The Hospital has established estimates based on information presently available of the amounts due to or from Medicare, Medicaid, workers compensation, and no-fault payors and amounts due from the indigent care pool for such adjustments. Those adjustments, which can be reasonably estimated, have been provided for in the accompanying financial statements. The Hospital has estimated the potential impact of such adjustments based on the most recent information available. However, those which are either (a) without current specific regulations to implement such adjustments, or (b) are dependent upon certain future events and cannot be reasonably estimated, have not been provided for in the accompanying financial statements. Management believes the amounts recorded in the accompanying financial statements will not be materially affected upon the implementation of such adjustments. During fiscal years 2012 and 2011, the Hospital recognized approximately $19,300 and $17,300 of net patient service revenue as a result of changes in estimates related to third party settlements. In addition, the Hospital recognized additional third party payables of approximately $17,800 and $16,000 related to fiscal years 2012 and 2011, respectively.

There are various other proposals at the federal and NYS levels relating to Medicare and Medicaid, that could, among other things, reduce reimbursement rates, modify reimbursement methods or increase managed care penetration. The ultimate outcome of these proposals and other market changes cannot presently be determined.

The University of Rochester Medical Faculty Group (URMFG) is an operating division of the University. In the year ending June 30, 2012, over 1,111 full-time faculty in 18 clinical departments and two clinical centers participated in patient care at the University of Rochester Medical Center. These full-time faculty physicians handled 871,333 outpatient visits in their offices, mostly on University-owned or leased premises; and covered 35,802 hospital admissions, as well as participated in the coverage of the emergency department handling over 99,523 visits. Payments for these services are derived primarily from third-party insurers including Managed Care companies (19.67%), Medicare (21.93%), Blue Shield (24.20%), Medicaid (10.59%), commercial (9.03%), other (5.25%), and self-pay (9.33%).

In addition to providing clinical outpatient care, the faculty group's mission is met by providing education and teaching. The faculty supervise and instruct 436 University medical students and 782 residents and fellows.

(q) Charity Care and Provision for Bad Debts

As further described in Note 17, the University provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, these are not reported as revenue or patient accounts receivable.

The University grants credit without collateral to patients, most of whom are local residents and are insured under third-party arrangements. Additions to the allowance for uncollectible accounts are made by means of the provision for bad debts. Accounts written off as uncollectible are deducted from the allowance and subsequent recoveries are added. The amount of the provision for bad debts is based upon management's assessment of historical and expected net collections, business and economic conditions, trends in Federal and State governmental healthcare coverage and other collection indicators.

(r) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses during the reporting period. Management's assumptions are primarily related to the appropriate discount rate for the purposes of fair value calculations, allowances for doubtful accounts, self-insured risks, and third-party payor contractual adjustments and allowances. Actual results may differ from those estimates.

(s) Investment in Net Assets of Foundation

The University accounts for its interest in the net assets of the James P. Wilmot Foundation, Inc. (Foundation) in accordance with not-for-profit guidance. The guidance establishes standards for transactions in which a donor transfers assets to a not-for-profit organization or charitable trust, which then agrees to transfer those assets, the return on investment of those assets, or both to a beneficiary specified by the donor. Under the accounting guidance, the University is required to recognize the net assets and its share of the change in the net assets of the Foundation. The Foundation was established for the support of cancer research at the University's School of Medicine and Dentistry.

(t) Asset Retirement Obligations

The University accounts for asset retirement obligations in accordance with asset retirement and environmental obligations guidance. This guidance primarily affects the way the University accounts for asbestos-related removal costs. The University accrues for asset retirement obligations in the period incurred if sufficient information is available to reasonably estimate the fair value of the obligation. Over time, the liability is accreted to its settlement value. Upon settlement of the liability, the University will recognize a gain or loss for any difference between the settlement amount and liability recorded.

(u) Derivative Instruments and Hedging Activities

Derivative instruments related to the University's long-term debt are included in accounts payable and accrued expenses or in accounts receivable, net on the consolidated balance sheet. The change in the fair value of the derivative instruments is included in the net depreciation/appreciation in the statements of activities. The University selected the combination of variable rate bond issues and interest rate swap agreements to obtain fixed rate financing at the lowest available cost at the time of the transactions. The University is exposed to credit loss in the event of nonperformance by the counterparty to its long-term rate swaps. The interest rate swaps do not qualify for cash flow hedge accounting.

(v) Reclassification

Certain amounts in previously issued financial statements have been reclassified to conform to the current year presentation.

(dollars in thousands)

(2) Net Assets

Unrestricted net assets consist of the following at June 30:

	2012	2011
Designated:		
University divisions	$ 1,068,151	$ 1,035,335
Highland Hospital and affiliates	98,123	112,615
Eastman Dental Center Foundation	23,602	21,226
Other related entities	(24,927)	(20,146)
Total designated	1,164,949	1,149,030
Net investment in property, plant, and equipment	550,403	618,085
Undesignated	30,321	51,594
Total unrestricted net assets	$ 1,745,673	$ 1,818,709

Temporarily restricted net assets consist of the following at June 30:

	2012	2011
Accumulated appreciation on permanently restricted net assets subject to board appropriation and/or purpose restrictions	$ 387,543	$ 410,780
Interest in net assets of foundation	12,330	13,743
Related entities	720	897
Other gifts and income subject to:		
Purpose restrictions	19,670	14,872
Time restrictions:		
Contributions receivable	60,299	35,642
Split-interest agreements	28,971	30,282
Total temporarily restricted net assets	$ 509,533	$ 506,216

Permanently restricted net assets consist of the following at June 30:

	2012	2011
Perpetual endowment funds	$ 310,209	$ 286,849
Interests in perpetual trusts held by others	46,877	49,780
Split-interest agreements	3,077	2,758
Perpetual loan funds	3,670	3,634
Contributions receivable	30,628	15,914
Total permanently restricted net assets	$ 394,461	$ 358,935

(dollars in thousands)

Endowment net assets consist of the following at June 30, 2012:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor - restricted funds:				
True endowments	$ -	$ 386,425	$ 310,209	$ 696,634
Term endowments	-	1,118	-	1,118
	-	387,543	310,209	697,752
Funds functioning as endowment (quasi)	824,814	-	-	824,814
Total endowment funds	$ 824,814	$ 387,543	$ 310,209	$ 1,522,566

Rollforward of endowment net assets from July 1, 2011 to June 30, 2012:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, July 1, 2011	$ 861,660	$ 410,780	$ 286,849	$ 1,559,289
Investment return:				
Investment income, net of fees	6,652	5,467	-	12,119
Net appreciation	6,335	5,649	-	11,984
Total investment return	12,987	11,116	-	24,103
New gifts	1,666	920	21,746	24,332
Amounts appropriated for expenditure	(48,759)	(35,597)	-	(84,356)
Other changes and reclassifications	(2,740)	324	1,614	(802)
Endowment net assets, June 30, 2012	$ 824,814	$ 387,543	$ 310,209	$ 1,522,566

Endowment net assets consist of the following at June 30, 2011:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor - restricted funds:				
True endowments	$ -	$ 409,603	$ 286,849	$ 696,452
Term endowments	-	1,177	-	1,177
	-	410,780	286,849	697,629
Funds functioning as endowment (quasi)	861,660	-	-	861,660
Total endowment funds	$ 861,660	$ 410,780	$ 286,849	$ 1,559,289

(dollars in thousands)

Rollforward of endowment net assets from July 1, 2010 to June 30, 2011:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, July 1, 2010	$ 988,403	$ 94,100	$ 263,528	$ 1,346,031
NYPMIFA adjustment	(239,778)	239,778	-	-
Investment return:				
Investment income, net of fees	9,643	7,718	-	17,361
Net appreciation	136,375	104,636	-	241,011
Total investment return	146,018	112,354	-	258,372
New gifts	1,512	487	19,201	21,200
Amounts appropriated for expenditure	(48,502)	(34,946)	-	(83,448)
Other changes and reclassifications	14,007	(993)	4,120	17,134
Endowment net assets, June 30, 2011	$ 861,660	$ 410,780	$ 286,849	$ 1,559,289

(3) Accounts Receivable

Accounts receivable at June 30 consist of the following:

	2012	2011
Patient care and related activities, net of allowances for doubtful accounts of $31,832 and $31,897	$ 144,464	$ 150,648
Federal, state and local governments, foundations and companies, net of allowances for doubtful accounts of $541 and $598	41,088	42,835
Medical resident FICA refund claim (including interest), net of allowance of $16,818 and $16,818	31,718	31,520
Student receivables, net of allowances for doubtful accounts of $3,287 and $2,686	4,488	6,100
Royalties and other	104,015	61,066
Total accounts receivable	$ 325,773	$ 292,169

(dollars in thousands)

(4) Contributions

Contributions receivable, net, are summarized as follows at June 30:

	2012	2011
Unconditional promises expected to be collected in:		
Less than one year	$ 7,818	$ 3,181
One year to five years	72,385	43,802
More than five years	48,424	25,991
Subtotal	128,627	72,974
Less unamortized discount and allowance for uncollectible amounts	(37,700)	(21,418)
Total contributions receivable, net	$ 90,927	$ 51,556

At June 30, 2012, the University had also received $168,160 in bequest intentions and certain other conditional promises to give. These intentions and conditional promises to give are not recognized as assets. If they are received, they generally will be restricted for specific purposes stipulated by the donor, primarily endowments for faculty support, scholarships or general operating support of a particular department or division of the University.

