UNIVERSITY OF ILLINOIS
HEALTH SERVICES FACILITIES SYSTEM

Annual Financial Report

June 30, 2015

(With Independent Auditors' Report Thereon)

CliftonLarsonAllen

UNIVERSITY OF ILLINOIS
HEALTH SERVICES FACILITIES SYSTEM

Annual Financial Report

June 30, 2015

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UNIVERSITY OF ILLINOIS
Urbana-Champaign ● Chicago ● Springfield

Office of Vice President/Chief Financial Officer, Comptroller
349 Henry Administration Building
506 South Wright Street
Urbana, IL 61801

December 23, 2015

Holders of University of Illinois
Health Services Facilities System Revenue Bonds
and The Board of Trustees of the University of Illinois:

I am pleased to transmit the Annual Financial Report of the University of Illinois Health Services Facilities System for the fiscal year ended June 30, 2015. This report supplements the financial statements of the University of Illinois presented in the Annual Financial Report.

The 2015 financial statements and accompanying notes appearing on pages 4 through 30 have been audited by CliftonLarsonAllen LLP, Independent Certified Public Accountants, as special assistants to the Auditor General of the State of Illinois, whose report on the financial statements appears on pages 2 and 3.

CliftonLarsonAllen LLP will also prepare a report for the year ended June 30, 2015, containing special data requested by the Auditor General and another report covering their audit of the compliance of the University with applicable state and federal laws and regulations for the year ended June 30, 2015. These reports, which include some data related to the Health Services Facilities System, are not contained herein and are primarily for the use of the Auditor General and state and federal agencies.

Very truly yours,

Walter K. Knorr

Walter K. Knorr,
Vice President/Chief Financial Officer,
Comptroller

CliftonLarsonAllen LLP
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INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General, State of Illinois
and
Board of Trustees
University of Illinois

Report on the Financial Statements

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the business-type activities of the University of Illinois Health Services Facilities System ("the System") as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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 financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities for the System as of June 30, 2015, and the changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

The June 30, 2014 financial statements of the System were audited by other auditors whose report dated December 19, 2014 expressed an unmodified opinion. Based on the report from other auditors, the summarized comparative information presented herein as of and for the year ended June 30, 2014, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Emphasis of Matter

During fiscal year ended June 30, 2015, the System adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, and the related GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date — an amendment of GASB Statement No. 68.* As a result of the implementation of these standards, the University reported a restatement for the change in accounting principle. See Note 1. Our auditors' opinion was not modified with respect to the restatement.

As discussed in Note 1A, the financial statements of the System are intended to present the financial position, the changes in financial position, and cash flows of only that portion of the business-type activities of University of Illinois that is attributable to the transactions of the System. They do not purport to, and do not, present fairly the financial position of University of Illinois as of June 30, 2015 and 2014, and its changes in financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report under separate cover dated December 23, 2015, on our consideration of the System'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 the 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 the System's internal control over financial reporting and compliance.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Peoria, Illinois
December 23, 2015

UNIVERSITY OF ILLINOIS
HEALTH SERVICES FACILITIES SYSTEM

Statement of Net Position

June 30, 2015
(with comparative totals for June 30, 2014)

Assets and Deferred Outflow of Resources	2015	2014
Current assets:		
Claim on cash and on pooled investments	$ 189,930,030	161,634,663
Restricted claim on cash and on pooled investments, required for current liabilities	1,152,600	1,148,890
Restricted cash and cash equivalents	3,093	5,932
Accrued investment income	495,637	512,900
Patient accounts receivable, net	127,943,521	115,244,807
Other receivables	10,091,943	9,363,605
Inventories	6,037,514	5,799,381
Prepaid expenses, deposits, and other assets	449,984	701,512
Total current assets	336,104,322	294,411,690
Noncurrent assets:		
Restricted claim on cash and on pooled investments – less amount required for current liabilities disclosed above	12,584,104	8,591,077
Restricted cash and cash equivalents	2,860,508	4,001,804
Restricted investments	35,430,662	41,014,693
Capital assets, net of accumulated depreciation	185,918,874	186,123,445
Total noncurrent assets	236,794,148	239,731,019
Deferred outflow of resources	6,191,377	6,686,539
Total assets and deferred outflow of resources	$ 579,089,847	540,829,248
Liabilities and Net Position		
Current liabilities:		
Accounts payable	$ 35,103,846	30,333,751
Accrued payroll	17,842,121	20,229,656
Accrued interest payable	1,155,693	1,154,822
Estimated third-party settlements	62,319,695	28,936,396
Unearned revenues	227,001	165,230
Current maturities of long-term debt	5,382,584	5,231,217
Current portion of accrued compensated absences	2,277,559	2,783,092
Total current liabilities	124,308,499	88,834,164
Noncurrent liabilities:		
Long-term debt, net of current maturities	119,460,948	124,843,532
Accrued compensated absences, net of current portion	20,543,550	20,247,857
Derivative instrument – swap liability	4,251,511	4,574,241
Total noncurrent liabilities	144,256,009	149,665,630
Total liabilities	268,564,508	238,499,794
Net investment in capital assets	100,893,244	101,158,868
Restricted:		
Expendable for capital projects	12,636,514	10,691,930
Expendable for debt service	4,818	3,511
Unrestricted	196,990,763	190,475,145
Total net position	310,525,339	302,329,454
Total liabilities and net position	$ 579,089,847	540,829,248

See accompanying notes to financial statements.

UNIVERSITY OF ILLINOIS
HEALTH SERVICES FACILITIES SYSTEM

Statement of Revenues, Expenses and Changes in Net Position

Year ended June 30, 2015
(with comparative totals for the year ended June 30, 2014)

	2015	2014
Operating revenues:		
Net patient service revenues	$ 570,114,728	547,813,660
Payments on behalf of the System	21,488,592	17,463,650
Other revenues	46,959,539	39,640,925
Total operating revenues	638,562,859	604,918,235
Operating expenses:		
Salaries and wages	286,104,950	295,665,666
Fringe benefits	205,917,082	205,633,239
Supplies and general expenses	296,026,345	248,528,846
Administrative services	21,972,364	22,210,495
Depreciation and amortization	18,613,216	17,894,879
Total operating expenses	828,633,957	789,933,125
Operating loss	(190,071,098)	(185,014,890)
Nonoperating revenues (expenses):		
On-behalf payments for fringe benefits	198,745,979	197,707,845
State appropriations	43,987,500	45,000,000
Transfer of State appropriations to the Illinois DHFS Hospital Services Fund	(43,987,500)	(45,000,000)
Net (decrease) increase in fair value of investments	(984,818)	2,916,616
Interest on capital asset related debt	(1,482,341)	(2,026,174)
Investment income (net of related expenses)	2,301,715	1,126,421
Loss on disposal of capital assets	(205,645)	(458,961)
Other nonoperating (expenses) revenues, net	(107,907)	400,482
Net nonoperating revenues	198,266,983	199,666,229
Increase in net position	8,195,885	14,651,339
Net position, beginning of year	302,329,454	287,678,115
Net position, end of year	$ 310,525,339	302,329,454

See accompanying notes to financial statements.

