UNIVERSITY OF MICHIGAN

2011 Financial Report

On the cover: The North Quadrangle Residential and Academic Complex, a unique combination of living and learning environments, is the university's first new residence hall since 1967. Photo by Philip Dattilo.

Additional photos by Mark Clague, Philip Dattilo, Daryl Marshke, Ian Tadashi Moore, and U-M Photo Services (Scott Galvin, Paul Jaronski, Lin Jones, Scott Soderberg, Austin Thomason, and Martin Vloet).

Table of Contents

Letter from the President	3
Report from the Chief Financial Officer	5
Report from the Vice President for Development	11
Student Profile	15
Leadership & Service	17
Creativity & Innovation	21
Excellence & Achievement	25
Major Projects	29
Management Responsibility for Financial Statements	32
Report of Independent Auditors	33
Management's Discussion and Analysis	34
Financial Statements	51
Officers and Staff	80

Letter
FROM THE PRESIDENT

Mary Sue Coleman

Welcome to the story of the University of Michigan's financial performance this year, in the pages of this annual report. As you read about the university's strong financial position, you will see a vibrant and forward-moving research university with a deep public ethos and a laser-focus on academic excellence. Michigan's prudent financial management and budget discipline, including significant cost-cutting and reallocation from lower to highest priorities, has enabled the institution to remain extremely competitive and operate with stability, even as we continue to wrestle with the country's economic downturn.

The state's economic condition has resulted in significant reductions in the university's appropriation since 2002. However, we have worked together to focus on our priorities: academic quality and continued access to a Michigan education. Philanthropy, too, has played a key role in advancing Michigan's excellence and providing additional scholarship funding for students. Over the past several years, the university has maintained modest increases in tuition and substantially increased need-based financial aid for our students.

We are focused on building and expanding key institutional strengths as we look forward to the university's bicentennial in 2017:

- **Academic Excellence:** The university enjoys remarkable academic breadth and depth with 95 academic programs ranked in the top ten nationally. With more than $1.2 billion in research expenditures in 2010–11, U-M is among the largest research universities in the United States. This year we completed a $30 million, five-year faculty recruitment program to attract 100 junior faculty members with an interest and track record in interdisciplinary scholarship, one of the hallmarks of our academic community. With all of these resources and expertise, we work to deliver a truly transformative undergraduate educational experience, preparing our students for careers in a volatile and quickly changing marketplace.

■ **Public Ethos:** The University of Michigan has a deep commitment to the public good, both in the state of Michigan and around the world. This institution holds a special place in U.S. higher education because of its intersection of academic excellence and public ethos, and that culture permeates our community and defines it at its core. I often say that our students and our faculty develop their intellectual assets with the deeply held belief that they can and must make a powerful difference in the world around them. Our service orientation is perhaps nowhere more evident than in the university's seminal role in the development of the Peace Corps. When President John F. Kennedy stood on the steps of the Michigan Union and challenged our students to do something for the good of the world, U-M stepped up to the challenge, and continues to do so today.

■ **Entrepreneurship, Innovation, and Business Engagement:** We have built a powerful entrepreneurial ecosystem on our campus, with more than 5,000 students participating in entrepreneurial activities this past year. In 2010–11, U-M's student business plan competition called "1,000 Pitches" garnered three times that, with more than 3,000 student entries for new business ideas. All across our campus, from the Ross School of Business' longstanding Zell Lurie Institute for Entrepreneurial Studies and the Center for Entrepreneurship in the College of Engineering to the Medical School and Michigan Law, students and faculty are creating an entrepreneurial network leading to innovation and an increased commercialization of technologies. With the university's successful Business Engagement Center, we work to develop mutually beneficial relationships with businesses looking for research expertise, student support, and workforce talent.

■ **Sustainability:** Michigan is a leader among its higher education peers for sustainability research, teaching, and campus operations. In the last 18 months alone, the university has received federal funding for three national research centers focusing on Great Lakes climate change, solar energy, and clean vehicles, and our academic programs offer more than 640 courses across campus with content in sustainability. The university's own campus operations are modeling our commitment, in construction of LEED-certified buildings, in recycling, and in our highly successful Planet Blue energy conservation program, which annually saves $4 million across campus.

■ **Global Engagement:** The University of Michigan hosts one of the largest international student populations of any U.S. university, with almost 6,000 students studying or working on campus. Our ties to global communities are strong and deep, from teams of researchers and students working in Ghana and Liberia to joint institutes with Shanghai Jiao Tong University and Peking University. U-M's relationships with China reach as far back as President James B. Angell, who in 1880 took a one-year leave of absence from the university to serve as U.S. minister to China. In 2011–12 we will celebrate the 50th anniversary of the Center for Chinese Studies—among the most well-known and respected China studies programs in American higher education.

