



LEHIGH UNIVERSITY

Consolidated Financial Statements and
Information on Federal Awards

June 30, 2016

(With Independent Auditors' Reports Thereon)

LEHIGH UNIVERSITY

Table of Contents

	Page
Independent Auditors' Report	1
Consolidated Statement of Financial Position, June 30, 2016 (with comparative financial information for the year ended June 30, 2015)	3
Consolidated Statement of Activities, Year ended June 30, 2016 (with comparative financial information for the year ended June 30, 2015)	4
Consolidated Statement of Cash Flows, Year ended June 30, 2016 (with comparative financial information for the year ended June 30, 2015)	5
Notes to Consolidated Financial Statements	6
Schedule of Expenditures of Federal Awards, Year ended June 30, 2016	33
Notes to Schedule of Expenditures of Federal Awards	37
Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	39
Independent Auditors' Report on Compliance for the Major Federal Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance	41
Schedule of Findings and Questioned Costs, Year ended June 30, 2016	43



KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

The Board of Trustees
Lehigh University:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Lehigh University (the University), which comprise the consolidated statement of financial position as of June 30, 2016, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Lehigh University as of June 30, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.



Report on Summarized Comparative Information

We have previously audited Lehigh University's 2015 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated October 20, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2015 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 24, 2016 on our consideration of Lehigh University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Lehigh University's internal control over financial reporting and compliance.

KPMG LLP

Philadelphia, Pennsylvania

October 24, 2016

LEHIGH UNIVERSITY

Consolidated Statement of Financial Position

June 30, 2016

(with comparative financial information for June 30, 2015)

(In thousands)

Assets	2016	2015
Cash and cash equivalents (note 1(c))	\$ 24,930	28,626
Accounts receivable, net (note 5)	12,946	15,961
Inventories	1,590	1,752
Prepaid expenses and other assets	5,584	4,438
Contributions receivable, net (note 8)	37,030	56,688
Notes receivable, net (note 6)	12,767	13,140
Investments (notes 2 and 4)	1,554,579	1,662,156
Funds held in trust by others	4,332	4,615
Land, buildings, and equipment, net (note 7)	<u>401,190</u>	<u>391,763</u>
Total assets	<u><u>\$ 2,054,948</u></u>	<u><u>2,179,139</u></u>
Liabilities and Net Assets		
Accounts payable and accrued expenses	\$ 37,888	42,399
Deferred revenues	23,837	22,550
Annuity payment liability	19,443	18,786
Other liabilities (notes 10, 11, and 13)	55,982	47,838
Deposits held for others	1,385	1,348
Refundable federal student loan funds	2,194	2,289
Bonds, loans, and notes payable (note 10)	<u>240,025</u>	<u>280,887</u>
Total liabilities	<u><u>380,754</u></u>	<u><u>416,097</u></u>
Net assets (notes 3 and 9):		
Unrestricted	839,051	881,797
Temporarily restricted	309,160	374,325
Permanently restricted	<u>525,983</u>	<u>506,920</u>
Total net assets	<u><u>1,674,194</u></u>	<u><u>1,763,042</u></u>
Total liabilities and net assets	<u><u>\$ 2,054,948</u></u>	<u><u>2,179,139</u></u>

See accompanying notes to consolidated financial statements.

LEHIGH UNIVERSITY

Consolidated Statement of Activities

Year ended June 30, 2016

(with summarized comparative financial information for year ended June 30, 2015)

(In thousands)

		2016				
		Unrestricted	Temporarily restricted	Permanently restricted	Total	2015
Support and revenues:						
Tuition and fees, net (note 1(i))	\$ 185,644	—	—	—	185,644	180,099
Federal grants and contracts	23,597	—	—	—	23,597	27,085
State and local grants and contracts	6,314	—	—	—	6,314	7,255
Private grants and contracts	5,807	—	—	—	5,807	6,026
Contributions	15,090	—	—	—	15,090	12,141
Investment return (note 2)	82,527	—	—	—	82,527	77,949
Auxiliary enterprises	43,492	—	—	—	43,492	42,063
Independent operations (note 1(a))	11,123	—	—	—	11,123	10,087
Other sources	9,543	—	—	—	9,543	10,145
Gifts and trusts released from restrictions	3,164	(3,164)	—	—	—	—
Total support and revenues	<u>386,301</u>	<u>(3,164)</u>	<u>—</u>	<u>—</u>	<u>383,137</u>	<u>372,850</u>
Expenses:						
Instruction	144,281	—	—	—	144,281	141,789
Research	39,285	—	—	—	39,285	40,459
Public service	3,258	—	—	—	3,258	3,244
Academic support	32,460	—	—	—	32,460	32,416
Student services	36,216	—	—	—	36,216	36,320
Institutional support (note 16)	69,522	—	—	—	69,522	67,264
Auxiliary enterprises	37,757	—	—	—	37,757	36,039
Independent operations (note 1(a))	11,240	—	—	—	11,240	10,195
Total expenses (note 12)	<u>374,019</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>374,019</u>	<u>367,726</u>
Operating income (loss)	<u>12,282</u>	<u>(3,164)</u>	<u>—</u>	<u>—</u>	<u>9,118</u>	<u>5,124</u>
Nonoperating activity:						
Investment return (note 2):						
University	(68,149)	(48,245)	(370)	(116,764)	(31,678)	
Independent operations	387	—	—	387	(1,095)	
Gifts and trusts	3,244	3,107	15,180	21,531	20,215	
Gifts and trusts released from restrictions and changes in donor intent	16,899	(17,101)	202	—	—	
Change in fair value of interest rate swaps (note 11)	(3,189)	—	—	(3,189)	984	
Postretirement plan changes other than net periodic benefit costs (note 13):						
University	(2,559)	—	—	(2,559)	4,383	
Independent operations	(63)	—	—	(63)	129	
Other	<u>(1,598)</u>	<u>238</u>	<u>4,051</u>	<u>2,691</u>	<u>(2,081)</u>	
Nonoperating income (loss)	<u>(55,028)</u>	<u>(62,001)</u>	<u>19,063</u>	<u>(97,966)</u>	<u>(9,143)</u>	
Change in net assets	<u>(42,746)</u>	<u>(65,165)</u>	<u>19,063</u>	<u>(88,848)</u>	<u>(4,019)</u>	
Net assets, beginning of year	<u>881,797</u>	<u>374,325</u>	<u>506,920</u>	<u>1,763,042</u>	<u>1,767,061</u>	
Net assets, end of year	<u>\$ 839,051</u>	<u>309,160</u>	<u>525,983</u>	<u>1,674,194</u>	<u>1,763,042</u>	

See accompanying notes to consolidated financial statements.

LEHIGH UNIVERSITY

Consolidated Statement of Cash Flows

Year ended June 30, 2016

(with comparative financial information for year ended June 30, 2015)

(In thousands)

	2016	2015
Cash flows from operating activities:		
Change in net assets	\$ (88,848)	(4,019)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Gifts and trusts restricted for long-term investment	(17,393)	(26,483)
Noncash contributions	(2,132)	(1,914)
Investment earnings restricted for long-term investments	281	(343)
Net realized gains on investments	(24,912)	(86,355)
Net unrealized losses on investments	69,008	58,816
Change in fair value of rate swap liabilities	2,786	(791)
Payment of annuity obligations	1,336	1,341
Other nonoperating activity	417	476
Depreciation and amortization	27,903	26,455
Independent operations provision for bad debts	1,841	1,020
University provision for bad debts	381	92
Change in operating assets and liabilities:		
Decrease (increase) in accounts receivable	2,420	(89)
Decrease in inventories	162	45
Decrease in contributions receivable	19,658	13,462
(Decrease) increase in accounts payable and accrued expenses	(4,511)	2,357
Increase (decrease) in deferred revenues	1,287	(2,660)
Increase (decrease) in annuity payment liability	657	(167)
Increase (decrease) in deposits held for others	37	(13)
Increase (decrease) in accrued postretirement benefit costs	4,867	(1,926)
(Increase) decrease in other assets	(1,146)	1,338
(Decrease) increase in other liabilities	(53)	142
Net cash used in operating activities	<u>(5,954)</u>	<u>(19,216)</u>
Cash flows from investing activities:		
Proceeds from sale of investments	1,734,705	1,526,565
Purchases of investments	(1,670,942)	(1,520,371)
Student loans and other notes advanced	(1,272)	(1,304)
Independent operations loans advanced	(1,607)	(2,032)
Student loans and other notes collected	1,339	1,299
Independent operations loans collected	270	972
Purchase of land, buildings, and equipment	(34,895)	(51,797)
Net cash provided by (used in) investing activities	<u>27,598</u>	<u>(46,668)</u>
Cash flows from financing activities:		
Proceeds from issuance of indebtedness	—	25,000
Repayments of principal of indebtedness	(41,021)	(5,801)
Gifts and trusts restricted for long-term investment	17,393	26,483
Investment earnings restricted for long-term investments	(281)	343
Decrease in refundable loan funds	(95)	(101)
Payment of annuity obligations	(1,336)	(1,341)
Net cash (used in) provided by financing activities	<u>(25,340)</u>	<u>44,583</u>
Net decrease in cash and cash equivalents	<u>(3,696)</u>	<u>(21,301)</u>
Cash and cash equivalents at beginning of year	<u>28,626</u>	<u>49,927</u>
Cash and cash equivalents at end of year	<u>\$ 24,930</u>	<u>28,626</u>
Supplemental data:		
Interest paid	\$ 9,829	10,053

See accompanying notes to consolidated financial statements.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(1) Summary of Significant Accounting Policies

(a) Organization

Lehigh University (the University), an independent, nondenominational, coeducational university, is incorporated in the Commonwealth of Pennsylvania as a nonprofit corporation and is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended. The University is accredited by the Middle States Association of Colleges and Schools.