UNIVERSITY OF ILLINOIS
HEALTH SERVICES FACILITIES SYSTEM

Statement of Cash Flows

Year ended June 30, 2015
(with comparative totals for the year ended June 30, 2014)

	2015	2014
Cash flows from operating activities:		
Patient services	$ 590,799,312	550,353,890
Payments to suppliers	(287,613,084)	(246,089,031)
Payments for administrative services	(21,972,364)	(22,210,495)
Payments to employees	(272,191,485)	(279,264,129)
Payments for benefits	(7,380,943)	(8,916,208)
Other receipts	46,292,972	40,614,986
Net cash provided by operating activities	47,934,408	34,489,013
Cash flows from noncapital financing activities:		
Other receipts	138,184	75,774
Net cash provided by noncapital financing activities	138,184	75,774
Cash flows from capital and related financing activities:		
Proceeds on issuance of bonds		71,376,216
Purchases of capital assets	(13,066,366)	(28,304,754)
Principal paid on capital debt and leases	(5,210,882)	(6,554,221)
Interest paid on capital debt and leases	(5,565,567)	(3,891,724)
Payments on issuance of bonds		(664,608)
Net cash (used in) provided by capital and related financing activities	(23,842,815)	31,960,909
Cash flows from investing activities:		
Interest on investments	2,093,754	1,341,096
Pooled cash allocated (to) from University related to unrealized (losses) gains	(984,818)	2,916,616
Purchases of investments	(54,609,246)	(69,850,940)
Sales of investments	60,418,502	28,533,848
Net cash provided by (used in) investing activities	6,918,192	(37,059,380)
Net increase in cash and cash equivalents	31,147,969	29,466,316
Cash and cash equivalents, beginning of year	175,382,366	145,916,050
Cash and cash equivalents, end of year	$ 206,530,335	175,382,366

(Continued)

UNIVERSITY OF ILLINOIS
HEALTH SERVICES FACILITIES SYSTEM

Statement of Cash Flows

Year ended June 30, 2015
(with comparative totals for the year ended June 30, 2014)

	2015	2014
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss	$ (190,071,098)	(185,014,890)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization expense	18,613,216	17,894,879
Provision for uncollectible accounts	38,365,504	41,664,505
On-behalf payments for fringe benefits	198,745,979	197,707,845
Changes in assets and liabilities:		
Patient receivables	(51,064,219)	(24,046,358)
Other receivables	(728,338)	808,832
Inventories	(238,133)	21,447
Prepaid expenses, deposits, and other assets	(89,713)	(55,140)
Accounts payable and accrued expenses	1,165,980	1,411,394
Estimated third-party settlements	33,383,299	(15,077,917)
Accrued compensated absences	(209,840)	(990,814)
Unearned revenues	61,771	165,230
Net cash provided by operating activities	$ 47,934,408	34,489,013
Noncash investing, capital, and financing activities:		
On-behalf payments for fringe benefits	$ 198,745,979	197,707,845
State appropriation	43,987,500	45,000,000
Transfers to Illinois DHFS Hospital Services Fund	(43,987,500)	(45,000,000)
Other capital asset adjustments	(246,092)	901,511
Net interest capitalized	4,236,195	3,069,717
Increase (decrease) of capital assets obligations in accounts payable	1,216,580	(1,192,141)
Capital assets acquired through capital leases		2,084,800
Loss on disposal of capital assets	(205,645)	(458,961)
Capital assets placed in service subsequent to obligation incurrence	341,241	3,071,175

See accompanying notes to financial statements.

(1) Summary of Significant Accounting Policies

Organizational Background and Basis of Presentation

The University of Illinois Health Services Facilities System (System) comprises the University of Illinois Hospital (Hospital) and associated clinical facilities providing patient care at, but not limited to, the University of Illinois at Chicago Medical Center. The System is a tertiary care facility located primarily in Chicago, Illinois offering a full range of clinical services. The System does not include the operations of the University of Illinois' medical service plans or Colleges of Medicine. Management of the System is the responsibility of the University of Illinois (University).

The System was established by a Bond Resolution (Resolution) of the Board of Trustees (Board) of the University of Illinois adopted on January 22, 1997. These financial statements have been prepared to satisfy the requirements of the 1997B, 2008 and 2013 bond indentures. The financial balances and activities of the System, included in these financial statements, are included in the University's financial statements. The financial statements of the System are prepared in accordance with U.S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The System is not a separate legal entity and has not presented management's discussion and analysis.

The financial statements include certain prior year comparative information that has been derived from the System's 2014 financial statements. Such information does not include all of the information required to constitute a presentation in conformity with U.S. generally accepted accounting principles. Accordingly, such information should be read in conjunction with the System's financial statements for the year ended June 30, 2014.

Certain items in the June 30, 2014 comparative information have been reclassified to correspond to the June 30, 2015 financial statement presentation.

Significant Accounting Policies

(a) Financial Statement Presentation and Basis of Accounting

The System prepared its financial statements as a Business Type Activity, as defined by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, using the economic resources measurement focus and the accrual basis of accounting. Business Type Activities are those financed in whole or in part by fees charged to external parties for goods and services.

Under the accrual basis, revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Advances are classified as unearned revenues.

(b) Cash and Cash Equivalents

The Statement of Cash Flows details the change in the cash and cash equivalents balance for the fiscal year. Cash and all liquid investments with original maturities of ninety days or less are defined as cash and cash equivalents.

(c) Investments

Investments are recorded at fair value. Fair value is determined by quoted market prices for most of the System's investments. Fair value for investments in certain mutual funds is determined using net asset values as provided by external investment managers.

(d) Inventories

Inventories of pharmaceutical and other supplies are stated at the lower of cost, determined using the first-in, first-out method, or market.

(e) Capital Assets

Capital assets are recorded at cost or, if donated, at fair value at the date of a gift. Depreciation of the capital assets is calculated on a straight-line basis over the estimated useful lives (see below) of the respective assets. The System's policy requires the capitalization of land and collection purchases regardless of cost, equipment over $5,000, software, easements, buildings and improvements over $100,000 and infrastructure over $1,000,000. The System does not capitalize collections of works of art or historical treasures held for public exhibition, education or research in furtherance of public service rather than capital gain, unless they were previously capitalized as of June 30, 1999. Proceeds from the sale, exchange or other disposal of any item belonging to a collection of works of art or historical treasures must be applied to the acquisition of additional items for the same collection.

Estimated useful lives for capital assets are as follows:

	Useful life (in years)		**Useful life (in years)**
Buildings:		Improvements other than buildings:	
Shell	50	Site improvements	20
Service systems	25	Infrastructure	25
Fixed equipment	15	Moveable equipment:	
Remodeling	25	Equipment	3 – 20
Intangibles:			
Software	5 – 10		

(f) Deferred Outflow of Resources

Under hedge accounting, the University has determined that the interest rate swap agreement on the System's bonds payable, as a hedging derivative instrument, is an effective hedge. Accordingly, changes in the fair value of the interest rate swap, since being associated with the related outstanding bonds, is reported as a deferred outflow of resources on the accompanying Statement of Net Position. Additionally, an interest rate swap reassigned to new debt, after a refunding of debt that the swap was previously hedged, normally has an other than zero fair value upon the reassociation. For a swap with a fair value of other than zero upon reassociation with a hedgeable item, the fair value is amortized as an adjustment to interest expense in a systematic manner.