■ **Arts and Culture:** Across our campus, cultural and arts activities deepen the educational experience as well as the quality of life for faculty, staff, students, and the community. The U-M Symphony Band experienced this intimately with a broad tour of China, where students performed in six cities, experienced different cultures, and saw how music is a universal language. Creativity and the arts are integral to developing critical thinking skills, and we provide students with numerous avenues to explore. We offer the Creative Process, an intensive course where students use sound, motion, visual images, and language for expression and decisions. The holdings and collections of our 15 libraries and museums are gateways to new knowledge and diverse cultures.

The University of Michigan continues to be a place of bold ideas and actions, and a point of pride for our state and nation. We believe in the power of knowledge, the joy of discovery, and the special compact we embrace to better our state and world. And we look forward to a future filled with novel ideas, transformative research, and public service that improve our world.

Sincerely,

Mary Sue Coleman

Mary Sue Coleman
President

Report
FROM THE CHIEF FINANCIAL OFFICER

Timothy P. Slottow

The University of Michigan remains financially healthy, due in large part to the institution's 42,000 faculty and staff who maintain an unyielding focus on the university's core missions as they strive to find new ways to contain costs, maximize resources, and increase efficiencies. As a result of their dedication in building on our strong foundation and tradition of excellence, we continue to have the resources to make strategic investments in the facilities, programs, and people that make our institution one of the best public research universities in the world.

The university continues to maintain the highest credit ratings from both Standard & Poor's (AAA) and Moody's Investor Services (Aaa). These ratings are important indicators of the institution's strong financial health and outlook and are notable in light of the tumultuous economy we've faced for a number of years. U-M is one of only three public universities in the country to maintain these ratings—the highest possible—from both of these agencies.

A disciplined budget approach carefully balances the institution's need to remain competitive against a challenging economic environment. Over the years, we've been committed to innovative cost containment strategies, successful fundraising efforts, moderate tuition increases, and relentless protection and enhancement of the world-class quality of the institution's research, teaching, and clinical care. The success of this commitment, combined with our long-term investment strategy, ensures a strong future for the university.

The university's total net assets (assets less liabilities) increased by $1.6 billion in FY 2011 to $10.9 billion. This increase is primarily due to net investment income, which totaled $1.6 billion. In the following sections, I will discuss the important contributors to the university's overall financial health to provide context to the accompanying financial statements.

Revenue Diversification

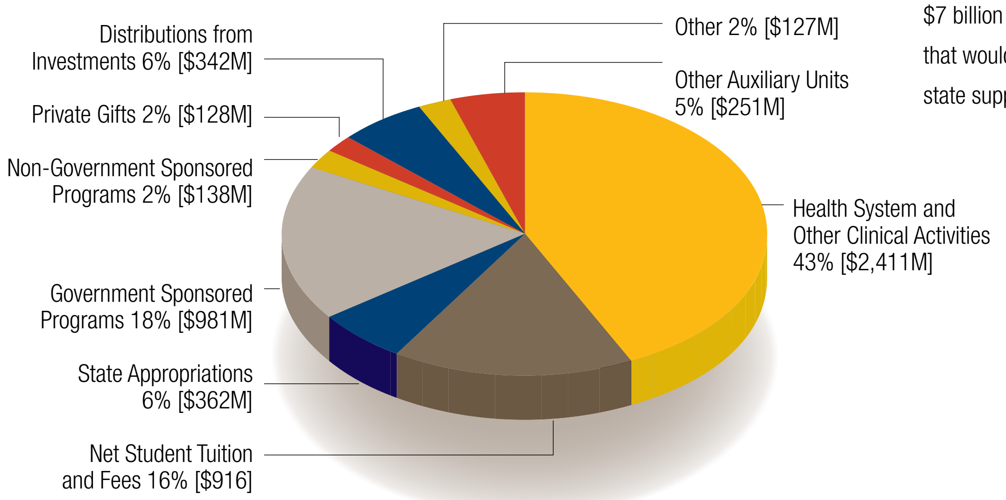
Revenue diversification has long been an important strategy for the university to achieve financial stability in light of unpredictable economic cycles. In the 1960s, for example, nearly 80 percent of the university's general fund revenues came from state appropriations, compared to the projected 17 percent in the FY 2012 general fund budget. The current mix of revenue can be seen on the charts below, which show the FY 2011 operating revenue sources with and without the Health System and other clinical activities.