The University expended $36,226 and $34,897 for University relations and development for the years ended June 30, 2012 and 2011, respectively.

(5) Notes Receivable

Notes receivable, net, are summarized as follows at June 30:

	2012		
	Gross Receivable	**Allowance**	**Net Receivable**
Federal student loans	$ 17,009	$ 904	$ 16,105
Institutional student loans	4,366	606	3,760
Other note receivable	28,482	-	28,482
Total	$ 49,857	$ 1,510	$ 48,347

	2011		
	Gross Receivable	**Allowance**	**Net Receivable**
Federal student loans	$ 17,002	$ 904	$ 16,098
Institutional student loans	4,032	606	3,426
Other note receivable	28,482	-	28,482
Total	$ 49,516	$ 1,510	$ 48,006

Student loan programs are funded by donor contributions, other institutional sources and governmental programs, primarily the Federal Perkins Loan Program. The amounts received from the federal government's portion of the Perkins program are ultimately refundable to the federal government and are reported as a liability on the University's consolidated balance sheet as refundable U.S. Government grants for student loans.

Credit worthiness is not a factor when granting a student a loan from institutional or federal resources; it is based on financial need. However, once the loan is in repayment status, the University monitors the aging of the student loans receivable.

Student loans are often subject to unique restrictions and conditions and, therefore, it is not practical to determine their fair values. The allowance is intended to provide for loans, both in repayment status and not yet in repayment status (borrowers are still in school or in the grace period following graduation), that may not be collected.

The other note receivable represents a $28,482 note receivable of the University of Rochester Real Estate Corporation (wholly-owned by the University) for a loan to the Chase NMTC Eastman Theatre Investment Fund LLC (a non-consolidated entity) which matures in December, 2049. The University receives interest only, at 1.0% during the first ninety months of the term. For the remainder of the term, the note shall bear interest at 1.7%, compounding annually, with a minimum of 1.0% principal payable annually, with all principal and any unpaid interest due on the maturity date. Refer to Note 8 (p) for further information.

(dollars in thousands)

(6) Investments Held for Long-Term Purposes

Investments were held for the following long-term purposes at June 30:

	2012	2011
Endowment and similar purposes	$ 1,601,323	$ 1,640,407
Property, plant and equipment purposes:		
Debt service reserves	17,892	13,515
Bond proceeds not yet expended	107,394	47,272
Other	4,494	2,187
Total property, plant and equipment purposes	129,780	62,974
Other purposes	91,851	79,975
Total investments held for long-term purposes	$ 1,822,954	$ 1,783,356

For investment purposes, substantially all investments held for endowment and similar purposes participate in one of several pools, each with its own investment policy and objectives. The investment pool assets are owned by the separate endowment and similar funds within each pool based on the percent ownership of each fund to the pool. Income, realized and unrealized gains and losses are distributed based on the percent ownership of the pooled assets measured at fair value.

The following table summarizes changes in relationships between cost and fair values of investments held for endowment and similar purposes:

	2012		
	Fair Value	Cost	Net Gains/ (Losses)
End of year	$ 1,601,323	$ 1,525,886	$ 75,437
Beginning of year	$ 1,640,407	$ 1,480,017	$ 160,390
Unrealized depreciation, net			(84,953)
Realized net gains for year			97,669
Net increase for year			$ 12,716

	2011		
	Fair Value	Cost	Net Gains/ (Losses)
End of year	$ 1,640,407	$ 1,480,017	$ 160,390
Beginning of year	$ 1,415,977	$ 1,428,432	$ (12,455)
Unrealized appreciation, net			172,845
Realized net gains for year			80,060
Net increase for year			$ 252,905

The University permits several of its investment managers to utilize forward contracts, currency options and futures with the specific authorization of the investment committee of the Board of Trustees. However, the University was not directly engaged in any of the above mentioned derivative transactions as of June 30, 2012 and 2011.

Management does not anticipate that losses, if any, resulting from its market or credit risks would materially affect the consolidated financial position of the University.

Investment fees were $33,615 and $32,427 for the years ended June 30, 2012 and 2011, respectively.

(dollars in thousands)

(7) Property, Plant, and Equipment

As of June 30, 2012 and 2011, the University's investment in property, plant and equipment is as follows:

	2012	2011
Buildings and improvements	$ 2,054,701	$ 1,934,740
Land improvements	45,717	42,805
Completed projects under leasehold agreements	10,148	9,086
Equipment owned	911,885	806,659
Library books	151,457	142,372
Subtotal	3,173,908	2,935,662
Less accumulated depreciation	1,787,538	1,676,285
Subtotal	1,386,370	1,259,377
Land	8,817	7,860
Museum collections	30,882	30,431
Construction in progress	135,888	156,107
Total property, plant and equipment, net	$ 1,561,957	$ 1,453,775

(dollars in thousands)

(8) Long-term Debt

The following is a summary of the University's long-term indebtedness at June 30:

	2012	2011
Obligations under capital lease agreements, 2.391% to 5.702% (a)	$ 2,665	$ 15,889
Urban Development Corporation Loan (b)	1,500	1,667
Direct Note Obligation – The Bank of New York, 5.40% to 5.75% (net of unamortized discount of $19 in 2012 and $21 in 2011) (c)	8,581	8,579
Bond payable – COMIDA, 10.00% (d)	567	598
Bonds payable – DHCR Series 1973A, 6.26% (e)	-	1,325
Bonds payable – DHCR Series 1979A, 8.40% (f)	-	300
Bonds payable – DASNY Series 1994B, 5.50% (g)	8,700	9,170
Bonds payable – DASNY Series 2001A, 2.90% to 5.00% (net of unamortized discount of $67 in 2011) (h)	-	13,952
Bonds payable – DASNY Series 2003A, B, and C, 3.97% (i)	106,755	114,904
Bonds payable – DASNY Series 2004A, 3.00 to 5.25% (net of unamortized premium of $337 in 2012 and $353 in 2011) (j)	25,562	26,283
Bonds payable – COMIDA, 3.125% to 5.450% (net of unamortized premium of $561 in 2012 and $661 in 2011) (k)	27,981	30,511
Bonds payable – DASNY Series 2006 A-1 and B-1, 3.919% (l)	111,180	111,180
Bonds payable – DASNY Series 2007A-1, A-2, B, and C, 4.000% to 5.000% (net of unamortized premium of $6,871 in 2012 and $7,121 in 2011) (m)	238,780	240,315
Bonds payable – DASNY Series 2009A, B, C, D, and E, 2.50% to 5.00% (net of unamortized premium of $2,270 in 2012 and $2,678 in 2011) (n)	96,913	106,523
Bonds payable – DASNY Series 2010, 2.00% to 5.20% (net of unamortized discount of $62 in 2012 and $65 in 2011) (o)	10,938	10,935
Notes payable – Eastman Theatre Renovation, 0.74% to 2.73% (p)	53,482	53,782
Bonds payable – MCIDC Series 2011 A and B, 2.00% to 5.00% (net of unamortized premium of $13,566 in 2012) (q)	171,766	-
Notes payable – Manufacturers and Traders Trust Bank, 3.28% (r)	8,839	-
Total long-term debt	$ 874,209	$ 745,913

The following is a description of the University's long-term debt:

(a) Obligations Under Capital Lease Agreements

The University entered into a tax-exempt capital lease program in November 2006 for $10,832. The lease is being repaid with quarterly payments of $573, including interest at 3.879% to 3.881% through November 2012. The leased equipment includes a network infrastructure upgrade and the purchase of an MRI.