Founded in 1865, the University has approximately 5,100 undergraduates within its three major units – the College of Arts and Sciences, the College of Business and Economics, and the P.C. Rossin College of Engineering and Applied Science – and approximately 2,000 students enrolled in graduate programs offered through these colleges and in the College of Education.

The University's subsidiary organization, LU Properties, LLC (LU Properties), a Pennsylvania limited liability company, serves as Manager for twenty-three limited liability companies that were established as a result of a real estate gift. The University is the sole member of all of the limited liability companies. As Manager, LU Properties is responsible for the strategic and operational aspects of the real estate investment. The results of their operations are shown as nonoperating investment return in the University's consolidated statement of activities.

The University is also the sole member of So-Beth Funding LLC (So-Beth Funding). So-Beth Funding was formed to improve the condition of residential properties and quality of property management in the South Bethlehem community in order to create a more attractive and safe neighborhood for University students and the greater community. The results of So-Beth Funding's operations appear as institutional support in the University's consolidated statement of activities.

In 2016 the University established South River Investments LLC (South River), a Pennsylvania limited liability company, to own and develop certain real estate properties in the local community. The results of South River's operations appear as public service in the University's consolidated statement of activities.

The Ben Franklin Technology Partners of Northeastern PA (BFTP), Manufacturers Resource Center (MRC), and Lehigh and Northampton Counties Revolving Loan Fund (RLF) are also wholly owned subsidiaries of the University. The results of their operations are shown as independent operations in the University's consolidated statement of activities.

BFTP is an entity that encourages public and private sector cooperation in stimulating economic growth. BFTP provides funds to its clients under the terms of its early stage and established manufacturer loan programs. Considering the nature of the loans and collection history, BFTP has recorded an estimated allowance for doubtful collections.

MRC provides resources to help small and medium-sized regional manufacturing companies enhance their ability to compete successfully by providing consulting, education, and strategic partnering services. RLF's principal activity is to provide capital (in the form of loans) to new and existing businesses for the purpose of creating and retaining permanent private-sector jobs.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

The majority of the independent operations revenue reported in the University's consolidated statement of activities relates to BFTP and MRC revenue received in the form of federal and state grants and client fees for services.

The assets and liabilities of all subsidiary organizations appear in the appropriate line items of the consolidated statement of financial position.

(b) Basis of Presentation

The accompanying consolidated financial statements of the University include all subsidiary organizations and have been prepared on the accrual basis of accounting and in conformity with U.S. generally accepted accounting principles (GAAP). All significant inter-organizational balances and transactions have been eliminated.

The University's consolidated financial statements are presented in accordance with the external financial reporting requirements for not-for-profit organizations, which include three basic financial statements and the classification of resources into three separate classes of net assets, as follows:

Unrestricted – Net assets that are free of donor-imposed restrictions; all revenues, expenses, gains, and losses that are not changes in permanently or temporarily restricted net assets. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees or management.

Temporarily Restricted – Net assets whose use by the University is limited by donor-imposed stipulations that either expire by passage of time or that can be fulfilled or removed by actions of the University pursuant to those stipulations.

Permanently Restricted – Net assets whose use by the University is limited by donor-imposed stipulations that neither expire with the passage of time nor can be fulfilled or otherwise removed by actions of the University. Generally, the donors of these assets permit the University to use all or part of the investment income on related investments for general or specific purposes. Such assets primarily include the University's permanent endowment fund.

Nonoperating activities reflect transactions of a long-term investment or capital nature, including contributions restricted for acquisitions of facilities and equipment, contributions restricted with donor-imposed stipulations, gains and losses on investments net of the University's spending policy, and certain postretirement benefits-related changes in net assets.

(c) Cash Equivalents

All highly liquid investments with an original maturity of three months or less, except those held for long-term investment purposes, are considered to be cash equivalents.

(d) Inventories

Inventories are stated at the lower of cost or net realizable value.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(e) Investments

Investments are stated at fair value or net asset value (NAV) as a practical expedient to fair value (see note 4).

Unrealized gains and losses on investments are included in nonoperating investment return in the consolidated statement of activities.

The University's investments are exposed to various risks such as interest rate, market, and credit risks. Such risks, and the resulting investment security values, may be influenced by changes in economic conditions and market perceptions and expectations. Accordingly, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the consolidated statement of financial position.

(f) Contributions

Contributions received, including unconditional promises to give, are recognized as revenues when the donor's commitment is received. Unconditional promises to give are recognized at the estimated present value of the future cash flows, net of allowances. Allowances for uncollectible amounts are recorded based on management's estimate of realizability of the underlying pledges.

Contributions made towards long-lived assets are held as temporarily restricted until the asset is completed and available for use. At such time, the contribution is considered to be released from restriction and reclassified to unrestricted net assets. Contributions that are released from restriction within the year received are classified as unrestricted gifts. Gifts of noncash assets are recorded at their fair value. Conditional promises are recorded when donor stipulations are substantially met.

(g) Split-Interest Agreements and Annuities Payable

The University's split-interest agreements with donors consist primarily of annuity, life income, and charitable trusts for which the University serves as trustee. A majority of the assets held in these trusts are included in investments. Contribution revenues are recognized at the date the trusts are established after recording liabilities for the present value of the estimated future payments to be made to the donors and/or other beneficiaries. The liabilities are adjusted during the term of the trusts for changes in the value of the assets and changes in the estimated present value of future cash outflows and other changes in the estimates of future benefits. The annuities payable represent the net present value of future cash outflows over the annuitant's life expectancy, as required by the annuity agreements. The net present value is calculated using a discount rate range of 1.57% to 7.5%. The University is required by the laws of certain states to register and maintain reserves against charitable gift annuities. Such reserves amounted to approximately \$11.8 million and \$11.4 million as of June 30, 2016 and 2015, respectively, and are reported within investments in the consolidated statement of financial position.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(h) Land, Buildings, and Equipment

Land, buildings, and equipment are carried at cost or at the fair market value at the date of the gift, less accumulated depreciation. Depreciation is computed on a straight-line basis over the estimated useful lives of the related asset. Depreciation is not recorded on land. Such assets and lives generally are as follows:

Buildings	50 to 60 years
Equipment	5 to 10 years
Leasehold and other improvements	10 to 20 years

(i) Tuition and Fees

Tuition and fees are reported net of financial aid that effectively reduces the amount of tuition and fees collected from students. Financial aid amounts offset against gross tuition and fees for 2016 and 2015 were \$86.6 million and \$82.5 million, respectively.

(j) Asset Retirement Liabilities

The University recognizes a liability for legal obligations associated with asset retirements in the period in which the obligation is incurred if a reasonable estimate of the fair value of the obligation can be made. When the liability is initially recorded, the University capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. The liability is accreted to its present value each period, and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the asset. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the consolidated statement of activities.

(k) Deferred Revenues

Revenues received in exchange transactions for specific activities that have not yet taken place are recorded as deferred revenue. Significant components of deferred revenue include student tuition and educational fees received in advance of services to be rendered and unexpended advances of grant and contract revenues.

(l) Use of Estimates

The preparation of the University's consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated statement of financial position and the reported amounts of revenue and expense included in the consolidated statement of activities. Actual results could differ from such estimates. Significant estimates include alternative investments that are measured at NAV per share as a practical expedient for fair value, the postretirement benefit liability, and allocation of functional expenses.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(m) Reclassifications

Certain 2015 amounts have been reclassified to conform to their presentation in the 2016 consolidated financial statements.

(n) Recent Accounting Pronouncements

In June 2015, the Financial Accounting Standards Board issued ASU No. 2015-10, *Technical Corrections and Improvements*, that addresses a variety of matters, including the amendment of the master glossary term, *readily determinable fair value*. Paragraph 30 of the ASU states that the fair value of an equity security that is an investment in a mutual fund or in a structure similar to a mutual fund (that is, a limited partnership or a venture capital entity) is readily determinable if the fair value per share (unit) is determined and published and is the basis for current transactions.

Paragraph 30 of the ASU became effective upon issuance. This guidance has resulted in the correction and reclassification of certain investments held by the University from investment funds measured at NAV (or its equivalent) to Level 2 of the fair value hierarchy. This guidance has been applied retrospectively and is reflected in the fair value hierarchy as of June 30, 2016 and 2015.