The General Fund Operating Budget Challenge

Although support from the state of Michigan remains a key element in the university's strength, state appropriations have declined significantly since FY 2002. Base state appropriations have decreased from $416 million in FY 2002 to $362 million in FY 2011, a decrease of $54 million, or 13 percent. In contrast, if appropriations had grown at the level of the Consumer Price Index for Detroit, our state appropriations would have been $127 million higher in FY 2011. To put the state's current support in perspective, it is useful to consider that in a stable economic environment, it would take an additional endowment of approximately $7 billion to generate a revenue stream that would equal the current level of state support.

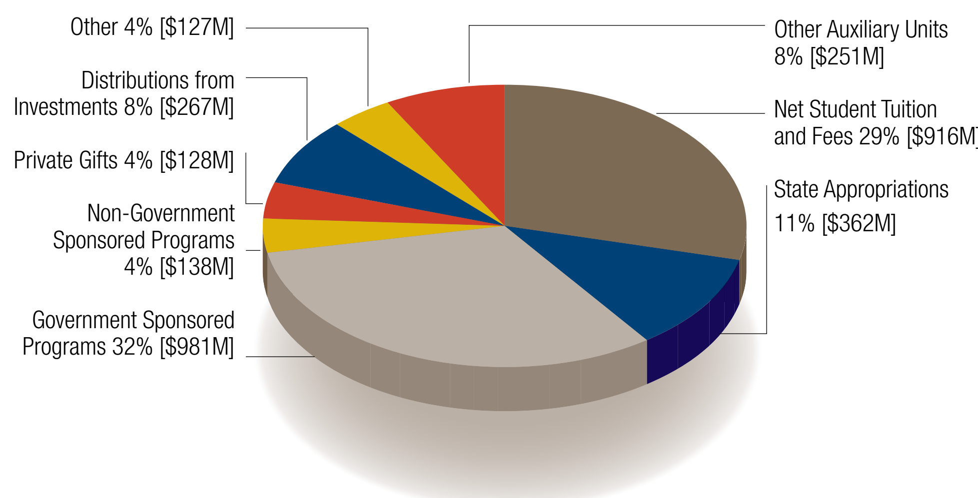
OPERATING ACTIVITIES

Total Revenue $5,656 Million



OPERATING ACTIVITIES EXCLUDING HEALTH SYSTEM AND OTHER CLINICAL ACTIVITIES

Total Revenue $3,170 Million



In FY 2012, the university faces a 15 percent—or $54 million—reduction in state appropriations, which is the largest cut in university history. The adopted budget fully absorbs this record cut while limiting the financial burden for students. At the same time, it demonstrates an unwavering commitment to the quality of the institution, both inside and outside the classroom. The general fund operating budget continues, as it has for a number of years, to balance our ongoing focus on academic excellence and access with our long-term cost containment efforts and the need to invest in our future. Multi-year budget planning, prudent management of resources, and our willingness to make tough decisions regarding priorities have enabled us to prepare for—and smooth out—the impact of the current tumultuous financial situation in the state and nation. We have been able to avoid the severe program cuts and double-digit tuition increases experienced by other institutions around the country because of our prudent long-term plan.

A disciplined approach to long-term cost containment is a driving force behind our ability to limit tuition increases, provide more financial aid, and continue to invest in teaching and research. The university's deans, directors, faculty, and staff reduced and reallocated $135 million in recurring general fund expenditures from the Ann Arbor campus budget over the period FY 2003–2009. Further, we have made significant progress over the past year toward our goal of achieving an additional $100 million reduction or reallocation of recurring general fund expenditures over the period FY 2010–2012. And, we're planning to reduce or reallocate recurring costs by another $120 million by 2017.

The approved Ann Arbor campus budget for FY 2012 includes tuition rate increases of 6.7 percent for resident undergraduates, 4.9 percent for nonresident undergraduate students, and 4.9 percent for most graduate programs. Additionally, the Ann Arbor campus budget includes $137 million in centrally awarded financial aid, the largest investment in financial aid in the university's history. Within that, centrally awarded financial aid for undergraduates is increasing by nearly 11 percent, which will help preserve access for our most financially vulnerable undergraduate students.