Losses on refundings for the System's bonds are reported as deferred outflow of resources on the accompanying Statement of Net Position. The losses on refundings are amortized over the life of the debt using the straight-line method.

(Continued)

Deferred Outflow of Resources

	Beginning balance	Additions	Deductions	Change in fair value	Ending balance
Interest rate swap agreement that hedges Series 2008 bonds	$ 3,615,172	78,300		(322,730)	3,370,742
Unamortized deferred loss on refunding	3,071,367		(250,732)		2,820,635
Total deferred outflow of resources	$ 6,686,539	78,300	(250,732)	(322,730)	6,191,377

(g) Compensated Absences

Accrued compensated absences for System personnel are charged as an operating expense, using the vested method, based on earned but unused vacation and sick leave days including the System's share of Social Security and Medicare taxes. The estimated outstanding liability at June 30, 2015 was $22,821,109.

(h) Premiums

Premiums for the System's bonds are reported within long-term debt and amortized over the life of the debt issue using the straight-line method.

(i) Net Position

The System's resources are classified into net position categories and reported in the Statement of Net Position. These categories are defined as (a) Net investment in capital assets – capital assets net of accumulated depreciation and related outstanding debt balances attributable to the acquisition, construction, or improvement of those assets, (b) Restricted – net position subject to externally imposed restrictions that can be fulfilled by actions of the System pursuant to those stipulations or that expire by the passage of time, and (c) Unrestricted – net position not subject to externally imposed stipulations but may be designated for specific purposes by action of management or the Board. The System first applies resources included in restricted net position when an expense or outlay is incurred for purposes for which resources in both restricted and unrestricted net positions are available.

(j) Classification of Revenues

The Statement of Revenues, Expenses and Changes in Net Position classifies the System's fiscal year activity as operating and nonoperating. Operating revenues generally result from exchange transactions such as payments received for providing goods and services.

Certain revenue sources that the System relies on for operations including on-behalf payments for fringe benefits and investment income are defined by GASB Statement No. 35 as nonoperating. In addition, transactions related to capital and financing activities are components of net nonoperating revenues.

In fiscal year 2015, $43,987,500 of State appropriations were transferred to the Illinois Hospital Services Fund, which is a special fund established in the State of Illinois Treasury pursuant to the State Finance Act, 30 ILCS 105/6z-30. This fund is owned and operated by the Illinois Department of Healthcare and Family Services (DHFS). It is not part of or a related organization of the University.

Other operating revenues of the System include capitation payments from Health Maintenance Organizations (HMOs) to provide medical services to subscribers, revenues from laboratory services provided to external organizations, cafeteria/gift shop sales and other sources.

(k) Patient Services Revenue

Net patient service revenue is reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Approximately 96% of the System's net patient service revenues were derived from Medicare, Medicaid, Blue Cross and managed care programs for the year ended June 30, 2015.

Accruals for settlements with third-party payors are made based on estimates of amounts to be received or paid under the terms of the respective contracts and related settlement principles and regulations of the federal Medicare program, the Illinois Medicaid program, and the Blue Cross Plan of Illinois. For the year ended June 30, 2015, the Statement of Revenues, Expenses and Changes in Net Position included decreases in net patient service revenue of approximately $2,048,822 related to retroactive settlements and changes in prior year third-party settlement estimates.

The System has agreements with various HMOs to provide medical services to subscribing participants. Under these agreements, the System receives monthly capitation payments based on the number of each HMO's participants, regardless of services actually performed by the System. In addition, the HMOs make fee-for-service payments to the System for certain covered services based upon discounted fee schedules.

The System provides allowances for uncollectible accounts receivable based upon management's best estimate of uncollectible accounts, considering type, age, collection history, and any other factors as considered appropriate.

(l) Charity Care

The System provides care without charge or at amounts at less than its established rates to patients who meet the criteria of its charity care policy. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Consideration for eligibility of charity care is based on the application of the System's charity care policy and includes patient qualification criteria, financial resource criteria and service criteria. The System does not include the unreimbursed cost of providing care to Medicaid and Medicare patients as charity care.

The net cost of charity care provided in fiscal year 2015 was approximately $8,468,000, a reduction of 58% from the prior year, primarily as a result of patients obtaining insurance under the Affordable Care Act. The net cost of charity care is determined by the total charity care cost less any patient related revenue due to the sliding scale payments or other patient specific resources.

(m) Classification of Expenses

The majority of the System's expenses are exchange transactions which GASB defines as operating expenses for financial statement presentation. Nonoperating expenses include transfers of State appropriations and capital financing costs.

(n) On-Behalf Payments for Fringe Benefits

In accordance with GASB Statement No. 24, *Accounting and Financial Reporting for Certain Grants and Other Financial Assistance*, the System reported payments made by the State of Illinois on behalf of the System for contributions to State group insurance and retirement programs, including postemployment benefits, for System employees and its retirees of $198,745,979 for the year ended June 30, 2015. On-behalf payments are classified as nonoperating revenues and the corresponding expenses are reported in fringe benefits of the System as operating expenses.

(o) Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the plan net position of the State Universities Retirement System (SURS) and additions to/deductions from SURS' plan net position has been determined on the same basis as they are reported by SURS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

For the purposes of financial reporting, the State of Illinois and participating employers are considered to be under a special funding situation. A special funding situation is defined as a circumstance in which a non-employer entity is legally responsible for making contributions directly to a pension plan that is used to provide pensions to the employees of another entity or entities and either (1) the amount of the contributions for which the non-employer entity is legally responsible is not dependent upon one or more events unrelated to pensions or (2) the non-employer is the only entity with a legal obligation to make contributions directly to a pension plan. The State of Illinois is considered a non-employer contributing entity. Participating employers are considered employer contributing entities.

(p) Use of Estimates

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

(q) New Accounting Pronouncements

The System adopted the provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which was effective for periods beginning after June 15, 2014. This Statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, and deferred inflows of resources, and expense/expenditures. For defined benefit pensions, this Statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about pensions also are addressed. Implementation of this pronouncement required a change in the notes to the System's financial statements.

The System adopted the provisions of GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*, which was effective for periods beginning after December 15, 2013. This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. This Statement requires disclosures to be made about government combinations and disposals of government operations to enable financial statement users to evaluate the nature and financial effects of those transactions. Implementation of this pronouncement did not impact the System's financial statements.

The System adopted the provisions of GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, which was effective for periods beginning after June 15, 2014. This Statement amends paragraph 137 of Statement 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts. Implementation of this pronouncement required a change in the notes to the System's financial statements.

(2) Cash, Cash Equivalents and Investments

The System has cash and certain investments that are pooled with other University funds for the purpose of securing a greater return on investment and providing an equitable distribution of investment return. Income is distributed based upon average quarterly balances invested in the investment pool.

Nearly all of the University's investments are managed by external professional investment managers, who have full discretion to manage their portfolios subject to investment policy and manager guidelines established by the University, and in the case of mutual funds and other commingled vehicles, in accordance with the applicable prospectus or limited partnership agreement.

The Board follows the State of Illinois Uniform Prudent Management of Institutional Funds Act, 760 ILCS 51/1-11, when managing the University's investments. The Board fulfills its fiduciary responsibility for the management of investments, including endowment farm real estate, by adopting policies to maximize investment return with a prudent level of risk.