In addition to the arrangement discussed above, the University and its related entities have entered into several other capital leases for equipment.

(b) Urban Development Corporation Loan

In March 1992, the New York State Urban Development Corporation (UDC) entered into an agreement with the University to partially fund the construction of the University's Center for Optoelectronics and Imaging (COI) with a loan of $5,000. The agreement requires the University to pay an amount equal to the debt service on the $6,320 tax-exempt bond issued by which UDC financed the loan and the associated reserve funds and costs of issuance. The loan is collateralized by a mortgage on the property.

Pursuant to an agreement authorized by statute, the State of New York leases the COI from the University for the 30-year term of the loan, paying, as rent, an amount sufficient to cover the University's obligations to UDC. These rents have been assigned to UDC as further collateral for the loan. The University retains possession of the property under a sub-lease from the State at an annual rent equivalent to one-thirtieth of the sum of the loan principal and the cost of issuance of the UDC bonds.

(c) Direct Note Obligation–The Bank of New York

Pursuant to an agreement between the University and the Bank of New York dated November 25, 2003, the Bank of New York issued $8,600 of notes known as the University of Rochester Direct Note Obligations, Series 2003. The Series 2003 notes were issued to refinance drawings under the University's revolving line of credit with JPMorgan Chase Bank. The line of credit had been used to refinance indebtedness and certain other mortgages related to Eastman Place. Eastman Place is a facility used partly to house activities of the Eastman School of Music.

The Series 2003 notes are general, unsecured obligations of the University.

(d) Bond Payable – COMIDA

Pursuant to an agreement between the University and the County of Monroe Industrial Development Agency (COMIDA) dated January 6, 2004, COMIDA issued a replacement bond in the amount of $698. The 2004 COMIDA Replacement bond is for the purchase of property at 10 Gibbs Street, Rochester, New York which has become part of the Eastman School of Music campus.

(e) Bonds Payable – DHCR Series 1973A

Pursuant to an agreement with a University related entity (Crittenden Boulevard Housing Company, Inc.) and the New York State Division of Housing and Community Renewal (DHCR) dated September 1973, DHCR issued and sold $7,065 of Series A bonds. The related entity was repaying the indebtedness at an average rate of 6.26%.

The Series 1973A bonds were paid off during fiscal year 2012.

(f) Bonds Payable – DHCR Series 1979A

Pursuant to an agreement with a University related entity (Crittenden Boulevard Housing Company, Inc.) and the New York State Division of Housing and Community Renewal (DHCR) dated April 1979, DHCR issued and sold $7,670 of Series 1979A bonds. The related entity was repaying the indebtedness at an average rate of 8.4%.

The Series 1979A bonds were paid off during fiscal year 2012.

(g) Bonds Payable – DASNY Series 1994B

Pursuant to an agreement with a University related entity (Highland Hospital and affiliates) and DASNY, $13,000 of Series 1994B Revenue Bonds were issued and sold by DASNY. The related entity is repaying the indebtedness at a fixed rate of 5.50%, maturing July 1, 2023.

During fiscal year 2009, the Series 1994B bonds were remarketed and converted from a fixed interest rate to a variable interest rate determined by the bond agent. The terms related to principal repayment did not change.

The bond issue is collateralized by an interest in certain buildings and equipment and an irrevocable direct pay letter of credit held by HSBC Bank which expires July 2015.

(h) Bonds Payable – DASNY Series 2001A

Pursuant to an agreement between the University and DASNY dated July 10, 2001, DASNY issued and sold $22,920 of bonds known as the University of Rochester Revenue Bonds, Series 2001A. The Series 2001A bonds were issued at a discount of $152 resulting in net proceeds of $22,768 to refinance (1) all the outstanding $184 University's Dormitory (Apartment) bonds of 1962, HUD Series D and all the outstanding $840 University's Dormitory (Apartment) bonds of 1966, HUD Series E and (2) a portion of the University of Rochester Revenue Bond, Series 1994A, maturing on and after July 1, 2007.

During fiscal year 2012, the Series 2001A bonds were refinanced under Series 2011A. A loss on debt extinguishment due to bond restructuring of $636 was recognized.

(i) Bonds Payable – DASNY Series 2003A, B, and C

Pursuant to an agreement with the University and DASNY dated October 29, 2003, DASNY issued and sold $164,425 of bonds known as the University of Rochester Revenue Bonds, Series 2003, consisting of $32,550 Series 2003A bonds, $49,650 Series 2003B bonds and $82,225 Series 2003C bonds.

Series 2003A bonds were issued to finance (1) an expansion of the Laboratory for Laser Energetics building to accommodate the construction of a federally funded laser expansion; (2) renovation of space to house a functional MRI; (3) deferred maintenance remediation in various buildings and (4) renovation and information technology upgrades in various faculty offices, laboratory space and student residential buildings. A portion of the proceeds from Series 2003A also refinanced the remaining portion of the University of Rochester Revenue Bonds, Series 1987.

Series 2003B bonds were issued to finance (1) equipment acquisitions for the Hospital; (2) the expansion of an existing garage and (3) laboratory relocations at the Hospital. Series 2003B bonds also refinanced University of Rochester Series 1993A bonds and a portion of the University of Rochester Series 1994 bonds.

Series 2003C bonds were issued to finance (1) construction of an Adult Intensive Care Unit; (2) renovations of the Cancer Center and (3) deferred maintenance, renovations and improvements to faculty offices, laboratory and clinical spaces for various departments and areas within the Hospital and School of Medicine and Dentistry. Series 2003C also refinanced a portion of the University of Rochester Series 1994 bonds.

On July 31, 2003, the University executed interest rate swaps with third parties. The University entered into interest rate swap agreements to exchange variable rate debt for a fixed rate obligation without the exchange of the underlying principal amount. Generally under this agreement, the counterparty pays the University a variable interest rate equal to 61.5% of one-month LIBOR plus 56 basis points. The University will pay the counterparty a fixed interest rate of 3.97%. These rates are subject to change based upon certain conditions as stated in the swap agreement. The contractual relationship under this agreement will last until July 1, 2033.

During fiscal year 2009, the Series 2003A, B and C bonds were restructured and converted from an auction rate to a variable rate as determined by the remarketing agent. The terms related to principal repayment did not change. The bonds have a corresponding letter of credit available at varying financial institutions, individually, in amounts totaling the outstanding debt service of each bond.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

The University has a letter of credit in place for DASNY Series 2003A and 2003C in the amount of $103,502 with JP Morgan Chase Bank, N.A which expires in March 2013. Of this total, no amounts were outstanding at June 30, 2012 and 2011.

The University has a letter of credit in place for DASNY Series 2003B in the amount of $34,745 with HSBC Bank, N.A which expires in September 2013. Of this total, no amounts were outstanding at June 30, 2012 and 2011.

(j) Bonds Payable – DASNY Series 2004A

Pursuant to an agreement between the University and DASNY dated August 26, 2004, DASNY issued $45,000 of bonds known as the University of Rochester Revenue Bonds, Series 2004A. The Series 2004A bonds were issued at a premium of $603, resulting in proceeds of $45,603, to finance the construction of a cogeneration facility to provide supplementary heat and/or electricity to the University and will also provide an addition to the University's central utility plant.

A portion of the Series 2004A bonds were refinanced as a result of the issuance of Series 2007C during fiscal year 2007.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

(k) Bonds Payable – COMIDA

Pursuant to an agreement with a University related entity (Highland Hospital and affiliates) and the County of Monroe Industrial Agency (COMIDA) dated June 23, 2005, COMIDA issued and sold $20,000 of fixed rate Civic Facility Revenue Refunding Bonds and $14,920 of fixed rate Civic Facility Revenue Project Bonds. The COMIDA Refunding Bonds were issued at a premium of $912 and were used to refund a portion of Series 1997A debt. These refunding bonds are collateralized by amounts in a debt service reserve fund. The COMIDA Project Bonds were issued at a premium of $362 and were issued to finance (1) the Park Ridge Oncology Project, (2) the Bariatric Surgery Project, (3) the Orthopedic Operating Room Project and (4) various renovation projects throughout Highland Hospital. These bonds are collateralized by the construction projects noted above. In addition, Highland Hospital issued $6,135 of direct taxable notes on June 23, 2005 to refund the remaining portion of Series 1997A and all of Series 1997B debt. These notes were issued at a discount of $5 and are collateralized by amounts in a debt service reserve fund.