The approved Dearborn campus budget includes a 6.9 percent increase in undergraduate and graduate tuition rates and a 15 percent increase in institutional financial aid. At UM-Flint, the approved budget includes a 6.8 percent increase in undergraduate tuition rates, a 4.9 percent increase in graduate program tuition, and an 8.8 percent increase in institutional financial aid.

The Health System

The U-M Health System—which integrates the Hospitals and Health Centers, Medical School, Michigan Health Corporation, and a range of shared administrative services under the direction of the university's executive vice president for medical affairs—continues to receive national recognition for its academic and clinical excellence.

Despite continued challenges from the external environment, the Health System had a solid year financially. We take great pride in the fact that the Hospitals and Health Centers have experienced 15 years of positive financial margins, while also improving the quality and safety of the care we deliver to patients. In FY 2011, the University of Michigan Hospitals and Health Centers (UMHHC) achieved an operating margin of 2.7 percent ($53 million) on revenues of $2.0 billion. This margin is a testament to the integrated efforts of team members throughout the Health System to succeed despite challenging times. Once again, UMHHC's success can be attributed to a combination of more patients, more efficiency, more teamwork, and more attention to every factor that affects the bottom line. More specifically, UMHHC saw 3.3 percent more patient activity, in terms of adjusted cases, when compared to the previous year.

Such growth and financial positioning is crucial as the Health System prepares for the opening of the new C.S. Mott Children's

and Von Voigtlander Women's Hospitals in fall 2011, the opening of the renovated emergency department and arrival of new advanced helicopters in winter 2012, and the first phase of the MiChart clinical information system implementation in spring 2012.

At the same time, the Health System faces challenges posed by the state of Michigan's prolonged economic downturn, health care reform, performance-based reimbursement by insurers, and a highly competitive federal research funding environment. UMHHC continued to experience increases in FY 2011 in both the number of patients who qualify for charity care, and those who cannot pay bills for care they have already received. Additionally there was a slight increase in the percentage of Health System patients covered by Medicare, Medicaid, and county health plans, which do not reimburse at the same rates as private insurers.

In FY 2011, the Health System laid the foundation for more cooperation with partners across the state, through the launch of the Pennant Health Alliance for hospitals, the Physician Organization of Michigan for physician groups, and new partnerships with St. Joseph Mercy and other individual institutions, as well as programs designed to optimize the care experience for patients traveling great distances to receive U-M's advanced care, and the physicians who refer them. These collaborative efforts will be more important than ever in coming years.

Growing Research

Total research spending in FY 2011 grew 8.5 percent over the previous year to $1.2 billion, the third straight year the university has surpassed the billion dollar milestone. Thanks in part to research awards attained through the American Recovery and Reinvestment Act, federally funded research spending rose 10 percent over the previous fiscal year, accounting for 67 percent of total research expenditures.

The effort to transform the former Pfizer property known as the North Campus Research Complex (NCRC) into a vibrant multidisciplinary research hub accelerated greatly in FY 2011. By the end of the fiscal year, nearly 800 university and private sector employees had moved into NCRC offices and laboratories, and more than 100 proposals for scientific use of the facility had been reviewed.

The private sector engagement that is a hallmark of the NCRC came into bloom this year, with life science firms Boropharm and Lycera establishing their new corporate homes on the campus, and the opening of the Venture Accelerator to house small U-M-related startups. The move of the university's Business Engagement Center and Office of Technology Transfer to NCRC and the co-location of research support services along with the addition of several "core" research services that can be used by scientists were also achieved in FY 2011. All of this effort sets the stage for the opening of several significant scientific laboratories at NCRC in FY 2012, and provides health services researchers from across U-M a hub for their work in the new Institute for Healthcare Policy and Innovation.

Physical Plant Improvements

The university's facilities serve a wide range of needs, from research efforts and patient care to academics and the arts. With that in mind, we carefully choose which facilities should be renovated or replaced when investing in the university's future.

Over the past decade, the university has invested an average of $497 million per year for renovation and replacement of buildings and related infrastructure. FY 2011 continued this trend, with the university completing more than 247 projects across campus. A number of significant facilities to support the university's ever-changing academic, research, patient care, and athletic functions have recently been completed or are presently under construction.

North Quad Residential and Academic Complex, the first new residence hall constructed at the university in more than 40 years and one of the largest construction projects in university history, opened in fall 2010. In addition to residential spaces for 450 upper-level undergraduate students and classrooms, North Quad has offices for the School of Information and four academic units of LSA—Screen Arts & Cultures, Communication Studies, the Language Resource Center, and the Gayle Morris Sweetland Center for Writing. The facility features 19 state-of-the-art classrooms and three labs, television/video production studios, faculty offices, a dining center, a media gateway, and abundant common areas shared and utilized by all of the building occupants.