The following details the carrying value of the System's cash, cash equivalents, and investments as of June 30, 2015:

U.S. government treasuries	$	6,124,822
U.S. government securities		4,822,782
Commercial paper		24,483,058
Mutual funds – money market		2,863,601
Subtotal		38,294,263
Claim on cash and pooled investments		203,666,734
Total cash, cash equivalents and investments	$	241,960,997

(a) Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. In accordance with its investment policy, the University employs multiple investment managers, of which each has specific maturity assignments related to the operating funds. The funds are structured with different layers of liquidity. Funds expected to be used within one year are invested using the Barclay's Capital 90-Day and Bank of America Merrill Lynch 12-month Treasury Bill Index as performance benchmarks. Core operating funds are invested in longer maturity investments. Core operating funds investment managers' performance benchmarks are the Barclays Capital one-year to three-year Government Bond Index, the Barclays Capital one-year-to-three-year Government Credit Bond Index and the Barclays Capital Intermediate Aggregate Bond Index.

The System's non-pooled investments and maturities as of June 30, 2015 was as follows:

		Maturities (in years)				
		Less than 1	1 – 5	6 – 10	Greater than 10	Total
U.S. government treasuries	$	5,502,326	622,496			6,124,822
U.S. government securities		4,822,782				4,822,782
Commercial paper		24,483,058				24,483,058
Mutual funds - money market		2,863,601				2,863,601
Total cash equivalents and investments	$	37,671,767	622,496	—	—	38,294,263

Claim on cash and on pooled investments represents the System's share of participation in the University's operating internal investment pool. At June 30, 2015, the University's operating internal investment portfolio had an effective duration of 1.4 years. The operating internal investment pool consists of money market funds and other short-term investments (38%), stocks (10%) and long-term investments such as corporate bonds and government securities (52%).

(b) Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University's investment policy requires that the University's short-term operating funds be invested in fixed income securities and short-term instruments (e.g. money markets, certificates of deposits). Fixed income securities shall be rated investment grade or better by one or more nationally recognized statistical rating organizations. Securities not covered by the investment grade standard are allowed if, in the manager's judgment, those instruments are of comparable credit quality. Securities that fall below the stated minimum credit requirements subsequent to initial purchase may be held at the manager's discretion.

The University reports the credit ratings of interest-bearing investments using Standard and Poor's and Moody's ratings. Securities with split ratings or with a different rating assignment are disclosed using the rating indicative of the greatest degree of risk. At June 30, 2015, the University's operating internal investment pool and non-pooled investments primarily consisted of securities with quality ratings of A or better.

(c) Custodial Credit Risk

Custodial credit risk is the risk that in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Exposure to custodial credit risk relates to investment securities that are held by someone other than the University and are not registered in the University's name. The University investment policy does not limit the value of investments that may be held by an outside party. At June 30, 2015, the System's investments and deposits had no custodial credit risk exposure.

(d) Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the University's investment in a single issuer. The University's investment policy provides that the total operating funds portfolio will be broadly diversified across securities in a manner that is consistent with fiduciary standards of diversification. Issuer concentrations are limited to 5% per issuer of the total market value of the portfolio at the time of purchase, or in the case of securitized securities, an individual issuance trust. These concentration limits do not apply to investments in mutual funds, exchange traded funds, or other pooled investment products or obligations of, and issues guaranteed by, the U.S. Treasury, U.S. agencies or U.S. government sponsored enterprises.

As of June 30, 2015, not more than 5% of the University's total investments were invested in securities of any one issuer, excluding securities issued or guaranteed by the U.S. government, mutual funds and external investment pools or other pooled investments.

(e) Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The University's operating fund investments generally are not exposed to foreign currency risk. The University does not have an overarching policy related to foreign currency risk; however, under each investment manager's respective fund agreement, the portfolio's foreign currency exposure may be unhedged or hedged back into U.S. dollars.

The University invests in non-U.S. developed and emerging markets through commingled funds invested in non-U.S. equities, global equities, private equity and absolute return strategies. As these funds are reported in U.S. dollars, both price changes of the underlying securities in local markets and changes to the value of local currencies relative to the U.S. dollar are embedded in investment returns.

(3) Capital Assets

Net interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Net interest of $4,236,195 was capitalized during the year ended June 30, 2015. The capital assets of the System are not pledged to secure outstanding indebtedness of the Board.

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

Capital assets

	Beginning balance	Additions	Retirements	Transfers	Ending balance
Nondepreciable capital assets:					
Land	$ 770,917				770,917
Construction in process	42,009,084	12,202,250		(38,761,644)	15,449,690
Total nondepreciable capital assets	42,780,001	12,202,250		(38,761,644)	16,220,607
Depreciable capital assets:					
Buildings	196,220,063			38,008,997	234,229,060
Leasehold improvements	2,177,211				2,177,211
Equipment	158,827,449	6,412,040	(13,387,172)		151,852,317
Software	33,085,187		(576,278)	752,647	33,261,556
Total depreciable capital assets	390,309,910	6,412,040	(13,963,450)	38,761,644	421,520,144
Less accumulated depreciation:					
Buildings	96,969,270	6,276,942			103,246,212
Leasehold improvements	2,092,522	72,374			2,164,896
Equipment	121,938,377	9,911,352	(13,181,527)		118,668,202
Software	25,966,297	2,352,548	(576,278)		27,742,567
Total accumulated depreciation	246,966,466	18,613,216	(13,757,805)	—	251,821,877
Total depreciable capital assets, net	143,343,444	(12,201,176)	(205,645)	38,761,644	169,698,267
Total capital assets, net	$ 186,123,445	1,074	(205,645)	—	185,918,874

(4) Long-Term Obligations

During fiscal year 1997, Health Services Facilities System Bonds Series 1997B were issued for $25,000,000. Series 1997B Bonds are variable rate bonds, which bear interest at a rate determined weekly and paid monthly.

During fiscal year 2008, the University issued $41,215,000 Variable Rate Demand Health Services Facilities System Revenue Bonds, Series 2008. Proceeds from the bonds funded the redemption of the Variable Rate Demand Health Services Facilities System Revenue Bonds, Series 2007 on July 28, 2008 and paid costs incidental to the issuance of the bonds. The difference between the reacquisition price and net carrying amount of the old debt, loss on refunding, was $4,485,000. This loss is deferred and amortized as a component of interest expense over the remaining life of the old debt or the life of the new debt, whichever is shorter.

During fiscal year 2014, the University issued $70,785,000 Health Services Facilities System Revenue Bonds, Series 2013. Proceeds from the bonds are used to finance the costs of certain construction, renovation and equipment purchases for the Health Services Facilities System and to pay costs incidental to the issuance of the Series 2013 Bonds. The bond premium, $591,216, is deferred and amortized over the remaining life of the issue.