(l) Bonds Payable – DASNY Series 2006A-1 and B-1

Pursuant to an agreement between the University and DASNY dated March 16, 2006, DASNY issued and sold $111,180 of bonds known as the University of Rochester Revenue Bonds, Series 2006, consisting of $94,130 Series 2006A-1 bonds and $17,050 Series 2006B-1 bonds. The Series 2006A-1 bonds were issued to refinance the University of Rochester Series 1999A bonds and portions of the University of Rochester Series 1997A bonds, the University of Rochester Series 1998A bonds and the University of Rochester Series 2000A bonds. The Series 2006B-1 bonds were issued to refinance portions of the University of Rochester Series 1999B bonds.

On March 16, 2006, the University executed interest rate swaps with a third party. The University entered into an interest rate swap agreement to exchange variable rate debt for the fixed rate obligation without the exchange of the underlying principal amount. Generally, under this agreement, the counterparty will pay the University a variable-interest rate based on the Bond Market Association (BMA) Municipal Swap Index. The University will pay the counterparty a fixed interest rate of 3.919%. These rates are subject to change based upon certain conditions as stated in the swap agreement. The contractual relationship under this agreement will last until July 1, 2027.

During fiscal year 2009, the Series 2006A-1 and B-1 bonds were restructured and converted from an auction rate to a variable rate as determined by the remarketing agent. The terms related to principal repayment did not change. The bonds have a corresponding letter-of-credit available at varying financial institutions, individually, in amounts totaling the outstanding debt service of each bond.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

The University has a letter of credit in place in the amount of $112,642 with Bank of America, N.A, which expires in September 2014. The letter of credit has a renewal option that can be exercised every three years. Of this total, no amounts were outstanding as of June 30, 2012 and 2011.

(m) Bonds Payable – DASNY Series 2007A-1, A-2, B and C

Pursuant to an agreement between the University and DASNY dated February 21, 2007, DASNY issued and sold $235,869 of bonds known as the University of Rochester Revenue Bonds, Series 2007, consisting of $111,210 Series 2007A-1 bonds, $20,534 Series 2007A-2 bonds, $40,290 Series 2007B bonds and $63,835 Series 2007C bonds. The Series 2007 bonds were issued at a net premium of $8,207 resulting in proceeds of $244,076.

Series 2007A-1 bonds were issued to finance (1) the construction of the University's portion of the Cancer Center; (2) the acquisition and renovation of a new University Data Center; (3) an upgrade to the central utilities chilled water capacity and the expansion of its infrastructure; (4) the construction of a new animal facility and the renovation of existing laboratory space at the Aab Cardiovascular Research Institute; (5) the construction or renovation of a University Health Service building; and (6) various deferred maintenance projects and renovations of laboratories, office space and student residential buildings.

Series 2007A-2 bonds were issued to finance (1) the renovation of the University Advancement and Alumni Center; and (2) the construction of the Goergan Hall for biomedical engineering and optics programs.

Series 2007B bonds were issued to finance (1) the construction of the Hospital's portion of the Cancer Center; (2) the renovation of the Hospital's surgical adult intensive care and intermediate care units; (3) the renovation of the Hospital's medical behavioral inpatient unit; and (4) the purchase of equipment for the Hospital.

Series 2007C bonds were issued to refinance (1) a portion of the University of Rochester Series 1998A bonds; and (2) a portion of the University of Rochester Series 2004A bonds.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

(n) Bonds Payable – DASNY Series 2009A, B, C, D and E

Pursuant to an agreement between the University and DASNY dated July 22, 2009, DASNY issued and sold $117,279 of bonds known as the University of Rochester Revenue Bonds, Series 2009, consisting of $54,469 Series 2009A bonds, $34,460 Series 2009B bonds, $11,135 Series 2009C bonds, $3,625 Series 2009D bonds and $13,590 Series 2009E bonds. The Series 2009 bonds were issued at a net premium of $3,463 resulting in proceeds of $120,742.

Series 2009A bonds were issued to finance (1) fire alarm replacements, sprinkler installations, and renovations in undergraduate halls; (2) renovations to laboratories and offices throughout the River Campus and Medical Center ; (3) the renovation of Wilson Commons dining hall; (4) central utilities infrastructure improvements for the River Campus and Medical Center; (5) various deferred maintenance and renovation projects at the Eastman School and Medical Center campuses; (6) a portion of the construction of the Saunders Research Building.

Series 2009B bonds were issued to refinance the remaining outstanding bonds for Series 1997A, Series 1998A, and Series 2000A.

Series 2009C bonds were issued to finance the relocation of certain electrical switchgear within the Medical Center.

Series 2009D bonds were issued to refinance the outstanding bonds for Series 1999B.

Series 2009E bonds were issued to finance a portion of the construction of the Saunders Research Building.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

(o) Bonds Payable - DASNY Series 2010

Pursuant to an agreement with a University related entity (Highland Hospital and affiliates) and DASNY dated June 25, 2010, DASNY issued and sold $11,000 of bonds known as Highland Hospital Revenue Bonds, Series 2010. The Series 2010 bonds were issued at a net discount of $68 resulting in proceeds of $10,932.

Series 2010 bonds were issued to finance the following: (1) the creation of a twenty-two bed Neuromedicine Inpatient Unit; and (2) the enhancement and expansion of the space, equipment, and technology used for Perioperative Services.

(p) Notes Payable – Eastman Theatre Renovation

In December 2009, the University entered into a financing arrangement for the renovation of the Eastman Theatre enhanced by qualified investors in the New Markets Tax Credit program. This transaction resulted in $53,782 in new external consolidated debt and $28,482 in new external notes receivable to the University.

Several loans were created through the NMTC financing structure. The first is an ordinary bank loan from JPMorgan Chase for $15,482 at a cost of LIBOR plus 2.5% for a seven-year term. After seven years, this loan is expected to be refinanced by tax-exempt bonds and amortized in equal payments over thirty years. The remaining loans are specialized NMTC notes payable totaling $38,300 at a cost of 0.74% for forty years, maturing on December 18, 2049. The University is required to pay interest only on these promissory notes for the first seven years. The lenders of the notes payable are a group of Community Development Entities that will receive significant tax credits as a result of this loan.

The University loaned $28,482 to an investment fund as a part of the setup of the community development entities. The external note receivable matures on December 18, 2049. Refer to Note 5 for further information on the external notes receivable.

(q) Bonds Payable – MCIDC Series 2011 A and B

Pursuant to an agreement between the University and Monroe County Industrial Development Corporation (MCIDC) dated September 1, 2011, MCIDC issued and sold $161,660 of bonds known as the University of Rochester Tax-Exempt Revenue Bonds, Series 2011, consisting of $122,340 Series 2011A bonds and $39,320 Series 2011B bonds. The Series 2011 bonds were issued at a premium of $14,088 resulting in proceeds of $175,748.

Series 2011A bonds were issued to finance (1) the renovation of Danforth Dining Center; (2) the construction of the Ronald Rettner Building to house the University’s digital media center and fabrication lab; (3) renovations to laboratories and offices throughout the River and Medical Center campuses; (4) various renovations for Fauver Stadium; (5) various deferred maintenance and renovation projects at the Eastman School of Music and related residential halls; (6) the construction of the O’Brien Residence Hall to house undergraduate students; (7) the renovation of various undergraduate and graduate residential facilities; (8) construction of the Raymond F. LeChase Hall to house the University’s Warner School of Education; (9) improvements and expansion of the central utilities plant; (10) renovation and modernization of the Medical Center storm sewer infrastructure; and (11) a portion of the Cancer Center Vertical Expansion improvements. A portion of Series 2011A was used to refinance all of the outstanding bonds for Series 2001A.