(o) Prior Year Summarized Financial Information

The consolidated financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the University's consolidated financial statements for the year ended June 30, 2015, from which the summarized information was derived.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

(2) Investments

Investments by major category at June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Short-term investments	\$ 69,021	6,100
Fixed income investments:		
U.S. government	146,084	161,952
Corporate	90,590	116,678
Other	3,300	6,905
Corporate stocks	22,192	19,863
Mutual and exchange-traded funds	191,661	239,284
Real estate	17,626	19,926
Alternative investments:		
Global equity	359,174	405,279
Hedged equity	59,585	65,323
Absolute return	252,878	273,305
Natural resources equity	23,542	28,650
Developed market credit	15,681	16,036
Private investments	300,089	299,720
Life insurance and other investments	3,156	3,135
Total investments	\$ 1,554,579	1,662,156

The University's investments are comprised of the assets of the University's endowment, assets supporting certain split interest agreements, and other investments for general operating purposes. Investments are reported at fair value or NAV as a practical expedient to fair value. Note 4, Fair Value Measurements, provides additional information about inputs used to determine fair value and about investments reported at NAV.

The majority of endowment and annuity fund investments are combined in investment pools with each individual account subscribing to or disposing of shares on the basis of the fair value per share. The investment objective is to maximize long-term total return through a combination of income and capital appreciation in a manner consistent with sound investment practices.

The University is obligated under certain investment agreements to periodically advance additional funding up to contractual levels. At June 30, 2016 and 2015, the University had unfunded commitments of \$156 million and \$155 million, respectively. While it is uncertain as to when these commitments will be called since the agreements do not specify exact funding dates, it is likely that funding will occur over the next several years. Funds to meet these commitments will be generated from rebalancing the investment pool asset allocation, as well as donor gifts and existing cash.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

The components of total investment return are reflected below (in thousands). Investment earnings at June 30, 2016 and 2015 are net of investment expenses of approximately \$10.2 million and \$9.1 million, respectively.

	2016	2015
Investment earnings	\$ 10,421	18,077
Net realized and unrealized (losses) gains	<u>(44,658)</u>	<u>28,194</u>
	(34,237)	46,271
Independent operations – net realized and unrealized gains (losses)	562	(655)
Independent operations – other investment earnings	<u>344</u>	<u>816</u>
Total	<u>\$ (33,331)</u>	<u>46,432</u>

Investment return, as reflected in the consolidated statement of activities, consists of the following components (in thousands):

	2016	2015
Operating:		
Endowment spending distribution	\$ 65,457	61,574
Spending distribution – other	9,821	9,916
Other investment earnings	<u>7,249</u>	<u>6,459</u>
	82,527	77,949
Independent operations – realized gains	175	440
Independent operations – other investment earnings	<u>344</u>	<u>816</u>
Total operating	<u>83,046</u>	<u>79,205</u>
Nonoperating:		
Endowment spending distribution	167	326
Other investment (losses) gains	(447)	17
Net realized and unrealized losses net of spending distribution	<u>(116,484)</u>	<u>(32,021)</u>
	(116,764)	(31,678)
Independent operations – net unrealized gains (losses)	387	(1,095)
Total nonoperating	<u>(116,377)</u>	<u>(32,773)</u>
Total investment return	<u>\$ (33,331)</u>	<u>46,432</u>

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(3) Endowment Net Assets

The University's endowment consists of approximately 2,700 individual funds established for a variety of purposes. Its endowment includes both donor-restricted funds and funds designated by the Board of Trustees to function as endowments (board-designated). Net assets associated with endowment funds are classified and reported based upon the existence or absence of donor-imposed restrictions.

The University has interpreted relevant law as requiring the preservation of the original fair value of permanently restricted endowment funds as of the gift date, absent explicit donor stipulations to the contrary. From time to time, the fair value of assets associated with these funds may fall below the original fair value amount. Deficiencies of this nature at June 30, 2016 and 2015 were \$27.1 million and \$10.5 million, respectively. Such deficiencies are recorded as a decrease to unrestricted net assets and an increase to temporarily restricted net assets. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of the new permanently restricted contributions.

Endowment funds include funds actively managed by the University as part of a single commingled investment pool as well as a limited number of individual funds that are separately invested or held in trust by others. The principal financial objective of the endowment pool is that the real purchasing power of the endowment principal should be preserved and, if possible, enhanced, to help ensure the University's financial future. The productivity of the endowment pool must strike a balance between the preservation of principal in real terms for perpetuity and supporting a spending policy that sustains the educational mission of the University.

The Prudent Investor Rule of the Commonwealth of Pennsylvania views investment prudence on the part of the fiduciary from the standpoint of the total portfolio. Therefore, any reasonable investment may be considered for endowment pool assets as long as the risk and return tradeoff of the entire portfolio is prudent. The University's investment policy includes a target asset allocation, well diversified among suitable asset classes that is expected to generate, on average, the level of expected return necessary to meet endowment objectives at a responsible level of volatility consistent with achieving that return. To monitor the effectiveness of the investment strategy of the endowment pool, performance goals are established to exceed the expected real rate of return, established benchmark indices, and the median return of comparable endowment funds.

Commonwealth of Pennsylvania law permits the University to allocate to operating income a minimum of 2% and a maximum of 7% of a three-year moving average of the market value of the endowed assets. Unless the terms of the gift instrument state otherwise, accumulated endowment gains may be spent over time by the University. Therefore, in accordance with Commonwealth of Pennsylvania law regarding the investment of trust funds, gains on permanently restricted funds are classified as temporarily restricted net assets until appropriated under the spending policy. Net gains in excess of the spending policy are reflected as nonoperating investment return activity.

The University has an endowment spending policy based on 5% of a three-year moving average market value with a minimum increase of 0% per year and a maximum increase of 10% per year over the prior year's spending rate.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

Any income earned in excess of the spending limit is reinvested while funds may be withdrawn from investment return earned in prior years if income is less than the spending policy provision. This is designed to insulate investment policy from budgetary pressures, and to insulate program spending from fluctuations in capital markets. Average annual spending rates per share were 5.6% and 5.2% for fiscal years 2016 and 2015, respectively.

Endowment net asset composition as of June 30, 2016 (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds (corpus)	\$ (27,131)	32,101	476,063	481,033
Board-designated endowment funds (corpus)	214,064	—	—	214,064
Accumulated gains on endowment funds	<u>155,747</u>	<u>257,348</u>	<u>—</u>	<u>413,095</u>
Total endowment net assets	\$ 342,680	289,449	476,063	1,108,192

Endowment net asset composition as of June 30, 2015 (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds (corpus)	\$ (10,543)	13,808	435,221	438,486
Board-designated endowment funds (corpus)	230,654	—	—	230,654
Accumulated gains on endowment funds	<u>175,149</u>	<u>323,879</u>	<u>—</u>	<u>499,028</u>
Total endowment net assets	\$ 395,260	337,687	435,221	1,168,168

LEHIGH UNIVERSITY
 Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

Changes in endowment net assets for the year ended June 30, 2016 (in thousands):

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Net assets, June 30, 2015	\$ 395,260	337,687	435,221	1,168,168
Investment return:				
Investment income	12,627	24	145	12,796
Net (depreciation) appreciation	<u>(28,328)</u>	<u>(8,772)</u>	<u>1,586</u>	<u>(35,514)</u>
Total investment return	<u>(15,701)</u>	<u>(8,748)</u>	<u>1,731</u>	<u>(22,718)</u>
Contributions	4,905	5	39,111	44,021
Board designations/changes in donor intent	(2,892)	-	-	(2,892)
Amounts appropriated for expenditure:				
Endowment spending distribution	(30,433)	(35,191)	-	(65,624)
Endowment operating expense	<u>(3,722)</u>	<u>(4,304)</u>	<u>-</u>	<u>(8,026)</u>
Total amounts appropriated for expenditure	<u>(34,155)</u>	<u>(39,495)</u>	<u>-</u>	<u>(73,650)</u>
Change in other endowment liabilities	<u>(4,737)</u>	<u>-</u>	<u>-</u>	<u>(4,737)</u>
Total change in endowment funds	<u>(52,580)</u>	<u>(48,238)</u>	<u>40,842</u>	<u>(59,976)</u>
Net assets, June 30, 2016	<u>\$ 342,680</u>	<u>289,449</u>	<u>476,063</u>	<u>1,108,192</u>

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

Changes in endowment net assets for the year ended June 30, 2015 (in thousands):

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Net assets, June 30, 2014	\$ 392,145	352,715	426,330	1,171,190
Investment return:				
Investment income	21,870	22	2,235	24,127
Net appreciation	<u>4,949</u>	<u>15,544</u>	<u>116</u>	<u>20,609</u>
Total investment return	<u>26,819</u>	<u>15,566</u>	<u>2,351</u>	<u>44,736</u>
Contributions	1,283	25	16,258	17,566
Board designations/changes in donor intent	9,811	1,697	(9,718)	1,790
Amounts appropriated for expenditure:				
Endowment spending distribution	(32,903)	(28,997)	—	(61,900)
Endowment operating expense	<u>(3,766)</u>	<u>(3,319)</u>	<u>—</u>	<u>(7,085)</u>
Total amounts appropriated for expenditure	<u>(36,669)</u>	<u>(32,316)</u>	<u>—</u>	<u>(68,985)</u>
Change in other endowment liabilities	<u>1,871</u>	<u>—</u>	<u>—</u>	<u>1,871</u>
Total change in endowment funds	<u>3,115</u>	<u>(15,028)</u>	<u>8,891</u>	<u>(3,022)</u>
Net assets, June 30, 2015	<u><u>\$ 395,260</u></u>	<u><u>337,687</u></u>	<u><u>435,221</u></u>	<u><u>1,168,168</u></u>

(4) Fair Value Measurements

The three levels of the fair value hierarchy are described below. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and lowest priority to unobservable inputs (Level 3 measurements):

Level 1 – Unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2 – Quoted prices for instruments that are identical or similar in markets that are not active and model-derived valuations for which all significant inputs are observable, either directly or indirectly in active markets.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

Level 3 – Prices or valuations that require inputs that are both significant to the fair value measurement and are unobservable.