Long-term obligations activity for the year ended June 30, 2015 was as follows:

Long–term obligations

Series	Rate on June 30 outstanding debt	Fiscal year maturity dates	Beginning balance	Additions	Deductions	Ending balance	Current portion
Bonds payable:							
1997B	Variable	2016 – 2027	$ 15,300,000		(900,000)	14,400,000	1,000,000
2008	Variable	2016 – 2027	35,885,000		(2,220,000)	33,665,000	2,240,000
2013	5% to 6.25%	2028 – 2043	70,785,000			70,785,000	
			121,970,000	—	(3,120,000)	118,850,000	3,240,000
Unamortized premium			574,440		(20,334)	554,106	20,334
Total bonds payable			122,544,440	—	(3,140,334)	119,404,106	3,260,334
Other obligations			7,530,309		(2,090,883)	5,439,426	2,122,250
Total long–term debt			130,074,749	—	(5,231,217)	124,843,532	5,382,584
Compensated absences			23,030,949	1,843,373	(2,053,213)	22,821,109	2,277,559
Total long–term obligations			$ 153,105,698	1,843,373	(7,284,430)	147,664,641	7,660,143

The bonds do not constitute obligations of the State of Illinois. Bond principal and interest payments are funded from revenues pledged from (a) System net revenues, principally consisting of all charges, income and revenues received from the continued use and operation of the System, excluding depreciation charges and transfers, (b) Medical Service Plan (MSP) revenues net of bad debt expense and (c) College of Medicine tuition revenue. These revenues for the year ended June 30, 2015 are as follows:

System net revenues	$ 21,470,913
Adjusted MSP revenues	189,932,368
College of Medicine student tuition	52,835,354
Total	$ 264,238,635

The table below shows the amount of revenues pledged for future principal and interest payments on the bonds:

Pledged revenues

Bond issue(s)	Purpose	Source of revenue pledged	Future revenues pledged[1]	Term of commitment	Debt service to pledged revenues (current year)
Series 1997B, 2008 and 2013	Additions to System and Refunding	Net System revenue, MSP revenue net of bad debt expense, College of Medicine net tuition revenue	$ 217,207,658	2043	3.24%

1 Total future principal and interest payments on debt

The resolution authorizing the University of Illinois Health Services Facilities System Revenue Bonds provides for the establishment of separate funds as follows: Revenue Fund, Project Fund, Repair and Replacement Reserve, Equipment Reserve, Bond and Interest Sinking Fund and Development Reserve. All income and revenues received from the continued use and operation of the System, as provided for by the Bond Resolution, are to be deposited in the Revenue Fund and used to pay necessary operation and maintenance expenses of the System. The Bond Resolution also requires transfers to funds as follows:

Project Fund – at the discretion of the University Comptroller, amounts not needed to complete construction and renovation projects specified in the Bond Resolution are required to be transferred either to the Repair and Replacement Reserve or to the Bond and Interest Sinking Fund.

Repair and Replacement Reserve – an amount calculated as specified in the Bond Resolution to provide for the cost of unusual maintenance and repairs.

Equipment Reserve – an amount approved by the Board for the acquisition of movable equipment to be installed in the facilities constituting the System. The reserve may not exceed 20% of the book value of the movable equipment of the System.

Bond and Interest Sinking Fund – amounts transferred into the Bond and Interest Sinking Fund sufficient to pay principal and interest as it becomes due on the outstanding bonds.

Development Reserve – an amount approved by the Board for System development. No transfers were authorized by the Board during the year ended June 30, 2015, and there were no balances in the reserve at June 30, 2015.

The System made all required transfers for the year ended June 30, 2015.

After fulfillment of the provisions described above, the surplus, if any, remaining in the Revenue Fund may be used at the Board's option (a) to redeem bonds of the System which are subject to early redemption, (b) to improve or add facilities to the System, or (c) for any other lawful purpose.

Assets restricted by Bond Resolution were held for the following purposes at June 30, 2015:

Restricted assets:		
Cash and investments	$	52,030,967
Purpose:		
Capital projects, bond projects	$	38,233,942
Repair and replacement reserve		12,636,514
Bond and interest sinking fund		1,160,511
Total assets limited as to use		52,030,967
Less amounts required for current liabilities		(1,155,693)
Total for long-term use	$	50,875,274

(a) Health Services Facilities System Variable Rate Debt and Interest Rate Swap Agreement

Demand Provisions

The System's bonds mature serially through October 2026. These bonds have variable interest rates that are adjusted periodically (i.e., daily, weekly, or monthly), generally with interest paid at the beginning of each month. The bonds are subject to purchase on the demand of the holder at a price equal to principal plus accrued interest on seven days' notice and delivery to the University's several remarketing agents. The University pays the remarketing agent fees on the outstanding bond balance. If the remarketing agent is unable to resell any bonds that are "put" to the agent, the University has a standby bond purchase agreement with a liquidity facility entity. The University has several such agreements, with the fees on the Bond Purchase Commitment (formula based on outstanding bonds plus pro forma interest). The University, in the event a liquidity facility is utilized, has reimbursement agreements with different financial entities. Generally, the payback period, in which the initial payment is due 366 days after the agreement takes effect, is five to seven years, at an interest rate initially set at slightly above prime or the federal funds rate.

The required future interest payments for these variable rate bonds have been calculated using the current interest rate, based upon short-term tax-exempt rates, or the synthetic fixed rate, as illustrated in the table below:

Variable rate bonds at June 30, 2015

Bond issues	Interest rate at June 30, 2015	Remarketing agent	Remarketing fee	Liquidity facility Bank	Liquidity facility Expiration	Liquidity facility Insured by	Liquidity facility Fee
HSFS, Series 1997B	0.07%	JPMorgan Securities	0.070%	Wells Fargo	May 30, 2019	Letter of Credit	0.32%
HSFS, Series 2008	0.06	Goldman Sachs	0.070	Wells Fargo	May 30, 2019	Letter of Credit	0.32

Interest Rate Swap Agreement

In April 2007, the University entered into a variable-to-fixed interest rate swap agreement with Lehman Brothers Commercial Bank (LBCB). The purpose of this interest rate swap was to hedge variable rate demand Health Services Facilities System revenue refunding bonds issued in July 2007. The objective of this swap was to effectively change the System's variable interest rate on the bonds to a synthetic fixed rate. The notional amount of the interest rate swap was $40,875,000. No cash was paid or received when the original swap agreements were entered into. In accordance with the swap agreement, the University makes monthly payments to the counterparty equal to 3.534% times the notional amount and receives monthly payments from the counterparty equal to 68% of one-month London Interbank Offered Rate (LIBOR), which commenced October 1, 2007. This interest rate swap agreement with LBCB transferred to the Series 2008 bonds in July 2008. A total of $275,000 of the HSFS Series 2008 bond is not covered by this agreement.

In December 2008, the University entered into a novation agreement, which terminated the swap with LBCB and entered into a new interest rate swap agreement with Loop Financial Products I LLC (Loop) with the same terms and conditions that were present in the April 2007 agreement. In December 2008, Loop officially became the new counterparty on the interest rate swap agreement.

The University engaged a third-party consultant to calculate the "mark to market" or "market value" of the swap transaction. On June 30, 2015, the mark to market value of the swap was $(4,251,511).

Credit Risk – As of June 30, 2015, the University was not exposed to credit risk because the swap had a negative fair value. If interest rates change and the fair value of the swap became positive, the University would be exposed to credit risk in the amount of the derivative's fair value. The counterparty may have to post collateral in the University's favor in certain conditions, and the University would never be required to post collateral in the counterparty's favor.

Interest Rate Risk – During fiscal year 2015, low interest rates exposed the University to interest rate risk, which adversely affected the fair value of the swap agreement.