(dollars in thousands)

Series 2011B bonds were issued to finance (1) a portion of the Cancer Center Vertical Expansion improvements; (2) the relocation of the Bone Marrow Transplant Unit; (3) the replacement of the air handler equipment within Strong Memorial Hospital, and (4) replacement of certain existing angiographic equipment.

The loan agreement and the obligation of the University to make payments under the loan agreement are general obligations of the University.

(r) Notes Payable – Manufacturers and Traders Trust Bank

Pursuant to an agreement between the University and the Manufacturers and Traders (M & T) Bank dated June 5, 2012, M & T Bank issued $9,000 of term notes. The note was issued to partially finance the purchase of the Lac De Ville facility. The University is repaying the indebtedness at a fixed rate of 3.28%, maturing April 2026.

The M & T Bank term notes are general, unsecured obligations of the University.

(s) Required Principal Payments

Required composite principal payments for long-term debt, net of unamortized discount or premium, for each of the years in the five-year period ending June 30, 2017 and thereafter are as follows:

Maturity	Principal Portions of Lease Payments	Principal Payments of Debt	Total Principal Payments
2013	$ 1,594	$ 29,138	$ 30,732
2014	342	31,388	31,730
2015	309	41,462	41,771
2016	169	53,346	53,515
2017	165	33,853	34,018
Thereafter	86	682,357	682,443
Total	$ 2,665	$ 871,544	$ 874,209

The University incurred $30,604 and $29,344 of interest expense for the years ended June 30, 2012 and 2011, respectively, net of interest capitalization of $4,454 and $2,766 for the years ended June 30, 2012 and 2011, respectively.

The University has letter of credit agreements with various financial institutions to purchase the University's variable rate demand bonds in the event they cannot be remarketed. In the event that the bonds covered by these agreements are not remarketable and the agreements are not otherwise renewed, the principal amounts (including variable rate demand bonds not subject to a liquidity facility) would be $106,212, $48,781, $120,961, $36,910, $15,788, and $545,557 for the five-year period ending June 30, 2017 and thereafter.

(t) Fair Value of Long-Term Debt

The fair value of the University's long-term debt is estimated based upon the amount of future cash flows, discounted using the University's current borrowing rate for similar debt instruments of comparable maturities. The fair value of total long term debt, excluding capital leases, was $909,850 and $729,909 at June 30, 2012 and 2011, respectively.

(9) Benefits Plans

Self-insurance Plans – University

The University is self-insured for workers' compensation. Based on estimates provided by actuaries, liabilities for asserted and unasserted claims under the workers' compensation program at June 30, 2012 were discounted by 1.75% and amounted to $46,610 (3.50% and $42,686 in 2011). These liabilities are offset by receivables for the expected insurance direct payments against these claims of $9,110 at June 30, 2012 ($8,882 at June 30, 2011). The liabilities are included in accrued pension, post-retirement, and post-employment liabilities, and the receivables are included in other assets on the consolidated balance sheet. The University has a standby letter of credit with

JPMorgan Chase Bank to cover potential liabilities under the University's self-insured workers' compensation program.

The University is self-insured for health care benefits. Based on estimates provided by actuaries, the University's obligation for incurred but not reported claims was $11,983 and $11,035 as of June 30, 2012 and 2011, respectively. These amounts are included in accounts payable and accrued expenses on the consolidated balance sheet and have not been discounted.

Retirement Plan – University

The University provides defined contribution retirement plans to its employees. The University of Rochester's Retirement Program offers four investment company options that are administered by each of the separate investment companies. Under these plans, the University made contributions of $73,395 and $70,334 in 2012 and 2011, respectively, which were vested for the benefit of the participants.

Post-retirement Benefit Plan – University

The University's post-retirement benefit plan includes basic medical, major medical, dental coverage, and life insurance. Benefit levels differ for current retirees, current employees eligible to retire, and current employees not eligible to retire.

The University incurred post-retirement plan expense of $12,492 and $16,325 for the years ended June 30, 2012 and 2011, respectively, which is recorded in fringe benefits expense on the consolidated statement of activities.

(dollars in thousands)

Benefit expense for this plan for the years ended June 30, 2012 and 2011 includes the following components:

	2012	2011
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 141,527	$ 143,377
Service cost	2,824	2,917
Interest cost	7,224	7,337
Estimated plan participant contributions	2,218	2,013
Actuarial (gain)/loss	21,005	(8,033)
Benefits paid	(10,096)	(9,244)
Amendments	-	3,160
Benefit obligation at end of year	$ 164,702	$ 141,527
Change in plan assets:		
Fair value of plan assets at beginning of year	$ -	$ -
Employer contributions	7,878	7,231
Participant contributions	2,218	2,013
Benefits paid	(10,096)	(9,244)
Fair value of plan assets at end of year	$ -	$ -
Components of accrued benefit:		
Funded status	$ (164,702)	$ (141,527)
Unrecognized net actuarial loss	39,360	18,678
Unrecognized prior service cost	6,742	8,863
Accrued benefits	$ (118,600)	$ (113,986)
Amounts recognized in the consolidated balance sheets consist of:		
Accrued post-retirement benefit cost	$ (113,986)	$ (104,892)
Net post-retirement benefit expense	(12,492)	(16,325)
Employer contributions	7,878	7,231
Accrued benefits	$ (118,600)	$ (113,986)
Amount recorded in unrestricted net assets	(46,102)	(27,541)
Net amount recognized in unrestricted net assets	$ (164,702)	$ (141,527)
Components of net periodic benefit cost:		
Service cost	$ 2,824	$ 2,917
Interest cost	7,224	7,337
Amortization of prior service cost	2,444	6,071
Net periodic benefit cost	$ 12,492	$ 16,325

(dollars in thousands)

Estimated future contributions, benefit payments, and 28% prescription subsidy payments are as follows:

	Estimated Contributions / Benefit Payments	Estimated 28% Rx Subsidy Payments
2013	$ 9,030	$ 967
2014	9,697	911
2015	10,204	947
2016	10,438	399
2017	10,675	379
2018 to 2022	54,299	1,514

Benefits are valued based upon the projected unit cost method. The weighted average assumptions used at the measurement date, July 1, are as follows:

	2012	2011
Discount rate for obligation	4.25%	5.25%
Expected return on plan assets	N/A	N/A
Rate of compensation increase	N/A	N/A
Health care cost trend rate – initial	10.00%	10.00%
Health care cost trend rate – final	4.50%	4.50%

The rate increase in health care costs was assumed to decrease to 4.50% in 2018 and to remain at that level thereafter.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one percentage-point change in the health care cost trend rate would have the following effects:

	One Percentage Point Increase	One Percentage Point Decrease
Effect on total of service and interest cost components	$ 816	$ (668)
Effect on post-retirement benefit obligation	$ 6,603	$ (5,596)

The Medicare Prescription Drug Improvement and Modernization Act of 2003 provides for a direct government subsidy for employers who continue to offer a retiree drug program that is deemed to be actuarially equivalent in the government plan. The University qualified for the Medicare Part D prescription drug federal subsidy.

Employers are required to recognize the over-funded or under-funded status of defined benefit pension and post-retirement plans as assets or liabilities in its consolidated balance sheet and to recognize changes in that funded status in the year in which the changes occur through changes in unrestricted net assets. In addition, employers are required to measure the funded status of the plan as of the consolidated balance sheet date.

Post-employment Benefits – University

Accrued post-employment benefits of the University amounted to $75,157 and $65,393 at June 30, 2012 and 2011, respectively.

Self-insurance Plans – Highland Hospital and Affiliates

Highland Hospital is self-insured for workers' compensation claim losses and expenses. A letter of credit in the amount of $7,397 is maintained as security for workers compensation claims. Included in accrued pension, post-retirement, and post-employment at June 30, 2012 and 2011 are accruals of approximately $13,193 and $10,534, respectively, for specific incidents to the extent that they have been asserted or are probable of assertion and can be reasonably estimated. These liabilities are offset by a receivable for the expected insurance direct payments against these claims of $1,557 and $1,767 at June 30, 2012 and 2011, respectively. This liability has been discounted by 0.75% and 1.75% at June 30, 2012 and 2011, respectively.

(dollars in thousands)

Retirement Plan –Highland Hospital and Affiliates

The retirement plan of Highland Hospital covers all employees who have completed two years of continuous employment. The benefits for this plan are based primarily on years of service and employees' pay near retirement. The funding policy is to contribute annually, an amount consistent with the requirement of the Employee Retirement Income Security Act. Plan assets consist principally of cash equivalents, common stocks and fixed income investments.