The hierarchy requires the use of observable market data when available. The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the measurement.

The following discussion describes the valuation methodologies used for assets and liabilities measured at fair value:

(a) *Short-Term Assets and Liabilities*

The carrying amount of student accounts receivable, accounts payable and accrued expenses, and the commercial paper component of the University's debt approximates fair value due to the short maturity of these financial instruments.

(b) *Notes Receivable*

Notes receivable are carried at face value less an allowance for doubtful accounts. A reasonable estimate of the fair value of loans receivable under student loan programs is not practical to determine because the federally sponsored loans are subject to significant government restrictions as to marketability, interest rates, and repayment terms. Because of the early stage nature of the companies to which program loans are provided by BFTP and the lack of a secondary market for such securities, it is not practical to determine their fair value.

(c) *Contributions Receivable*

The University values contributions receivable at fair value on the date the pledge is received using the present value of future cash flows as described in note 8 based on Level 3 inputs. Contributions receivable are not measured at fair value subsequent to this initial measurement, because the discount rate selected for each contribution remains constant over time.

(d) *Funds Held in Trust by Others*

Funds held in trust by others are held and administered by outside trustees, with the University deriving income or a residual interest from the assets of such funds. Funds held in trust by others are recognized at the estimated fair value of the assets or the present value of the future cash flows when the irrevocable trust is established or the University is notified of its existence. As of June 30, 2016 and 2015, the inputs to fair value of these funds are classified as Level 2 or Level 3, depending on whether the assets will ultimately be distributed to the University.

(e) *Split-Interest Agreements*

Depending on the type of agreement, fair value measurements for split-interest agreements are performed either at inception or on a recurring basis. Fair value of the residual gift is generally based on the present value of expected future cash flows including payments to beneficiaries and investment return, and Level 3 inputs include the life expectancy of the donor and other beneficiaries as well as financial assumptions.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(f) *Debt and Related Interest Rate Swaps*

The fair value of variable rate revenue bonds is based on current interest rates for bonds of similar ratings and maturities. The fair value of fixed rate bond debt is determined by discounting future cash flows of each instrument at rates that reflect, among other things, market interest rates and the University's credit standing. The inputs to fair value of the University's debt are Level 2 inputs.

The fair value of the University's rate swap liability is based on valuations provided by an independent party, taking into account current interest rates and the current creditworthiness of the swap counterparties, which are considered Level 2 inputs to fair value.

(g) *Investments*

Fair value of equity securities has been determined from observable market quotations, when available. Fair value for fixed maturity securities is based upon prices provided by the University's investment managers and custodian banks. Both the investment managers and the custodian banks use a variety of pricing sources to determine fixed maturity market valuations.

Estimated fair value of alternative investments that are not readily marketable are recorded at the NAV as provided by external investment managers as a practical expedient for fair value. The University reviews and evaluates the values provided by external investment managers and agrees with the valuation methods and assumptions used in determining the NAV of those investments.

Certain investments that are measured at fair value using the NAV per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in the tables below are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

The following table presents the University's fair value hierarchy for investments at June 30, 2016 (in thousands):

	Fair value measurements at reporting date using				
	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Measured at NAV per share (or its equivalent)	Total
Short-term investments	\$ 69,021	—	—	—	69,021
Fixed income investments:					
U.S. government	103,210	42,874	—	—	146,084
Corporate	—	90,042	548	—	90,590
Other	—	3,300	—	—	3,300
Corporate stocks	22,192	—	—	—	22,192
Mutual and exchange-traded funds	191,661	—	—	—	191,661
Real estate	—	17,626	—	—	17,626
Alternative investments:					
Global equity	—	24,858	—	334,316	359,174
Hedged equity	—	—	—	59,585	59,585
Absolute return	—	—	—	252,878	252,878
Natural resources equity	56	5,071	—	18,415	23,542
Developed market credit	—	—	—	15,681	15,681
Private investments	—	—	—	300,089	300,089
Life insurance and other investments	<u>3,142</u>	<u>14</u>	<u>—</u>	<u>—</u>	<u>3,156</u>
Total investments	<u>\$ 389,282</u>	<u>183,785</u>	<u>548</u>	<u>980,964</u>	<u>1,554,579</u>

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

The following table presents the University's fair value hierarchy for investments at June 30, 2015 (in thousands):

	Fair value measurements at reporting date using				
	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Measured at NAV per share (or its equivalent)	Total
Short-term investments	\$ 6,100	—	—	—	6,100
Fixed income investments:					
U.S. government	106,657	55,295	—	—	161,952
Corporate	—	115,965	713	—	116,678
Other	—	6,905	—	—	6,905
Corporate stocks	19,863	—	—	—	19,863
Mutual and exchange-traded funds	239,284	—	—	—	239,284
Real estate	—	19,926	—	—	19,926
Alternative investments:					
Global equity	—	27,635	—	377,644	405,279
Hedged equity	—	—	—	65,323	65,323
Absolute return	—	—	—	273,305	273,305
Natural resources equity	252	6,536	—	21,862	28,650
Developed market credit	—	—	—	16,036	16,036
Private investments	—	—	—	299,720	299,720
Life insurance and other investments	<u>3,108</u>	<u>27</u>	<u>—</u>	<u>—</u>	<u>3,135</u>
Total investments	<u>\$ 375,264</u>	<u>232,289</u>	<u>713</u>	<u>1,053,890</u>	<u>1,662,156</u>

In accordance with ASU 2015-10, *Technical Corrections and Improvements*, the University removed \$34,171 as of June 30, 2015 from investments measured at NAV per share (or its equivalent) and included these amounts in Level 2 to correct the fair value hierarchy table.

LEHIGH UNIVERSITY
 Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

The following redemption table clarifies the nature, risk, and liquidity of the University's investments in alternative investment vehicles that calculate NAV per share (or its equivalent) at June 30, 2016 (in thousands):

	Fair value	Estimated remaining lives	Unfunded commitments	Redemption frequency after end of initial restriction period	Redemption notice period
Global equity (1)	\$ 334,316	N/A	\$ —	daily-quarterly	5–90 days
Hedged equity (2)	59,585	N/A	—	quarterly-annually various or not	45–80 days
Absolute return (3)	252,878	N/A	5,239	eligible monthly or not	30–180 days
Natural resources equity (4)	18,415	N/A	—	eligible	35 days
Developed market credit (5)	15,681	1–10 years	10,974	not eligible generally not	—
Private investments (6)	<u>300,089</u>	1–13 years	<u>140,097</u>	eligible	—
Total	<u><u>\$ 980,964</u></u>		<u><u>\$ 156,310</u></u>		

- (1) This category includes investments in both developed and emerging market equity funds. The portfolio's return is driven primarily by economic growth. Its primary objective is to capture the returns of publicly traded equities on a global developed market basis and the growth potential of emerging markets in order to provide long-term growth to the endowment. These funds will also provide a diversification to U.S. and other developed equity and bond markets. Investments representing approximately 14% of the total value in this category have restrictions that prevent full redemption at June 30, 2016.
- (2) This category's return is driven by economic growth and manager skill. Its primary objective is to provide opportunity to profit from positive equity market cycles while offering protection during negative equity market cycles in order to provide long-term growth to the endowment.
- (3) The primary objective of this category is to capture the returns associated with skill-based active management by exploiting the inefficiencies associated with marketable securities, thus providing a diversifying return stream with low correlation to returns of stocks and bonds. These funds will also provide principal protection in equity sell-offs. Investments representing approximately 11% of the total value in this category have restrictions that prevent full redemption at June 30, 2016.
- (4) Investment returns for this category are driven by a combination of global economic growth, as well as supply/demand curves in the commodity market. Funds gain direct and indirect exposure to commodities and natural resources through liquid, publicly traded securities in order to provide long-term growth to the endowment while providing principal protection in unexpected inflationary environments.