Termination Risk – The swap is scheduled to terminate in October 2026. The University has the option to terminate the swap early. The University or the counterparties may terminate a swap if the other party fails to perform under the terms of the contract. The University may terminate a swap if both credit ratings of the counterparties fall below BBB+ as issued by Standard & Poor's and Baa1 as issued by Moody's Investors Service. As of June 30, 2015, the counterparty (Loop) credit rating by Standard & Poor's was BBB+ and by Moody's Investors Service was A3.

If a swap is terminated, the variable-rate bonds would no longer carry a synthetic fixed interest rate. In addition, if at the time of termination, a swap has a negative fair value, the University would be liable to the counterparties for a payment equal to the swap's fair value.

Basis Risk – The swap exposes the University to basis risk should the relationship between LIBOR and the variable weekly rate determined by remarketing agents change, changing the synthetic rate on the bonds. If a change occurs that results in the difference in rates widening, the expected cost savings may not be realized.

Other Risks – Since the swap agreement extends to the maturity of the related bond, it does not expose the University to rollover risk. In addition, the University is not exposed to foreign currency risk associated with this swap agreement. The University is not exposed to market access risk as of June 30, 2015. However, if the University decides to issue refunding bonds and credit is more costly at that time, it could be exposed to market access risk.

(b) Debt Service Requirements

Future debt service requirements for the Series 1997B, 2008 and 2013 Bonds at June 30, 2015 are as follows:

	Principal	Interest
2016	$ 3,240,000	5,394,010
2017	3,365,000	5,311,894
2018	3,485,000	5,225,483
2019	3,620,000	5,136,789
2020	3,755,000	5,044,478
2021 - 2025	21,030,000	23,721,650
2026 - 2030	18,220,000	20,800,492
2031 - 2035	18,300,000	16,261,712
2036 - 2040	24,855,000	9,707,350
2041 - 2043	18,980,000	1,753,800
Total debt service	118,850,000	$ 98,357,658
Unamortized premium	554,106	
Total bonds payable	$ 119,404,106	

The required debt service for the variable rate Series 1997B and 2008 Bonds has been calculated using the current interest rate of 0.07% and 0.06%, respectively, over the remaining life of the bonds.

Using the actual rate in effect as of June 30, 2015 (0.06% for Series 2008), debt service requirements of the variable rate debt and net swap payments, assuming current interest rates remain the same for their term, were as follows. As rates vary, variable-rate bond interest payments and net swap payments will also vary.

Health Services Facilities System Revenue Bonds, Series 2008
Variable-Rate Debt Service Requirements

		Variable rate bonds		Interest rate	
		Principal	Interest	swaps, net	Total
2016	$	2,240,000	20,199	1,107,657	3,367,856
2017		2,365,000	18,855	1,027,590	3,411,445
2018		2,485,000	17,436	943,297	3,445,733
2019		2,520,000	15,945	856,838	3,392,783
2020		2,655,000	14,433	766,808	3,436,241
2021 - 2025		14,730,000	47,283	2,371,019	17,148,302
2026 - 2027		6,670,000	6,027	190,139	6,866,166
Total	$	33,665,000	140,178	7,263,348	41,068,526

Other obligations consist of third-party financing arrangements for equipment, which have maturity dates from 2016 through 2019 and interest rates ranging from 1.26% to 6.10%.

As of June 30, 2015, future minimum payments under other obligations are as follows:

		Principal	Interest
2016	$	2,122,250	88,438
2017		1,976,042	51,570
2018		1,144,354	19,885
2019		196,780	3,236
Total minimum payments – other obligations	$	5,439,426	163,129

(5) Operating Leases

The System leases various real property and equipment under operating lease agreements, including leases renewed on an annual basis. Total rental expense under these agreements was $1,452,019 for the year ended June 30, 2015.

As of June 30, 2015, future minimum payments under operating leases are as follows:

2016	$	113,265
2017		116,333
2018		118,140
2019		101,070
Total minimum payments – operating leases	$	448,808

(6) Patient Accounts Receivable, Accounts Payable and Other Current Liabilities

Patient accounts receivable and accounts payable and other current liabilities as of June 30, 2015, reported as current assets and liabilities, consisted of the following amounts:

Patient accounts receivable:		
Patients and their insurance carriers	$	204,196,855
Medicare		56,077,186
Medicaid		66,487,194
Medicaid Managed Care		181,258,210
Total		508,019,445
Less allowance for uncollectible accounts		(380,075,924)
Total patient accounts receivable, net	$	127,943,521
Accounts payable and other current liabilities:		
Payable to employees	$	17,842,121
Payable to suppliers and service providers		31,900,156
Payable to health plans and for workers' compensation claims		3,203,690
Estimated third-party settlements		62,319,695
Total accounts payable and other current liabilities	$	115,265,662

The System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2015 was as follows:

Medicare	11.0%
Medicaid	13.1%
HMO/PPO	29.5%
Medicaid Managed Care	35.7%
Commercial	10.4%
Self-pay and other	0.3%
	100.0%

(7) Net Patient Service Revenues

The Hospital has agreements with third-party payers that provide for payments to the Hospital at established program rates, as defined, for rendering services to program beneficiaries. The Hospital provides contractual allowances on a current basis for the differences between charges for services rendered and the expected payments under these programs. The patient revenues from third-party payer programs, less the contractual allowances and provision for uncollectible accounts for fiscal year 2015, were as follows:

Medicaid	$	381,333,698
Medicare		462,086,776
HMO/PPO		642,414,025
Medicaid Managed Care		455,027,544
Commercial		57,915,044
Self-pay and other		71,189,115
Total gross revenue		2,069,966,202
Less:		
Contractual allowances		(1,461,485,970)
Provision for uncollectible accounts		(38,365,504)
Net patient revenue	$	570,114,728

A summary of the payment arrangements with major third-party payers follows:

Medicare – Inpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient acute care services are paid at prospectively determined rates that are based on the patients' acuity. Other inpatient non-acute services are paid based on their prospectively determined methodologies. Substantially all outpatient services are subject to a prospective payment system. Under this system, payments to the Hospital are based on a predetermined package rate based on services provided to patients. The Hospital is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. At June 30, 2015, all Medicare settlements for 2010 through 2015 are subject to audit and retroactive adjustment.

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates-per-diem. Outpatient services rendered to program beneficiaries are reimbursed at prospectively determined rates – rate per Enhanced Ambulatory Procedure Grouping or a fee screen. Medicaid payment methodologies and rates for services are subject to change based on the amount of funding available to the State of Illinois Medicaid Program, and any such changes could have a significant effect on the Hospital's revenues.

HMO/PPO and Medicaid Managed Care - System has payment agreements with certain commercial insurance carriers, (HMOs) and preferred provider organizations (PPOs). The basis for payment under these agreements includes prospectively determined rates-per-discharge, discounts from established charges, prospectively determined daily rates and capitated per-member per-month rates.

(8) Retirement and Postemployment Benefits

(a) Retirement Benefits

General Information about the Pension Plan

Plan Description: The University contributes to the State Universities Retirement System of Illinois, a cost-sharing multiple-employer defined benefit plan with a special funding situation whereby the State makes substantially all actuarially determined required contributions on behalf of the participating employers. SURS was established July 21, 1941 to provide retirement annuities and other benefits for staff members and employees of State universities, certain affiliated organizations, and certain other State educational and scientific agencies and for survivors, dependents and other beneficiaries of such employees. SURS is considered a component unit of the State's financial reporting entity and is included in the State's financial reports as a pension trust fund. SURS is governed by Section 5/15, Chapter 40, of the *Illinois Compiled Statutes*. SURS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by accessing the website at www.surs.org.