Retirement plan expense of $6,160 and $6,590 was incurred for the years ended December 31, 2011 and 2010, respectively, and is recorded in fringe benefits in the consolidated statement of activities. In addition, a pension related benefit other than net periodic pension cost of ($26,651) and ($4,635) for the years ending December 31, 2011 and 2010, respectively, was recorded in other changes on the consolidated statement of activities.

Pension expense for this plan for the years ended December 31, 2011 and 2010 includes the following components:

	2011	2010
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 121,482	$ 105,693
Service cost	4,542	4,739
Interest cost	6,586	6,235
Curtailment	-	(839)
Actuarial loss	21,205	8,458
Benefits paid	(3,219)	(2,804)
Benefit obligation at end of year	$ 150,596	$ 121,482

	2011	2010
Change in plan assets:		
Fair value of plan assets at beginning of year	$ 84,212	$ 73,648
Actual return on plan assets	(110)	7,657
Employer contribution	7,150	6,000
Benefits paid	(3,587)	(2,805)
Administrative expenses paid	-	(288)
Fair value of plan assets at end of year	$ 87,665	$ 84,212

	2011	2010
Amounts recognized in the balance sheets consist of:		
Accrued benefits	$ (4,026)	$ (5,016)
Amount recognized in unrestricted net assets	(58,905)	(32,254)
Funded Status	$ (62,931)	$ (37,270)
Components of net periodic benefit cost:		
Service cost	$ 4,542	$ 4,739
Interest cost	6,586	6,235
Expected return on plan assets	(7,353)	(6,401)
Amortization loss	2,385	2,017
Net periodic benefit cost	$ 6,160	$ 6,590
Weighted-average assumptions as of December 31:		
Discount rate for obligation	4.63%	5.48%
Discount rate for pension expense	5.48%	5.97%
Investment return assumption (regular)	8.00%	8.50%
Future compensation increase rate	3.60%	3.80%

The pension plan funds are allocated to two money managers, each with a balanced portfolio. These money managers monitor financial market funds and adjust inconsistent strategy accordingly.

The weighted-average asset allocation for the pension plan as of December 31, by asset manager categories is as follows:

	2011	2010
Weighted-average assumptions by asset categories:		
Equity securities	57%	54%
Fixed income securities	38%	40%
Cash and other investments	5%	6%
Total	100%	100%

(dollars in thousands)

Estimated future benefit payments for the years ending December 31:

2012	$	3,496
2013		3,973
2014		4,393
2015		4,910
2016		5,632
2017 to 2021		40,675
Total estimated future payments	$	63,079

Highland Hospital expects to contribute $8,770 to the plan in 2012 and contributed $7,150 to the plan in 2011.

The plan's asset allocation policy states the assets should be allocated as follows:

	2011	**2010**
Asset Category		
International equity	57%	54%
Fixed income	38%	40%
Inflation protection assets	5%	6%
Total	100%	100%

In addition, the total equity commitment should not exceed 75% of assets.

The asset allocation ranges established by this investment policy represent a long-term perspective, and as such, rapid unanticipated market shifts or changes in economic conditions may cause the asset mix to fall outside of the policy range. These divergences should be of a short-term nature.

Inflows and disbursements should be allocated such that the assets are rebalanced toward the target allocation.

The plan assets are invested with an outside trustee for the sole benefit of the plan participants. Investments are managed to maximize total return while maintaining a prudent level of risk.

The following assets were recorded at fair value within the plan assets of Highland Hospital as of December 31, 2011 and 2010, respectively. Fair value for Level 1 is based upon quoted market prices. Level 2 may be based on quoted prices for similar assets and/or inputs other than quoted prices that are observable for the asset or liability. Level 3, which primarily consists of a mutual fund investing in publicly traded stock, bonds, short-term investments, preferred stocks, warrants, asset backed securities, and mortgage backed securities.

The following assets were recorded at fair value within the plan assets of the related entity as of December 31:

Description	**Level 1**	**Level 2**	**Level 3**	**2011 Total Fair Value**
Cash	$ 370	$ -	$ -	$ 370
Mutual fund – global balanced asset	44,116	-	-	44,116
Mutual fund – multi asset	-	43,179	-	43,179
Total	$ 44,486	$ 43,179	$ -	$ 87,665

Description	**Level 1**	**Level 2**	**Level 3**	**2010 Total Fair Value**
Cash	$ 1,411	$ -	$ -	$ 1,411
Mutual fund – global balanced asset	41,135	-	-	41,135
Mutual fund – multi asset	-	41,666	-	41,666
Total	$ 42,546	$ 41,666	$ -	$ 84,212

(dollars in thousands)

(10) Investment in Captive Insurance Company

The Hospital, together with other universities and teaching hospitals, has formed a captive insurance company (captive) to insure the professional liability risks of the shareholders. The Hospital's investment in the captive represents 20% of the voting rights; however, the dissolution provisions of the captive agreement indicate that the Hospital's financial participation (based on percentage of premiums paid) is approximately 8% of the financial results of the captive. Due to the Hospital's significant influence in the captive, the investment in the captive has been recorded under the equity method.

The Hospital's premiums are based on its professional liability experience and a shared risk factor with the other participants. Premiums are subject to retrospective adjustment based on, among other things, actual loss experience of the Hospital.

The most recent audited financial information for the captive for years ended December 31 is summarized below:

		2011		2010
Results of operations				
Net earned premiums	$	169,622	$	210,377
Expenses		(214,203)		(244,235)
Investment income and realized gains on sales of marketable securities		48,183		43,927
Net income		3,602		10,069
Other comprehensive income / (loss)		(33,110)		58,824
Comprehensive income / (loss)		(29,508)		68,893
Net capital additions from shareholders		69,900		4,765
Change in shareholders' equity	$	40,392	$	73,658
Financial position				
Total assets	$	2,566,269	$	2,488,113
Total liabilities		2,297,209		2,259,444
Shareholders' equity	$	269,060	$	228,669

(11) Professional Liability Claims

The University's coverage for professional liability insurance is provided under insurance policies obtained jointly with other universities and teaching hospitals. The primary layer of coverage, as well as the buffer and self-insured layers of excess insurance, were written by MCIC Vermont, Inc. (a Risk Retention Group) formed and directed by the participating insured institutions. Multiple layers of excess insurance were purchased from several different insurance companies. The maximum coverage for the Medical Center is $221,000 per claim. The per claim coverage amount at each of the five participating institutions has been tailored to their own experience and exposures.

In fiscal year 2012, the University adopted the principles of insurance claim and recovery accounting for professional liability claims. These principle liability claims, and any anticipated insurance recoveries, to be reported on a gross basis versus the previous practice of netting the recoveries against liability claims. The insurance claims receivable, as calculated by the actuaries, was approximately $47,691 as of June 30, 2012, and has been included in other accounts receivable as shown in note 3. A corresponding increase to the accrued professional liability cost has been included in accounts payable and accrued expenses.

Based on estimates provided by the actuaries retained by MCIC Vermont, Inc., the University's obligations for incurred but not reported claims were $30,124 and $31,995 as of June 30, 2012 and 2011, respectively. These amounts have not been discounted and are included in accounts payable and accrued expenses on the consolidated balance sheet.