LEHIGH UNIVERSITY
Notes to Consolidated Financial Statements

June 30, 2016
(with comparative financial information for June 30, 2015)

- (5) This category's return is driven by a combination of changes in interest rates and credit spreads. Its objectives are to provide income, to mitigate overall portfolio volatility through its lower correlation to equity investments, and add yield over the U.S. Treasuries portfolio. These investments receive distributions through the liquidation of the underlying assets of the fund and do not have redemption provisions.
- (6) This category includes investments in private equity and real estate funds. Returns are driven primarily by economic growth. The primary objective of these funds is to provide long-term returns in excess of publicly traded equity markets, portfolio diversification relative to global equities and bonds, and long-term returns between that of stocks and bonds while carrying relatively lower risk than equities. These funds will also potentially offer some protection for the endowment in the event of inflation. All but one of these investments receives distributions through the liquidation of the underlying assets of the fund and do not have redemption provisions.

(5) Accounts Receivable

Accounts receivable at June 30, 2016 and 2015 (net of allowances for doubtful accounts) are as follows (in thousands):

	2016	2015
Accounts receivable, net:		
Student accounts	\$ 816	553
Grants and contracts	6,040	7,261
Investment income	1,788	2,806
Other	4,302	5,341
	<hr/> \$ 12,946	<hr/> 15,961

Allowances for doubtful accounts were \$2.6 million and \$2.3 million in 2016 and 2015, respectively.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
(with comparative financial information for June 30, 2015)

(6) Notes Receivable

Notes receivable at June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Notes receivable, net:		
University:		
Student loans	\$ 8,350	8,377
Other	2,903	2,975
Less allowance for doubtful loans	(285)	(285)
Total University	<u>10,968</u>	<u>11,067</u>
Independent operations:		
Program loans	11,563	10,631
Less allowance for doubtful accounts	(9,764)	(8,558)
Total independent operations	<u>1,799</u>	<u>2,073</u>
	<u>\$ 12,767</u>	<u>13,140</u>

Independent operations notes receivable primarily consist of loans provided by BFTP to early stage firms. The majority of these loans are fully reserved.

(7) Land, Buildings, and Equipment, Net

Land, buildings, and equipment are summarized as follows at June 30, 2016 and 2015 (in thousands):

	2016	2015
Land and improvements	\$ 62,560	57,431
Buildings and improvements	631,388	574,370
Furniture, equipment, books, and collections	198,986	193,985
Construction in progress	7,479	40,365
	<u>900,413</u>	<u>866,151</u>
Less accumulated depreciation	<u>(499,223)</u>	<u>(474,388)</u>
Total	<u><u>\$ 401,190</u></u>	<u><u>391,763</u></u>

Depreciation expense totaled \$27.7 million and \$26.3 million for the years ended June 30, 2016 and 2015, respectively.

LEHIGH UNIVERSITY
 Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

(8) Contributions

Unconditional promises to give are included in the consolidated financial statements as contributions receivable and revenue of the appropriate net asset category. Contributions arising from unconditional promises to give are recorded at fair value determined based on the present value of estimated future cash flows. Contributions receivable also include charitable remainder trusts where the University is not the trustee of the assets of the trust, but will receive a distribution upon its termination. The net present value of contributions receivable is calculated using a discount rate range of 1.76% to 5.05%. Outstanding pledges that were conditional amounted to \$16.7 million as of both June 30, 2016 and 2015. Unconditional promises are expected to be realized in the following periods (in thousands):

	2016	2015
In one year or less	\$ 16,682	12,352
Between one year and five years	17,468	42,526
More than five years	6,831	5,677
	40,981	60,555
Less:		
Unamortized discount	(1,325)	(1,494)
Allowance for uncollectible accounts	(2,626)	(2,373)
	\$ 37,030	56,688

(9) Net Assets

Temporarily restricted net assets include the following at June 30, 2016 and 2015 (in thousands):

	2016	2015
Contributions receivable	\$ 12,480	12,517
Temporarily restricted endowment funds	31,492	15,224
Life income funds	3,096	3,368
Accumulated gains on permanent endowment funds	257,957	322,463
Other – related to time and purpose restrictions	4,135	20,753
	\$ 309,160	374,325

Based upon spending restrictions in effect as of June 30, 2016, accumulated gains on permanent endowment funds are designated for the following future spending purposes: scholarships and fellowships 32%, professorships and chairs 12%, student loans 1%, other restrictions 10%, and no purpose restrictions 45%.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

Permanently restricted net assets include the following at June 30, 2016 and 2015 (in thousands):

	2016	2015
Contributions receivable	\$ 21,636	19,999
Permanent loan funds	2,226	2,074
Annuity and life income funds	26,058	49,626
Permanent endowment funds	<u>476,063</u>	<u>435,221</u>
	<u>\$ 525,983</u>	<u>506,920</u>

Included in life income funds are \$1.0 million (temporarily restricted) and \$1.9 million (permanently restricted) net assets classified as contributions receivable on the consolidated statement of financial position.

(10) Bonds, Loans, and Notes Payable

At June 30, 2016 and 2015, bonds, loans, and notes payable, including net unamortized discounts of \$0.9 million at both June 30, 2016 and 2015 and unamortized bond issuance costs of \$1.5 million and \$1.6 million at June 30, 2016 and 2015 respectively, consisted of the following (in thousands):

	2016	2015
Taxable Commercial Paper Series A, up to \$75 million, weighted average interest rate of 0.48% and 0.15% on June 30, 2016 and 2015 respectively; average duration of 28 days and 94 days for the years ended June 30, 2016 and 2015, respectively	\$ 20,000	55,000
Northampton County General Purpose Authority (NCGPA): Series 2000B bonds; tax-exempt variable rate revenue bonds, \$25,000 due serially from December 1, 2003 to December 1, 2030, variable rates of 0.43% and 0.05% on June 30, 2016 and 2015, respectively; bonds are supported with a standby bond purchase agreement, which expires on September 16, 2016	17,271	18,029
Series 2001 bonds; tax-exempt variable rate revenue bonds, \$21,780 due serially from October 15, 2006 to October 15, 2019, variable rates of 0.43% and 0.05% on June 30, 2016 and 2015, respectively; bonds are supported with a standby bond purchase agreement, which expires on September 16, 2016	10,791	13,468
Series 2004 bonds; tax-exempt index rate revenue bonds, \$50,000 due serially from May 15, 2025 to May 15, 2034, rates of 0.96% and 0.75% on June 30, 2016 and 2015, respectively	49,739	49,721

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
(with comparative financial information for June 30, 2015)

	2016	2015
Series 2006A bonds; tax-exempt variable rate revenue bonds, \$16,820 due serially from November 15, 2007 to November 15, 2021, variable rates of 0.40% and 0.05% on June 30, 2016 and 2015, respectively	\$ 10,414	11,938
Series 2007 bonds; tax-exempt revenue bonds, \$24,615 variable rate CPI bonds due serially from November 15, 2019 to November 15, 2025, variable rates of 2.03% and 1.10% on June 30, 2016 and 2015 respectively; \$2,975 term bonds, 4.375%, due November 15, 2031; \$26,335 term bonds, 4.5%, due November 15, 2036: Term bonds are insured by MBIA Insurance Corporation	53,488	53,455
Series 2009 bonds; 5.00% to 5.50% tax-exempt revenue bonds, \$66,165 due serially from November 15, 2029 to November 15, 2039	64,674	64,602
Taxable fixed rate term loan issued by Bank of America, N.A., \$15,000 due serially from February 1, 2012 to December 23, 2018, 2.61%	13,025	13,494
Fixed rate term loan (converted from September 10, 2012 construction loan) issued by Wells Fargo Bank, N.A. as agent for Lehigh Valley Economic Development Corporation Loan Pool to Lehigh University subsidiary BFTP, \$800 due serially from March 1, 2014 to March 1, 2017, balance due February 1, 2018, 3.5%	176	668
Mortgage issued by First Keystone National Bank assumed by Lehigh University subsidiary BFTP, \$528 due serially from June 23, 2010 to September 23, 2025; variable rate of 3.75% and 3.25% on June 30, 2016 and 2015, respectively	447	462
Interest free loan issued by Columbia Alliance for Economic Growth to Lehigh University subsidiary BFTP, \$250 due serially from June 30, 2010 to June 30, 2016	—	50
	<hr/> <hr/> \$ 240,025	<hr/> <hr/> 280,887

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

Proceeds from all tax-exempt bonds, loans, and notes were used by the University to purchase land and buildings, construct or renovate facilities, upgrade computing and information service facilities, purchase equipment, and finance certain completed facilities. Payment of all outstanding tax-exempt bonds is secured by separate loan agreements between the University and the Northampton County General Purpose Authority (NCGPA). Each loan agreement is a general obligation of the University for which it has pledged its full faith and credit. In addition, the University has granted NCGPA a security interest in the University's gross revenues as defined in each loan agreement. Pursuant to the NCGPA loan agreements, the University is required to establish rates and charges sufficient to provide, in each fiscal year, for the payment of the University's operating expenses and debt service on its long-term indebtedness. The University may incur additional indebtedness under certain conditions described in the loan agreements and the bond indentures.