Benefits Provided: A traditional benefit plan was established in 1941. Public Act 90-0448 enacted effective January 1, 1998, established an alternative defined benefit program known as the portable benefit package. The traditional and portable plan Tier 1 refers to members that began participation prior to January 1, 2011. Public Act 96-0889 revised the traditional and portable benefit plans for members who begin participation on or after January 1, 2011, and who do not have eligible Illinois reciprocal system services. The revised plan is referred to as Tier 2. New employees are allowed 6 months after their date of hire to make an irrevocable election. A summary of the benefit provisions as of June 30, 2014 can be found in the SURS' comprehensive annual financial report (CAFR) Notes to the Financial Statements.

Eligible employees must participate upon initial employment. Employees are ineligible to participate if (a) employed after having attained age 68; (b) employed less than 50% of full time; or (c) employed less than full time and attending classes with an employer. Of those University employees ineligible to participate, the majority are students at the University.

Contributions: The State of Illinois is primarily responsible for funding the System on behalf of the individual employers at an actuarially determined amount. Public Act 88-0593 provides a Statutory Funding Plan consisting of two parts: (i) a ramp-up period from 1996 to 2010 and (ii) a period of contributions equal to a level percentage of the payroll of active members of the System to reach 90% of the total Actuarial Accrued Liability by the end of Fiscal Year 2045. Employer contributions from "trust, federal, and other funds" are provided under Section 15-155(b) of the Illinois Pension Code and require employers to pay contributions which are sufficient to cover the accruing normal costs on behalf of applicable employees. The employer normal cost for fiscal year 2014 and 2015 respectively, was 11.91% and 11.71% of employees payroll. The normal cost is equal to the value of current year's pension benefit and does not include any allocation for past unfunded liability or interest on the unfunded liability. Plan members are required to contribute 8.0% of their annual covered salary. The contribution requirements of plan members and employers are established and may be amended by the Illinois General Assembly.

Participating employers make contributions toward separately financed specific liabilities under Section 15.139.5(e) of the Illinois Pension Code (relating to contributions payable due to the employment of "affected annuitants" or specific return to work annuitants) and Section 15.155(g) (relating to contributions payable due to earning increases exceeding 6% during the final rate of earnings period).

Pension Liabilities, Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

Net Pension Liability: At June 30, 2014, SURS reported a net pension liability (NPL) of $21,790,983,000. The net pension liability was measured as of June 30, 2013.

Employer Proportionate Share of Net Pension Liability: The amount of the proportionate share of the net pension liability to be recognized for the System is $0. The proportionate share of the State's net pension liability associated with the System is $1,546,893,194. This amount should not be recognized in the financial statement. The net pension liability was measured as of June 30, 2014, and the total pension used to calculate the net pension liability was determined based on the June 30, 2013 actuarial valuation rolled forward. The basis of allocation used in the proportionate share of net pension liability is the actual reported pensionable earnings made to SURS during fiscal year 2014.

Pension Expense: At June 30, 2014 SURS reported a collective net pension expense of $1,650,338,000.

Employer Proportionate Share of Pension Expense: The employer proportionate share of collective pension expense should be recognized similarly to on-behalf payments as both revenue and matching expenditure in the financial statements. The basis of allocation used in the proportionate share of collective pension expense is the actual reported pensionable contributions made to SURS during fiscal year 2014. As a result, the University recognized on-behalf revenue and pension expense of $681,300,000 for fiscal year ended June 30, 2015, of which $117,154,000 was related to the System.

Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions: Deferred Outflows of resources are the consumption of net position by SURS that is applicable to future reporting periods.

SURS Collective Deferred Outflows and Deferred Inflows of Resources by Sources
(nearest thousand)

		Deferred Outflows of Resources	Deferred Inflows of Resources
Changes in assumption	$	88,941	
Net difference between projected and actual earnings on pension plan investments			1,271,106
Total	$	88,941	1,271,106

Assumptions and Other Inputs

Actuarial assumptions: The actuarial assumptions used in the June 30, 2014 valuation were based on the results of an actuarial experience study for the period June 30, 2006 – 2010 and an economic study completed June 2014. The total pension liability in the June 30, 2014 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.75 percent
Salary increases	3.75 to 12.00 percent, including inflation
Investment rate of return	7.25 percent beginning with the actuarial valuation as of June 30, 2014

Mortality rates were based on the RP2000 Combined Mortality Table, projected with Scale AA to 2017, sex-distinct, with rates multiplied by 0.80 for males and 0.85 for females.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return were adopted by the plan's trustees after considering input from the plan's investment consultant(s) and actuary(s). For each major asset class that is included in the pension plan's target asset allocation as of June 30, 2014, these best estimates are summarized in the following table:

Asset Class	**Target Allocation**	**Long-Term Expected Real Rate of Return**
U.S. Equity	31%	7.65%
Private Equity	6%	8.65%
Non-U.S. Equity	21%	7.85%
Global Equity	8%	7.90%
Fixed Income	19%	2.50%
Treasury-Inflation Protected Securities	4%	2.30%
Real Estate	6%	6.20%
REITS	4%	6.20%
Opportunity Fund	1%	2.50%
Total	100%	5.00%
Inflation		2.75%
Expected Geometrical Normal Return		**7.75%**

Discount Rate: A single discount rate of 7.090% was used to measure the total pension liability. This single discount rate was based on an expected rate of return on pension plan investments of 7.250% and a municipal bond rate of 4.290% (based on the weekly rate closest to but not later than the measurement date of the 20-Year Bond Buyer Index as published by the Federal Reserve). The projection of cash flows used to determine this single discount rate were the amounts of contributions attributable to current plan members and assumed that plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the statutory contribution rates under SURS' funding policy. Based on these assumptions, the pension plan's fiduciary net position and future contributions were sufficient to finance the benefit payments through the year 2065. As a result, the long-term expected rate of return on pension plan investments was applied to projected benefit payments through the year 2065, and the municipal bond rate was applied to all benefit payments after that date.

Sensitivity of the SURS' Net Pension Liability to Changes in the Discount Rate: Regarding the sensitivity of the net pension liability to changes in the single discount rate, the following presents the plan's net pension liability, calculated using a single discount rate of 7.09%, as well as what the plan's net pension liability would be if it were calculated using a single discount rate that is 1-percentage-point lower or 1-percentage-point higher:

1% Decrease 6.09%	**Current Single Discount Rate Assumption 7.09%**	**1% Increase 8.09%**
$26,583,701,134	$21,790,983,139	$17,796,570,836

Additional information regarding the SURS basic financial statements including the Plan Net Position can be found in the SURS comprehensive annual financial report by accessing the website at www.SURS.org.