(dollars in thousands)

(12) Fair Value of Financial Instruments

The following tables present the fair value of the financial instruments recorded on the consolidated balance sheet as of June 30:

	Quoted Market Prices (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	2012 Total Fair Value
Assets				
Cash and cash equivalents	$ -	$ 26,040	$ -	$ 26,040
Collateral held for securities lending	-	-	-	-
Operating and long term investments:				
Cash and cash equivalents	143,988	67,980	-	211,968
Debt securities				
Asset backed securities	-	35,543	-	35,543
Bank loans	-	175	-	175
Bond funds	72,678	1,642	2,013	76,333
Corporate bonds	-	49,498	35	49,533
Government bonds & securities	-	63,475	-	63,475
Mortgage backed bonds	-	7,448	-	7,448
Other	5,591	5,464	-	11,055
Common, mutual fund & preferred stock				
Common stock	237,280	-	200	237,480
Equity exchange traded funds	129	-	-	129
Mutual funds (domestic)	14,546	29,821	-	44,367
Mutual funds (global)	4,965	-	-	4,965
Mutual funds (international)	56,888	181,384	-	238,272
Preferred stock	683	-	-	683
Real assets	323	-	291,513	291,836
Private equity	-	-	362,398	362,398
Hedge funds	-	68,168	285,318	353,486
Other	14,317	4,351	24,156	42,824
Total operating and long term investments	551,388	514,949	965,633	2,031,970
Interest in net assets of foundation	-	-	12,330	12,330
Trusts held by others	-	-	46,877	46,877
Total assets at fair value	$ 551,388	$ 540,989	$ 1,024,840	$ 2,117,217
Liabilities				
Interest rate swap payable	$ -	$ 37,755	$ -	$ 37,755
Total liabilities at fair value	$ -	$ 37,755	$ -	$ 37,755

(dollars in thousands)

	Quoted Market Prices (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	2011 Total Fair Value
Assets				
Cash and cash equivalents	$ -	$ 16,465	$ -	$ 16,465
Collateral held for securities lending	-	69,282	-	69,282
Operating and long term investments:				
Cash and cash equivalents	71,911	72,446	-	144,357
Debt securities				
Asset backed securities	-	19,347	-	19,347
Bank loans	-	692	-	692
Bond funds	68,576	-	1,608	70,184
Corporate bonds	-	71,526	107	71,633
Government bonds & securities	-	47,636	-	47,636
Non-government backed securities	-	633	-	633
Mortgage backed bonds	-	7,434	-	7,434
Other	7,633	23,188	-	30,821
Common, mutual fund & preferred stock				
Common stock	226,346	609	-	226,955
Equity exchange traded funds	135	-	-	135
Mutual funds (domestic)	17,593	21,843	-	39,436
Mutual funds (global)	5,312	-	-	5,312
Mutual funds (international)	49,147	190,019	-	239,166
Preferred stock	319	-	-	319
Real assets	323	-	262,627	262,950
Private equity	-	-	400,557	400,557
Hedge funds	-	99,001	294,549	393,550
Other	6,317	7,650	17,665	31,632
Total operating and long term investments	453,612	562,024	977,113	1,992,749
Interest in net assets of foundation	-	-	13,743	13,743
Trusts held by others	-	-	49,780	49,780
Total assets at fair value	$ 453,612	$ 647,771	$ 1,040,636	$ 2,142,019
Liabilities				
Interest rate swap payable	$ -	$ 24,984	$ -	$ 24,984
Total liabilities at fair value	$ -	$ 24,984	$ -	$ 24,984

The valuation methodologies for assets and liabilities measured at fair value described below may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. The University believes its valuation methods are appropriate and consistent with other market participants. However, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Fair value for Level 1 is based upon quoted market prices in active markets. Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources including market participants, dealers, and brokers. Level 3 consists primarily of the University's alternative investments (primarily limited partnership interests in absolute return, hedge funds, private equity, real estate, and natural resource funds) and represents the ownership interest in the net asset value (NAV) of the respective partnerships. Investments held by the partnerships consist of marketable securities as well as securities that do not have readily determined fair values. The fair values of the securities held by limited partnerships that do not have readily observable fair values are determined by the general partner and are based on historical cost, appraisals, and/or other estimates that require varying degrees of judgment. If no public market exists for the investment securities, the fair value is determined by the general partner taking into consideration the costs of the securities, prices of recent significant placements of securities of the same issuer, and subsequent developments concerning the companies to which the securities relate.

Interest in net assets of foundation are considered Level 3 assets as they represent the University's share of net assets as reported by the foundation.

Investments in perpetual trusts held by others are valued at the fair value of the assets contributed to the trusts and are considered Level 3 assets.

Interest rate swaps are valued using both observable and unobservable inputs, such as quotations received from the counterparty, dealers or brokers, whenever available and considered reliable. In instances where models are used, the value of the interest rate swap depends upon the contractual terms of, and specific risks inherent in, the instrument as well as the availability and reliability of observable inputs. Such inputs include market prices for reference securities, yield curves, credit curves, measures of volatility, prepayment rates, assumptions for nonperformance risk, and correlations of such inputs. The University's interest rate swap arrangements have inputs which can generally be corroborated by market data and are therefore classified within level 2.

Fair value of interest rate swaps in the consolidated balance sheets:

	Notional Amount	2012 Level 2 Fair Value	2011 Level 2 Fair Value
Accounts payable	$ 217,935	$ 37,755	$ 24,984

Effect of interest swaps on statements of activities:

	2012 Unrealized Gain/(Loss)	2011 Unrealized Gain/(Loss)
Non-operating net appreciation / (depreciation)	$ (12,772)	$ 3,355

Activity related to interest rate swaps affect unrestricted net assets and, in the consolidated statement of cash flows, are included in changes in accounts payable and accrued expenses in the operating activities section.

(dollars in thousands)

The following tables are rollforwards of the consolidated balance sheet amounts for financial instruments classified by the University within Level 3 of the fair value hierarchy defined above.

	Balance June 30, 2011	Realized Gains/(Losses)	Unrealized Gains/(Losses)	Purchases	Sales	Settlements	Transfers In/(Out) of Level 3	Balance June 30, 2012
Investments:								
Debt securities	$ 1,715	$ 2	$ 378	$ 60	$ (107)	$ -	$ -	$ 2,048
Common, mutual fund & preferred stock	-	-	-	200	-	-		200
Private equity	400,557	(363)	(24,576)	37,080	-	(50,300)	-	362,398
Hedge funds	294,549	5,482	(1,470)	15,763	(23,573)	(5,433)	-	285,318
Real assets and other	280,292	(5)	(9,943)	67,464	-	(22,139)	-	315,669
Interest in net assets of foundation	13,743	31	(213)	2,310	(3,541)	-	-	12,330
Investments in perpetual trusts held by others	49,780	503	(3,502)	637	(541)	-	-	46,877
Total fair value	$ 1,040,636	$ 5,650	$ (39,326)	$ 123,514	$ (27,762)	$ (77,872)	$ -	$ 1,024,840

	Balance June 30, 2010	Realized Gains/(Losses)	Unrealized Gains/(Losses)	Purchases	Sales	Settlements	Transfers In/(Out) of Level 3	Balance June 30, 2011
Investments:								
Debt securities	$ 1,745	$ 12	$ (9)	$ 208	$ (241)	$ -	$ -	$ 1,715
Common, mutual fund & preferred stock	-	-	-	-	-	-	-	-
Private equity	337,226	(4,882)	35,596	65,977	(621)	(32,739)	-	400,557
Hedge funds	270,736	(2,031)	25,736	109,027	(136,540)	27,621	-	294,549
Real assets and other	219,215	(9,941)	34,860	59,394	(2,993)	(20,246)	3	280,292
Interest in net assets of foundation	12,370	(566)	2,413	1,710	(897)	-	(1,287)	13,743
Investments in perpetual trusts held by others	43,119	(2,011)	8,577	952	(857)	-	-	49,780
Total fair value	$ 884,411	$ (19,419)	$ 107,173	$ 237,268	$ (142,149)	$ (25,364)	$ (1,284)	$ 1,040,636

All net realized and unrealized gains/(losses) in the table above are reflected in net appreciation/(depreciation) of long-term investment activities in the accompanying statement of activities. Net unrealized gains/(losses) relate to those financial instruments held by the University at June 30, 2012.

The University is permitted under US GAAP to estimate the fair value of an investment at the measurement date using the reported NAV without further adjustment unless the entity expects to sell the investment at a value other than NAV or if the NAV is not calculated in accordance with US GAAP. The University's investments in private equity, real estate, and certain hedge funds in the absolute return portfolio are recorded at fair value based on the most current NAV.

The University performs additional procedures including due diligence reviews on its investments in investment companies and other procedures with respect to the capital account, or NAV provided, to ensure conformity with US GAAP. The University has assessed factors including, but not limited to, managers' compliance with the Fair Value Measurement standard, price transparency and valuation procedures in place, the ability to redeem at NAV at the measurement date, and existence of certain redemption restrictions at the measurement date.

The guidance also requires additional disclosures to enable users of the financial statements to understand the nature and risk of the University's investments. Furthermore, investments which can be redeemed at NAV by the University on the measurement date or within 90 days are classified as Level 2. Investments which cannot be redeemed on the measurement date or within 90 days are classified as Level 3.