BFTP debt was used for the renovation of a new business incubator facility, a building purchase, and other building renovations. The Wells Fargo loan is subject to a financial covenant requiring BFTP to maintain not less than two times the outstanding balance of the term loan in unencumbered liquid assets at all times.

At June 30, 2016, the aggregate annual maturities of long-term bonds, loans, and notes payable for the next five years and, thereafter, are as follows (in thousands):

2017	\$	5,878
2018		5,971
2019		17,753
2020		5,567
2021		5,753
Thereafter		181,436

The Series of 2000B, 2001, and 2006A bonds bear interest at a weekly rate determined by the remarketing agent. In 2013 all outstanding Series 2004 bonds were converted to a ten-year bank purchase and the prior standby bond purchase agreement was terminated. The Series 2004 bonds were converted from a weekly rate to a LIBOR index rate. The LIBOR Index Rate is set by the calculation agent on a monthly basis. The University may elect to convert to another variable rate mode or to a fixed mode as determined by the remarketing agent. The bondholders have a right to tender bonds at interest rate reset dates. The University entered into separate standby bond purchase agreements with banks to provide liquidity in case of tender of the 2000B or 2001 bonds. These agreements expire prior to the maturity of the bonds and may be extended at the University's request. However, the banks have no obligation to agree to the extended purchase period.

The University serves as the liquidity facility for its 2006A bonds and the Commercial Paper program. As of June 30, 2016, Lehigh estimates that \$71 million of liquid assets were available on a same day basis and an additional \$68 million was available within 30 days.

LEHIGH UNIVERSITY
 Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

As a component of the tax-exempt debt portfolio, the University entered into interest rate swap agreements that effectively convert certain variable rate revenue bond obligations to fixed rates or reduce the University's effective interest rate. As of June 30, 2016, the rate swaps are classified as Level 2 fair value financial instruments. Significant terms of each of the swap agreements are as follows (in thousands):

Series	Counterparty	Effective date	Current notional amount	University pays	University receives	Expiration date
2000B bonds	JPMorgan Chase Bank, N.A.	12/7/2000	\$ 17,365	4.530%	67% of USD-1 month LIBOR-BBA	12/1/2030
2001 bonds	JPMorgan Chase Bank, N.A.	9/4/2001	10,810	4.400	67% of USD-1 month LIBOR-BBA	10/15/2019
2004 bonds	Wells Fargo Bank, N.A.	12/18/2008	50,000	1.953	67% of USD-3 month LIBOR-BBA	5/15/2034
2006A bonds	JPMorgan Chase Bank, N.A.	8/24/2006	10,445	3.392	67% of USD-1 month LIBOR-BBA	11/15/2021
2007 CPI bonds	JPMorgan Chase Bank, N.A.	2/1/2007	24,615	3.980 to 4.100	Variable rate based on CPI-U	various through 11/15/2025
2009 bonds	Wells Fargo Bank, N.A.	3/19/2009	66,165	USD-SIFMA Municipal Swap Index	67% of USD-3 month LIBOR-BBA plus 1%	11/15/2039
			<u><u>\$ 179,400</u></u>			

(11) Derivative Instruments

The University employs derivatives, primarily interest rate swap agreements, to manage interest rate risk associated with outstanding debt. The endowment fund also includes a swap position as part of its portfolio. The fair value of the University's swap agreements is included in other liabilities in the statement of financial position, and was \$6.1 million and \$3.3 million at June 30, 2016 and 2015, respectively. The change in fair value of interest rate swaps is reflected in nonoperating activity on the statement of activities and was \$(3.2) million and \$1.0 million for the years ended June 30, 2016 and 2015, respectively.

Certain of the University's interest rate swap agreements contain provisions that require the University's debt to maintain an investment grade credit rating from each of the major credit rating agencies. If the University's debt were to fall below investment grade, it would be a violation of these provisions, and the counterparties to the rate swap agreement could request next-day full collateralization on all rate swaps in net liability positions. To date, the University has not posted collateral for any rate swap agreements. If the credit-risk related contingent features underlying these agreements were triggered on June 30, 2016, the University would be required to post an additional \$14.2 million of collateral to its counterparties.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

(12) Natural Expense Classification

The following table compares operating expenses by type for the years ended June 30, 2016 and 2015, respectively, (in thousands):

	2016	2015
Salaries and wages	\$ 167,519	162,010
Employee benefits	52,264	56,152
Utilities	7,802	9,767
Purchased services	34,680	33,010
Building and grounds maintenance	22,108	21,452
Depreciation	27,742	26,290
Interest	9,580	10,198
All other business expenses	<u>52,324</u>	<u>48,847</u>
Total	<u><u>\$ 374,019</u></u>	<u><u>367,726</u></u>

(13) Postretirement and Postemployment Benefits Other than Pensions

The University pays for a portion of the cost of medical insurance for retired employees and their eligible dependents. During fiscal year 2016, the University reimbursed retirees a maximum of \$96.50 per month for premium expenses, or a total of \$903,000 (as compared to \$830,000 in fiscal year 2015). The maximum monthly reimbursement amount will increase each year at the lesser of medical Consumer Price Index (CPI) or 8%. These postretirement medical benefits accrue from the later of date of hire or age 30. The University uses a July 1 measurement date for its plan. Summarized plan information is stated below (in thousands):

The following shows the reconciliation of the beginning and ending balances of the benefit obligation (in thousands):

	2016	2015
Benefit obligation at beginning of year	\$ 38,868	40,794
Operating:		
Service cost	1,302	1,539
Interest cost	1,846	1,877
Benefits paid	<u>(903)</u>	<u>(830)</u>
Total operating	<u><u>2,245</u></u>	<u><u>2,586</u></u>
Nonoperating:		
Actuarial gain	(455)	(9)
Assumption changes	<u>3,077</u>	<u>(4,503)</u>
Total nonoperating loss/(gain)	<u><u>2,622</u></u>	<u><u>(4,512)</u></u>
Benefit obligation at end of year	<u><u>\$ 43,735</u></u>	<u><u>38,868</u></u>

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016
 (with comparative financial information for June 30, 2015)

The following table sets forth the status of the plan, which is unfunded, at June 30, 2016 and 2015:

	2016	2015
Accumulated postretirement benefit obligation:		
Retirees	\$ 14,140	11,819
Fully eligible active plan participants	15,489	13,320
Other active plan participants	<u>14,106</u>	<u>13,729</u>
Total	43,735	38,868
Plan assets at fair value	<u>—</u>	<u>—</u>
Accumulated postretirement benefit liability	<u>\$ 43,735</u>	<u>38,868</u>

Weighted average assumptions for the years ended June 30, 2016 and 2015 are as follows:

	2016	2015
Discount rate for net periodic postretirement benefit cost	4.80%	4.65%
Discount rate for accumulated postretirement benefit obligation	4.15%	4.80%
Maximum increase in reimbursement rate	lesser of medical CPI or 8%	lesser of medical CPI or 8%

Assumed healthcare cost trend rate at June 30, 2016 and 2015 is as follows:

	2016	2015
Healthcare cost trend rate assumed for next year	4.00%	4.00%
Rate to which the cost trend rate is assumed to decline (ultimate rate)	4.00	4.00
Year that ultimate rate is reached	N/A	N/A

Impact of 1% increase in assumed healthcare cost trend rate at June 30, 2016 and 2015 is as follows (in thousands):

	2016	2015
Increase in accumulated postretirement benefit obligation	\$ 8,930	8,008
Increase in net periodic postretirement benefit cost	804	900

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

Estimated future University contributions reflecting expected future service are as follows (in thousands):

Fiscal year ending June 30:	\$	
2017	\$ 951	
2018	1,048	
2019	1,165	
2020	1,274	
2021	1,382	
2022 through 2026	8,742	

(14) Retirement Plans

The University provides pensions to substantially all salaried faculty and staff through a defined contribution plan administered by Teacher's Insurance and Annuity Association / College Retirement Equities Fund. The plan features base contributions from the University and voluntary employee contributions with a University match. Total expense for this plan was \$14.5 million and \$14.4 million in 2016 and 2015, respectively.

(15) Grants and Contracts

The University receives grant and contract revenue from various government agencies and private sources for the support of research, training, and other sponsored programs. Revenues associated with the direct costs of these programs are recognized as the related costs are incurred. Indirect cost reimbursements from federal agencies are based on predetermined rates negotiated with the University's cognizant agency, the Office of Naval Research, and are in effect through fiscal year 2017. These rates are also used for other sponsored programs except where separately negotiated. Indirect cost reimbursements from all sources totaled \$7.9 million and \$8.6 million in 2016 and 2015, respectively.

(16) Fund-Raising Costs

Fund-raising costs were approximately \$13.5 million and \$13.6 million in 2016 and 2015, respectively, and are included in institutional support in the consolidated statement of activities.

(17) Commitments and Contingencies

Open commitments for contracts with general contractors amounted to approximately \$0.7 million and \$7.1 million as of June 30, 2016 and 2015, respectively.