(b) *Postemployment Benefits*

The State Employees Group Insurance Act of 1971 (Act), as amended, authorizes the State to provide health, dental, vision and life insurance benefits for certain retirees and their dependents. Substantially all State and university component unit employees become eligible for these other postemployment benefits (OPEB) if they eventually become annuitants of one of the State sponsored pension plans. The Department of Central Management Services administers these benefits for annuitants with the assistance of the State's sponsored pension plans. The portions of the Act related to OPEB establish a cost-sharing multiple-employer defined-benefit OPEB plan (plan) with a special funding situation in which the State funds substantially all nonparticipant contributions. The plan does not issue a stand-alone financial report but is included as a part of the State's financial statements. A copy of the financial statements of the State can be obtained at www.ioc.state.il.us.

The health, dental and vision benefits provided to and contribution amounts required from annuitants are the result of collective bargaining between the State and various unions that represent the State and the university employees in accordance with limitations established in the Act. Therefore, the benefits provided and contribution amounts are subject to periodic change. The Act requires the State to provide life insurance benefits for annuitants equal to their annual salary as of the last day of employment until age 60, at which time the benefit amount becomes $5,000.

The State makes substantially all of the contributions for OPEB on behalf of the State universities. Since the State contributes substantially all of the employer contributions, the single-employer provisions of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, have been followed for reporting the plan. The State is not required to and does not fund the plan other than the pay-as-you-go amount necessary to provide the current benefits.

(9) Related-Party Transactions

The University charged the System for administrative and other services totaling $21,972,364 in fiscal year 2015, primarily based upon the gross expenditures and debt service transfers of various operations of the System. These charges represent a portion of the estimated administrative and other service costs incurred by the University in support of the System. An additional $21,488,592 was paid by the University on behalf of the System for salaries and utility costs for the year ended June 30, 2015, in exchange for System services and facilities provided, and are recognized as operating expenses (salaries and general) and operating revenues.

The System provides funds to the College of Medicine to support programmatic initiatives that benefit the System's strategic goals and to pay for salaries of physicians and staff in the College of Medicine who serve as medical directors and physician leaders of the System under various agreements. During fiscal year 2015, approximately $37 million was recognized in supplies and general expenses by the System under these agreements.

The System contracts with the University's College of Pharmacy to provide certain pharmacy services related to the Federal drug discount program under Section 340b of the Public Health Service Act, under which the System is a covered entity and purchases drugs for dispensing to eligible outpatients. During fiscal year 2015, the System paid approximately $9.2 million to the College of Pharmacy for these services.

Most healthcare services rendered by physicians at the University are charged, billed and collected through the MSP. For ambulatory care services, there is a charge for both a professional and technical component. The System bills and collects on behalf of the MSP for the professional component of ambulatory care services. Based on the underlying agreements between the MSP and the University, the System remits funds collected to the MSP. Total MSP remittances from the System for the year ended June 30, 2015 relating to the billing and collection of physician fees and the delivery of ambulatory care were $27,049,690.

During 2015, various departments within the College of Medicine agreed to reimburse the System for a portion of the expenses related to the resident and fellowship training program. This reimbursement, which totaled $2,517,516, has been reflected in the financial statements as a reduction of the related expenses.

(10) Commitments and Contingencies

(a) Commitments

At June 30, 2015, the System had commitments on various construction projects and contracts for repairs and renovation of health services facilities of $5,290,712.

(b) Contingencies

The University (including the System) is involved in regulatory audits arising in the normal course of business.

On June 8, 2007, a notice was received from the Office of Inspector General (OIG) on behalf of the Illinois Department of Healthcare and Family Services (IDHFS) indicating that the University received an overpayment of $14.8 million covering the period May 1, 2004 through April 30, 2006 on behalf of Medicaid patients, of which $10 million and $4.8 million related to the University's College of Pharmacy and the System, respectively. University management is in the process of contesting this overpayment. During fiscal year 2010, the University submitted additional documentation and evidence of its positions. On September 29, 2011, the OIG on behalf of the IDHFS contacted the University to request its settlement offer to resolve the audit. The University intends to pursue settlement discussion with OIG and IDHFS with a view toward resolution of the matter. It is estimated that the System's established liability including a provision for subsequent audits totaling $8.5 million remains sufficient to cover the probable outcome of the audits and has been included in estimated third-party settlements payable within the accompanying Statement of Net Position as of June 30, 2015.

In 2015 and 2014, the System received notices from Medicare requiring that it provide documentation for certain claims as part of the Recovery Audit Contractor (RAC) program. The System has responded to these requests. Review of claims through the RAC program may result in a liability to Medicare which could have a material impact on the System's net patient service revenues.

The System is subject to program compliance audits from the Health Resources and Services Administration (HRSA) of the US Department of Health and Human Services (USDHHS) in relation to the System's participation as a covered entity in the Federal drug discount program under Section 340b of the Public Health Service Act.

The University (including the System) is a defendant in a number of legal actions primarily related to medical malpractice. These legal actions have been considered in estimating the University's accrued self-insurance liability, which covers hospital and medical professional/general liability; estimated general and contractual liability; and workers' compensation liability. At June 30, 2015, the University's total accrued self-insurance liability was $243,959,743.

The University's accrued self-insurance liability includes $175,838,584 at June 30, 2015, for the most probable and reasonably estimable ultimate cost for medical malpractice liabilities. Ultimate cost consists of amounts estimated by the University's risk management division and actuaries for asserted claims, unasserted claims arising from reported incidents, expected litigation expenses and amounts determined by actuaries using relevant industry data and System specific data to cover projected losses for claims incurred but not yet reported. The System contributes to the University's self-insurance reserve through annual assessments. Therefore, no liability related to medical malpractice claims is included in the System's financial statements, but the entire self-insurance liability is reflected in the University's financial statements.

(11) Subsequent Events

During October 2015, the HRSA of the USDHHS conducted a program compliance audit related to the System's participation in the Federal Drug discount program under Section 340b of the Public Health Service Act as a covered entity. As of December 23, 2015, the issuance date of these financial statements, the results of this audit have not been received by the System.

Required Supplementary Information

Schedule of University of Illinois Health Services Facilities System Proportionate Share of the Net Pension Liability	Fiscal Year 2014
(a) Proportion Percentage of the Collective Net Pension Liability	0%
(b) Proportion Amount of the Collective Net Pension Liability	$0
(c) Portion of Nonemployer Contributing Entities' Total Proportion of Collective Net Pension Liability associated with Employer	$1,546,893,194
Total (b) + (c)	$1,546,893,194
Employer Covered-employee payroll	$299,799,478
Proportion of Collective Net Pension Liability associated With Employer as a percentage of covered-employee payroll	515.98%

Schedule of Contributions	
SURS Plan Net Position as a Percentage of Total Pension Liability	44.39%

Changes of benefit terms. There were no benefit changes recognized in the Total Pension Liability as of June 30, 2014.

Changes of assumptions. In accordance with Illinois Compiled Statutes, an actuarial review is to be performed at least once every five years to determine the reasonableness of actuarial assumptions regarding the retirement, disability, mortality, turnover, interest and salary of the members and benefit recipients of SURS. An experience review for the years June 30, 2010 to June 30, 2014 was performed in February 2015, resulting in the adoption of new assumptions as of June 30, 2015. There are no changes of assumptions that affect measurement of the total collective pension liability since the prior measurement date.

*Note: The System implemented GASB No. 68 in fiscal year 2015. The information above is presented for as many years as available. The Schedule is intended to show information for 10 years.