The facility is also home to two academic learning communities, the Global Scholars Program and the Max Kade German Program, providing a one-of-a-kind living and learning environment that leverages advanced networking technologies and international programs to extend the university experience to a global perspective. North Quad is a cornerstone of the university's Residential Life Initiatives, a multi-year plan to revitalize and expand the residential experience for U-M students, and to strengthen the connection between living and learning on campus.

In FY 2011, work continued on another of the largest construction projects ever undertaken by the university—the replacement for the C.S. Mott Children's Hospital and the Women's Hospital, the latter of which will be known as the Von Voigtlander Women's Hospital. The new facility, which is slated to open in November 2011, will total 1.1 million square feet with a capacity of nearly 350 beds. It is designed to bridge inpatient and outpatient services within the same medical disciplines to create a seamless approach to patient care. This state-of-the-art facility will help us continue to evolve, transform, and drive the future of children's medicine and pregnancy and childbirth care.

INVESTMENT PERFORMANCE

	Return for the twelve-month period ended June 30, 2011	Annualized five-year return	Annualized ten-year return
Long Term Portfolio	24.3%	7.4%	9.2%
U-M's Benchmark	21.4%	5.8%	6.4%
Equity/Fixed Income Index (80/20)	25.6%	4.1%	3.6%

The Endowment

The university's long-term diversified investment strategy is designed to maximize total return, while our spending rule policy is designed to protect and grow the endowment corpus in real terms and provide dependable support for operations.

The Long Term Portfolio's 24 percent return in FY 2011 follows a 12 percent return in FY 2010 and a -23 percent return in FY 2009. The Long Term Portfolio's annualized ten-year return of 9 percent was 2.8 percentage points above the custom market benchmark designed to capture the university's long-term diversified investment strategy and 5.6 percentage points over the undiversified benchmark consisting of major equity and fixed income indices in an 80/20 ratio. The return of the S&P 500 stock index was 2.7 percent over the same ten-year period.

The table above shows the endowment's favorable investment performance relative to its benchmarks. Utilizing a diversified investment strategy has limited the loss of capital in the more challenging years.

The university's endowment spending rule smoothes the impact of volatile capital markets by providing for annual distributions based on a percent of the moving average fair value of the endowment. The spending rule, along with the growth of the endowment, allowed for distributions to support operations of $266 million in FY 2011, for a total of $1.2 billion over the past five years. The payout from our more than 7,200 separate endowment funds enables us to serve a diverse population, ranging from patients in our Health System to students. For example, approximately $1.9 billion, or 24 percent, of our $7.8 billion endowment is restricted for use by our Health System, where nearly 1.9 million patient visits take place each year. The portion of the endowment available for U-M operations supports the education of more than 58,000 students. About 20 percent of our total endowment, or $1.5 billion, has been set aside for student aid, with 70 percent of our undergraduate students who are Michigan residents receiving some form of financial aid, which includes grants, work-study, and loans. Endowment income also provides key support to the university's research efforts, which have made countless contributions to our global society in areas ranging from medicine and law to the arts and sciences. The average effective annual spending rate from our endowment over the last 10 years, including spending rule payouts and withdrawals from funds functioning as endowment, primarily for strategic capital investment, was 5.6 percent.

Improving Technology

Information technology (IT) is increasingly critical to the university's success. The primary goal of the university's NextGen initiative is to dramatically advance U-M's academic, teaching, research, and clinical programs technology. As a first step, U-M completed the first-ever, comprehensive assessment of Ann Arbor campus information technology during FY 2011. The results of that process led to a set of recommendations aimed at improving the sustainability, cost effectiveness, and alignment of IT services.

The NextGen program office, which was created to prioritize those recommendations and oversee their implementation, has since launched a series of projects to improve IT quality while lowering costs. Current projects underway include the introduction of Google's suite of online collaboration tools, e-mail, and calendaring systems; IT rationalization efforts to consolidate and enhance desktop support, campus networking services, and cloud computing capabilities; and the creation of high-performance computing assets to support research activities.

The university also continues to improve and enhance its enterprise-wide systems. In FY 2011, the university completed the implementation of an automated travel and expense system for faculty and staff. In addition to automating the previous paper-based processes, the more comprehensive data available through the system will assist our strategic purchasing initiatives.