The University leases certain equipment and real property. These leases are classified as operating leases and have lease terms ranging from one to seven years. Total lease expense for both fiscal 2016 and 2015 was approximately \$1.1 million.

LEHIGH UNIVERSITY

Notes to Consolidated Financial Statements

June 30, 2016

(with comparative financial information for June 30, 2015)

(18) Income Taxes

The University has been recognized by the Internal Revenue Service (IRS) as exempt from federal income tax under Section 501(c)(3) of the U.S. Internal Revenue Code, except for taxes on income from activities unrelated to its exempt purpose. Accordingly, no provisions for income taxes have been made in the accompanying consolidated financial statements. Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the University and recognize a tax liability (or asset) if the University has taken an uncertain tax position that more likely than not would not be sustained upon examination by the IRS. Management has analyzed the tax positions taken by the University, and has concluded that as of June 30, 2016, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The University is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

(19) Subsequent Events

On October 6, 2016, the University issued \$150,000,000 aggregate principal amount of its Series 2016 taxable bonds (the Bonds). The Bonds are secured by a pledge of and security interest in the University's gross revenues. The proceeds of the Bonds will be used to finance current and future capital projects consistent with the University's capital plan, to pay the costs of issuance, and any other purpose duly authorized by the University.

Concurrently, the Northampton County General Purpose Authority (NCGPA) issued \$26,715,000 Higher Education Fixed Rate Revenue Bonds, Series A of 2016 (the 2016A Bonds) and \$74,950,000 Higher Education Variable Rate Revenue Bonds, Series B of 2016 (the 2016B Bonds). The 2016A Bonds are tax-exempt bonds for the purpose of refunding, on a current basis, the University's 2007 term bonds, as well as paying certain issuance costs. The 2016B Bonds are tax-exempt bonds for the purpose of the legal defeasance of all of the University's 2009 Bonds. The University also entered into an interest rate swap agreement to effectively convert the 2016B Bonds to fixed rates and reduce the University's effective interest rate.

LEHIGH UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2016

Program: Federal sponsor/project title	CFDA #	Pass-through entity Identifying number	Pass-through entity	Passed through to subrecipients	Total expenditures
Student Financial Assistance Cluster:					
U.S. Department of Education:				\$	
Federal Supplemental Education Opportunity Grant	84.007			—	372,000
Federal Perkins Loan Program	84.038			—	2,707,827
Federal Work Study Program	84.033			—	453,222
Federal Pell Grant Program	84.063			—	3,164,201
Federal Direct Loan Program	84.268			—	22,337,429
Total Student Financial Assistance Cluster				—	29,034,679
Research and Development Cluster:					
DOD – Office of Economic Adjustment:				—	
Economic Adjustment Assistance for State Governments	12.617			—	17,757
DOD – Defense Threat Reduction Agency:				—	
Basic Scientific Research – Combating Weapons of Mass Destruction	12.351			—	218,723
DOD – U.S. Air Force :				29,004	
Air Force Defense Research Sciences Program	12.800		National Center for Defense Manufacturing and Machining	208,442	631,931
Air Force Defense Research Sciences Program	12.800	FA8650-12-2-7230			298,837
DOD – U.S. Army-Research Laboratory:					
Basic Scientific Research	12.431			80,279	323,725
Basic Scientific Research	12.431	W15QKN-09-9-1001	Keystone Automation Inc	—	25,250
Basic Scientific Research	12.431	W911NF-12-2-0033	Steel Founders Society of America	—	10,818
DOD – U.S. Navy:				684,192	
Basic and Applied Scientific Research	12.300			—	2,003,980
Basic and Applied Scientific Research	12.300	N00014-14-1-0533	University Of Virginia	—	156,839
Basic and Applied Scientific Research	12.300	N00014-15-1-2080	Wright State University	—	55,443
Basic and Applied Scientific Research	12.300	N00014-14-C-0078	E-Harvest Systems	—	39,151
DOD – Defense Logistics Agency:				—	
Defense Logistics Agency	12.000	SP4701-11-D-0025	Advance Technology Institute	—	63,800
DOD – Defense Advanced Research Projects Agency:				—	
Research and Technology Development	12.910	HR0011-12-C-0035	The Boeing Company	—	203,707
DOD – National Security Agency:				—	
Mathematical Sciences Grants Program	12.901			—	23,875
U.S. Dept of Energy:					
General Area	81.000	DE-AC52-06NA25396	Los Alamos National Lab	—	80,297
General Area	81.000	DE-AC02-05CH11231	Lawrence Berkley National Lab	—	15,764
General Area	81.000	DE-AC52-07NA27344	Lawrence Livermore National Lab	—	18,847
General Area	81.000	DE-EE0005660	United States Council for Automotive Research	—	24,097
Basic Energy Sciences University and Science Education	81.049			77,795	1,588,653
Basic Energy Sciences University and Science Education	81.049	DE-SC00-12577	Georgia Institute of Technology	—	153,966
Basic Energy Sciences University and Science Education	81.049	DE-SC00-09651	UHV Technologies, Inc	—	92,343
Basic Energy Sciences University and Science Education	81.049	DE-AC02-09CH11466	Princeton Plasma Physics Lab	—	44,774
Basic Energy Sciences University and Science Education	81.049	DE-SC00-01057	Carnegie Institute of Washington	—	154,673
Inertial Fusion Science – Support of Stockpile Stewardship	81.112			—	153,705
Energy Efficiency and Renewable Energy Information Dissemination, Outreach, Training and Technical Analysis/Assistance (B)	81.117			—	412,665
Nuclear Energy Research, Development and Demonstration	81.121			108,580	200,165

LEHIGH UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2016

Program: Federal sponsor/project title	CFDA #	Pass-through entity Identifying number	Pass-through entity	Passed through to subrecipients	Total expenditures
Electricity Delivery and Energy Reliability, Research Development and Analysis (B)	81.122	DE-OE00000779	University of Arkansas	\$ —	225,927
Advanced Research and Projects Agency – Energy Financial Assistance Program	81.135	DE-AR00000582	Advanced Cooling Technologies Inc.	—	174,106
U.S. Department of Education:					
Graduate Assistance in Areas of National Need	84.200			—	256,007
Education Research, Development and Dissemination	84.305	R305A140356	Ohio University	—	374,214
Research in Special Education	84.324		Ohio State University	—	164,966
Research in Special Education	84.324	1R324A130066	Ohio State University	—	176,156
National Institutes of Health:					
Oral Diseases and Disorders Research	93.121			—	369,469
Health Services Research and Development Grants	93.226	1R18HS018649-01A1	Lehigh Valley Health Network	—	8,002
Mental Health Research Grants	93.242	1R01MH094435-01A1	Univ. of North Carolina – Greensboro	—	324,977
Mental Health Research Grants	93.242	7R01MH099557-05	Wayne State University	—	74,663
Drug Abuse and Addiction Research Programs	93.279	2R01DA032950-05A1	University of Washington	—	10,819
Drug Abuse and Addiction Research Programs	93.279	1R41DA032464-01	Ophidion, Inc	—	125,038
Discovery and Applied Resh for Tech Innovations to Imp Human Health	93.286		University of Arizona	23,772	130,655
Minority Health and Health Disparities Research	93.307	1R01MD008940	University of Arizona	—	72,065
Cancer Treatment Research	93.395			74,054	159,234
Cancer Biology Research	93.396			39,288	88,272
Affordable Care Act (ACA) Maternal, Infant, and Early Childhood Home Visiting Research Programs	93.615			35,555	134,676
Cardiovascular Diseases Research	93.837			—	126,667
Blood Diseases and Resources Research	93.839	5R01HL082808-11	Emory University	—	54,374
Blood Diseases and Resources Research	93.839	2P01HL040387-26A1	University of Pennsylvania	—	63,139
Arthritis Musculoskeletal and Skin Diseases Research	93.846	2U54AR055073-09	University of Med. & Dent. of NJ	—	325,020
Clinical Research Related to Neurological Disorders	93.853			—	180,657
Allergy Immunology and Transplantation Research	93.855	2R42AI091049-03	TB Biosciences, Inc	—	3,769
Pharmacology Physiology and Biological Chemistry	93.859			104,257	1,024,130
Child Health and Human Development Extramural Research	93.865			86,135	989,568
Vision Research	93.867			—	96,965
Medical Library Assistance	93.879			—	28,846
U.S. Department of Interior:					
Cooperative Endangered Species Conservation Fund	15.615	TX E150-R	Texas Parks and Wildlife Department	—	5,313
Earthquake Hazards Research Grants	15.807			—	40,461
U.S. Department of Transportation:					
U.S. Department of Transportation	20.000			—	14,649
Highway Research and Development Program (B)	20.200			258,423	492,054
National Recreational Trails Funding Program	20.219			144,330	144,330
Public Transportation Research	20.514	HR 24-36	Regents Of Univ Of Minnesota	—	126,722
National Aeronautics and Space Administration:					
State Grants for Assistive Technology	43.001	NNX10AK74H	PA Space Grant Consortium	—	8,129
Education	43.008	NNX15AK06H	Penn State University	—	313
National Science Foundation:				—	
ARRA – Trans-NSF Recovery Act Research Support	47.082			35,398	96,358
Engineering Grants	47.041			29,360	3,827,134
Engineering Grants	47.041	CBET-1403239	Georgia Institute of Technology	—	(25)
Engineering Grants	47.041	CMMI-0927178	Purdue University	—	33,523
Engineering Grants	47.041	IIP-1456358	Brighton Technologies Group, Inc.	—	49,952
Engineering Grants	47.041	IIP-1256080	Love Park Robotics, Inc.	—	312
Mathematical and Physical Sciences	47.049			—	1,582,868