(dollars in thousands)

Strategy	2012 Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice
Hedge funds:				
Long/short	$ 170,004	$ -	Quarterly, annually, 1 & 3 year rolling lock-ups	45 - 90 days
Multi-strategy	153,511	-	Quarterly, annually, 1 & 2 year rolling lock-ups	45 - 90 days
Private equity:			**Remaining Fund Life**	**Drawdown Period**
Buyouts	239,729	60,831	1 to 10 years	1 to 7 years
Venture capital	83,484	19,762	1 to 12 years	1 to 6 years
Distressed	33,182	9,667	1 to 5 years	1 to 3 years
Real assets:				
Real estate	185,899	50,791	1 to 10 years	1 to 5 years
Natural resources	105,614	56,018	1 to 12 years	1 to 5 years
Total alternative partnerships	971,423	197,069		
Other Alternative Investments:				
Comingled funds of public equities	223,021	-	Monthly	15 - 60 days
Comingled funds of fixed income	6,003	-	NA – held to maturity	NA
Total other alternative investments	229,024	-		
Total alternative investments	$ 1,200,447	$ 197,069		

Strategy	2011 Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice
Hedge funds:				
Long/short	$ 165,726	$ -	Quarterly, annually, 1 & 3 year rolling lock-ups	45 - 90 days
Multi-strategy	196,611	-	Quarterly, annually, 1 & 2 year rolling lock-ups	45 - 90 days
Private equity:			**Remaining Fund Life**	**Drawdown Period**
Buyouts	257,035	65,527	1 to 10 years	1 to 7 years
Venture capital	78,465	24,460	1 to 12 years	1 to 6 years
Distressed	38,052	7,426	1 to 5 years	1 to 3 years
Real assets:				
Real estate	148,598	88,115	1 to 10 years	1 to 5 years
Natural resources	106,150	56,419	1 to 12 years	1 to 5 years
Total alternative partnerships	990,637	241,947		
Other Alternative Investments:				
Comingled funds of public equities	220,319	-	Monthly	15 - 60 days
Comingled funds of fixed income	10,528	-	NA – held to maturity	NA
Total other alternative investments	230,847	-		
Total alternative investments	$ 1,221,484	$ 241,947		

(dollars in thousands)

(13) Lines of Credit

The University has a $50,000 committed line of credit agreement with Northern Trust Company that is subject to credit review and renewal. Under this agreement, no amounts were outstanding at June 30, 2012 and 2011, respectively.

The University has a $75,000 committed line of credit agreement with JPMorgan Chase Bank, N.A. that is subject to credit review and renewal. Under this agreement, no amounts were outstanding at June 30, 2012 and 2011, respectively.

The University has a $50,000 committed line of credit agreement with U.S. Bank, N.A. that is subject to credit review and renewal. Of this total, $950 and $1,000 were outstanding at June 30, 2012 and 2011, respectively.

The University has $788 in standby letters of credit with JPMorgan Chase Bank, N.A. to cover potential liabilities of other financial obligations.

(14) Commitments and Contingencies

In the ordinary course of operations, the University is named as a defendant in various lawsuits, or events occur which could lead to litigation, claims, or assessments. Although the outcome of such matters cannot be predicted with certainty, management believes that insurance coverage is sufficient to cover current or potential claims, or that the final outcomes of such matters will not have a material adverse effect on the consolidated financial position.

At June 30, 2012, the University has entered into construction contracts and commitments aggregating $687,474 ($603,405 at June 30, 2011) of which $573,178 ($484,210 at June 30, 2011) had been fulfilled.

(15) Leases

The University leases research laboratories, office space, and equipment under operating leases expiring through August 2023. Rental expense for the years ended June 30, 2012 and 2011 totaling $32,583 and $33,799, respectively, is included in the accompanying consolidated statements of activities.

Future minimum payments by year and in the aggregate, under non-cancelable operating leases, with initial or remaining terms of one year or more are as follows:

	University	Related Entities
2013	$ 27,919	$ 3,052
2014	23,066	2,718
2015	17,455	2,601
2016	14,928	2,603
2017	10,160	2,380
Thereafter	34,106	4,302
Total minimum lease payments	$ 127,634	$ 17,656

(16) Scholarships, Grants, and Fellowships

The University awarded a total of $151,430 and $142,321 in scholarships, grants and fellowships during fiscal years 2012 and 2011, respectively. In addition, the University awarded $22,407 and $21,317, respectively, of scholarships, grants and fellowships as compensation to the recipients. Of this amount, $19,783 and $20,514, respectively, of the total scholarships, grants and fellowships awarded were specifically funded by federal, state or private gifts or grants, or by investment income and gains earned on investments held for endowment and similar purposes and utilized under the University's total return spending policy.

(dollars in thousands)

(17) Uncompensated Care

The University's policy is to treat patients in need of medical services without regard to their ability to pay for such services. The University maintains records to identify and monitor the level of uncompensated care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy. In addition to charity care, the University also provides services at rates significantly below the cost of rendering those services. The estimated difference between the cost of services provided to Medicaid patients and the reimbursement from NYS for this patient care is also monitored.

Effective January 1, 2007, the New York State Public Health Law required all hospitals to implement financial aid policies and procedures. The law also required hospitals to develop a summary of its financial aid policies and procedures that must be made publicly available. All standards set forth in the law are minimum standards.

In order to qualify for charity care, patients are expected to submit financial information demonstrating need. In many cases, patients may be unable or unwilling to provide that data. In those cases, the uncompensated care is classified as bad debt expense unless the University is able to obtain information that would indicate the patient appears to be eligible for charity care assistance. In those cases the uncompensated care is recorded as charity care.

The estimated costs of providing charity services is based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The University received funding from NYS to help defray some of the costs of indigent care in the amount of $8,160 and $7,476 in 2012 and 2011, respectively.

During the years ended June 30, 2012 and 2011, the following levels of uncompensated care were provided:

	2012	2011
Charity care at cost	$ 19,172	$ 12,253
Excess of cost over reimbursement for services provided to Medicaid patients	39,112	36,969
Bad debts expense	7,698	19,868
	$ 46,810	$ 56,837

(18) Functional Expenses

The University also records expenses according to major classes of programs or functions. Functional expenses for the years ended June 30 consisted of the following:

	2012	2011
Instruction	$ 313,698	$ 300,191
Research	315,548	334,396
Public service	8,337	10,235
Libraries and other academic support	59,377	60,165
Student services	50,325	45,212
Institutional support	97,600	89,749
Hospital and faculty practice patient care	1,795,828	1,721,125
Auxiliary enterprises	91,216	90,164
Total functional expenses	$ 2,731,929	$ 2,651,237

(19) Subsequent Events

(a) DASNY Series 2006 Letter of Credit Replacement

Pursuant to an agreement between the University and DASNY dated August 14, 2012, DASNY remarketed $111,180 of bonds known as the University of Rochester Revenue Bonds, Series 2006, consisting of $94,130 Series 2006A-1 bonds and $17,050 Series 2006B-1 bonds. These bonds were remarketed as the existing direct-pay letter of creditor (Bank of America, N.A.) was replaced with Wells Fargo Bank, N.A. This letter of credit expires in August 2015, with an option to renew. The terms related to the repayment of principal on these bonds remains unchanged.

Additionally, the letter of credit available totals the outstanding debt service for the Series 2006 bonds.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

(b) Alignment Agreement

The University entered into an Alignment Agreement with F.F. Thompson Health System, Inc. (THS), The Frederick Ferris Thompson Hospital (FFTH), M.M. Ewing Continuing Care Center (CCC), F.F.T Senior Communities, Inc. (FFTSC), FFTH Properties and Services, Inc. (FFTH Properties), and The F.F. Thompson Foundation, Inc. (FFTF). The closing of the agreement occurred on August 31, 2012, when the University became the sole member of F.F. Thompson Health System, Inc. THS remains the sole member of FFTH, CCC, FFTSC, and FFTF and the sole shareholder of FFTH Properties. The University, THS and THS's affiliates continue as separate and distinct corporations. THS and THS's affiliates will be included in the 2013 consolidated financial statements of the University.

The University has performed an evaluation of subsequent events through October 16, 2012, the date on which the consolidated financial statements were issued.