LEHIGH UNIVERSITY
 Schedule of Expenditures of Federal Awards
 Year ended June 30, 2016

Program: Federal sponsor/project title	CFDA #	Pass-through entity Identifying number	Pass-through entity	Passed through to subrecipients	Total expenditures
Geosciences	47.050			\$ —	440,175
Geosciences	47.050	EAR-1239285	The Pennsylvania State University	—	5,006
Computer and Information Science and Engineering	47.070			—	1,161,597
Biological Sciences	47.074			—	222,713
Biological Sciences	47.074	EF#-1137306	Massachusetts Institute of Technology	34,301	100,292
Social Behavioral and Economic Sciences	47.075			—	131,183
Social Behavioral and Economic Sciences	47.075	SMA-1416651	Yale University	—	69,436
Education and Human Resources	47.076			—	366,435
Polar Programs	47.078			—	41,353
Total Research And Development Cluster				2,053,165	21,736,449
Other Clustered Programs:					
Public Works And Economic Development Cluster:					
Economic Adjustment Assistance (Revolving Loan Fund)	11.307			—	352,676
Total Public Works and Economic Deveopment and Adjustment Assistance Cluster				—	352,676
Total Other Clustered Programs				—	352,676
Other:					
Department of Agriculture:					
Wholesale Farmers and Alternative Market Development	10.164			—	2,418
Child and Adult Care Food Program	10.558	300-48-383-0	PA-Department of Education	—	8,074
National Endowment for the Humanities:					
Promotion of the Humanities Challenge Grants	45.100			—	445,401
DOD – Defense Logistics Agency:					
Procurement Technical Assistance	12.002	SP4800-14-2-1436	University of Pennsylvania	—	4,634
Procurement Technical Assistance	12.002	SP4800-15-2-1536	University of Pennsylvania	—	66,818
Total CFDA				—	71,452
Department of State:					
Educational Exchange – Univeristy Lecturers (Professors) and Researchers	19.401	S-ECAGD-13-CA-149	Institute of International Education	5,000	63,932
U.S. Securities and Exchange Commission:					
Securities Investiation of Complaints and SEC Information	58.001			—	39,230
Small Business Administration:					
Small Business Development Centers	59.037	SBAHQ-15-B-0053	University of Pennsylvania	—	60,633
Small Business Development Centers	59.037	SBAHQ-16-B-0043	University of Pennsylvania	—	249,159
Total CFDA				—	309,792

LEHIGH UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2016

Program: Federal sponsor/project title	CFDA #	Pass-through entity Identifying number	Pass-through entity	Passed through to subrecipients	Total expenditures
Entrepreneurial Development Disaster Assistance	59.064	SBAHQ-13-E-0011	University of Pennsylvania	\$ —	21,199
Department of Education					
Special Education – Personnel Prep to Improve Services and Results	84.325			1,453	254,541
School Leadership	83.363			18,950	167,316
Department of Health and Human Services					
Head Start	93.600			—	5,135
Total Other				25,403	1,388,490
Total Expenditures of Federal Awards				\$ 2,078,568	52,512,294

See accompanying notes to Schedule of Expenditures of Federal Awards.

LEHIGH UNIVERSITY

Notes to Schedule of Expenditures of Federal Awards

Year ended June 30, 2016

(1) Basis of Presentation

The accompanying schedule of expenditures of federal awards (Schedule) includes the federal award activity of Lehigh University (the University) under programs of the federal government for the year ended June 30, 2016 in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the University, it is not intended to, and does not, present the financial position, changes in net assets, or cash flows of the University. The schedule of expenditures of federal awards does not present the activity for the University's subsidiary Manufacturers Resource Center that expended \$828,947 in federal awards and submits a separate audit report in accordance with the Uniform Guidance.

(2) Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following, as applicable, either the cost principles in Office of Management and Budget Circular A-21, *Cost Principles for Educational Institutions*, or the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

(3) Indirect Cost Rate

The University has not elected to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance.

(4) Federal Perkins Loan Program

Perkins loans are administered directly by the University, and balances and transactions relating to Perkins loans are included in the University's consolidated financial statements. Perkins loan expenditures reported on the Schedule include the balance of outstanding loans at June 30, 2015, loans made during the year ended June 30, 2016 of \$227,602 and the administrative cost allowance claimed during the year ended June 30, 2016 of \$90,401. The outstanding balance of Federal Perkins Loans at June 30, 2016 was \$2,288,827.

There were no federal or institutional capital contributions to the Perkins revolving loan fund for the year ended June 30, 2016.

(5) Direct Loans

Direct Loans are made by the Secretary of Education, and therefore balances and transactions relating to Direct Loans are not included in the University's consolidated financial statements. The University is responsible for the performance of certain administrative duties under the Direct Loan program, including origination and disbursement of loans.

LEHIGH UNIVERSITY

Notes to Schedule of Expenditures of Federal Awards

Year ended June 30, 2016

(6) Revolving Loan Fund

The Lehigh and Northampton Counties Revolving Loan Fund (RLF) has as its principal activity to provide capital (in the form of loans) to new and existing businesses for the purpose of creating and retaining permanent private sector jobs. Additional “other funding” of \$50,000 was recorded during the year from Northampton County, and is included when calculating the ratio of federal and local match for the year ended June 30, 2016. At June 30, 2016, the assets of the fund were as follows:

Cash and investments	\$ 287,499
Loans receivable	<u>234,689</u>
Total RLF assets	<u><u>\$ 522,188</u></u>

The RLF expended \$6,801 on administrative expenses for the year ended June 30, 2016. The federal portion of the RLF is 66.67%. The total expenditures reported on the schedule of expenditures of federal awards (SEFA) is \$352,676, which is 66.67% of both the RLF’s assets at June 30, 2016 and the RLF’s administrative expenses for the year ended June 30, 2016.



KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

**Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance
and Other Matters Based on an Audit of Financial Statements Performed in Accordance With
*Government Auditing Standards***

The Board of Trustees
Lehigh University:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the consolidated financial statements of Lehigh University (the University) which comprise the consolidated statement of financial position as of June 30, 2016, and the related consolidated statements of activities and cash flows for the year then ended⁵ and the related notes to the consolidated financial statements, and have issued our report thereon dated October 24, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the University's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control. Accordingly, we do not express an opinion on the effectiveness of the University's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.



Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the University's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Philadelphia, Pennsylvania

October 24, 2016



KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report on Compliance for the Major Federal Program; Report on Internal Control Over Compliance; and Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

The Board of Trustees
Lehigh University:

Report on Compliance for the Major Federal Program

We have audited Lehigh University's (the University's) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the University's major federal program for the year ended June 30, 2016. The University's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal program.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for Lehigh University's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the University's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the University's compliance.

Opinion on the Major Federal Program

In our opinion, Lehigh University complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2016.

Report on Internal Control Over Compliance

Management of Lehigh University is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the University's internal control over compliance with the types of



requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the consolidated financial statements of Lehigh University as of and for the year ended June 30, 2016, and have issued our report thereon dated October 24, 2016, which contained an unmodified opinion on those consolidated financial statements. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Philadelphia, Pennsylvania
March 20, 2017

LEHIGH UNIVERSITY
Schedule of Findings and Questioned Costs
Year ended June 30, 2016

(1) Summary of Auditors' Results

- (a) Type of report issued on whether the consolidated financial statements were prepared in accordance with generally accepted accounting principles: **Unmodified**
- (b) Internal control deficiencies over financial reporting disclosed by the audit of the consolidated financial statements:
 - Material weaknesses: **No**
 - Significant deficiencies: **None Reported**
- (c) Noncompliance material to the financial statements: **No**
- (d) Internal control deficiencies over the major program disclosed by the audit:
 - Material weaknesses: **No**
 - Significant deficiencies: **None reported**
- (e) Type of report issued on compliance for the major program: **Unmodified**
- (f) Audit findings that are required to be reported in accordance with 2 CFR 200.516(a): **No**
- (g) Major program:
 - Research and Development Cluster (various CFDA numbers)
- (h) Dollar threshold used to distinguish between Type A and Type B programs: **\$ 1,575,369**
- (i) Auditee qualified as a low-risk auditee: **Yes**

(2) Findings Relating to the Financial Statements Reported in Accordance with *Government Auditing Standards*

None

(3) Findings and Questioned Costs Relating to Federal Awards

None