Work is continuing on the Donor & Alumni Relationship Tool, which will replace the university's last mainframe application. With implementation targeted for spring 2012, this new system will enable the university to better manage the entire lifecycle of a gift while improving the efficiency and effectiveness of development business processes.

Controlling Health Benefit Costs

The university remains very attentive to the cost of employee and retiree health benefits. This is an ever-present challenge for organizations across the country. For the university, total healthcare spending for employees and retirees was just over $305 million in FY 2011.

Drawing on the combined expertise of top clinical and health policy faculty and financial experts, we have adjusted the health benefits premium structure over the past eight years to increase the overall contribution toward healthcare coverage made by employees, dependents, and retirees. The initial premium structure changes, which began to be phased in during FY 2004, are now generating cash savings of more than $30 million annually. The most recent adjustment to the health benefit cost sharing structure commenced January 1, 2010 and is being phased in over two years. This adjustment, when fully implemented, will provide a reduction in cash outlays for university healthcare expenses of an additional $31 million annually.

Beyond that, we called on some of the university's national healthcare and health policy experts to form the Committee on Retiree Health Benefits to help us more specifically address the acceleration of benefits costs projected for current and future retirees and their dependents. The committee completed its work and the recommendations to be adopted were announced to the university community in early 2011. The changes will begin taking effect on January 1, 2013 to allow current faculty and staff time to plan for changes in retirement eligibility and the amount of university contribution they will receive during retirement. Projections indicate that these comprehensive changes will yield recurring annual cash outlay savings of more than $9 million by the year 2020 and $165 million by 2040, helping to preserve vital funding for the university's core missions and creating greater opportunity to control the rate of future tuition increases.

Prevention, early intervention, and wellness also help to reduce the pressures on the healthcare system and promote overall control of costs. The university's health and well-being program, MHealthy, addresses these factors with an array of programs designed to support healthy lifestyles, and uses health data to ensure that those programs are targeted to the greatest needs of U-M faculty and staff. University-wide health risk assessments are an important source of such population-specific data on health risk factors.

In FY 2012, MHealthy will offer its fourth health risk questionnaire and second biometric screening to all benefits-eligible employees. These assessments provide ongoing measures of our community's health and offer the university a rich opportunity to understand its greatest community health risks for targeted programs and interventions that improve health and thereby reduce the costs incurred by the university's health plans. Toward that goal, we also have begun considering recommendations from the Member Engagement Health Plan Design Committee about further steps to make the most effective use of incentives, potentially including lower premiums for employees who actively manage their chronic conditions and health risks.

Internal Controls

FY 2011 represents the seventh consecutive year that more than 40 deans and other top administrators from across campus completed an internal control review and certification of internal controls and financial information. This year, we added control guidance for employee travel and expense and use of human subject incentives to the unit certification, which already focuses on other key risk areas such as cash handling, employment, information technology security, conflict of interest, and identity theft prevention.

The launch of the Compliance Resource Center website in FY 2011 strengthened the ongoing work of compliance specialists throughout the university. This website provides a comprehensive overview of the full range of legislative and regulatory compliance obligations that impact activities throughout the university. In addition, it offers faculty and staff practical information to assist with enterprise risk management and self-monitoring while significantly increasing the visibility—and accessibility—of compliance specialists across the institution.

Conclusion

It is, once again, satisfying to receive an unqualified opinion from the university's independent financial auditors. This opinion, which appears on page 33, signifies that the financial statements present fairly the financial position of the university. Included on page 32 is my certification of management's responsibility for the preparation, integrity, and fair presentation of the university's financial statements.

I hope you will read Management's Discussion and Analysis, which begins on page 34. It provides details on how the university's financial strength, prudent financial policy, and the institution-wide commitment to sustaining the highest level of excellence work collectively to ensure the university's mission is met in the years to come.

Timothy P. Slottow
Executive Vice President
and Chief Financial Officer

Report
FROM THE VICE PRESIDENT FOR DEVELOPMENT

Jerry A. May

The University of Michigan remains a strong, vibrant, exciting place where students come to fulfill their dreams, researchers explore fascinating topics, faculty ignite curiosity and drive, patients are treated, the arts are celebrated, and great minds address the challenges facing our state and our world. It's truly an amazing place.

All these activities happen, in part, because of the generosity of our donors. And for that we are most grateful.

This year, 116,469 donors, about 5,000 more than in FY 2010, made gifts of cash and pledge payments totaling $273 million, an increase of 7 percent over FY 2010. We were particularly pleased to see that gifts from alumni increased 8 percent over last year. Along with outright gifts, bequest intentions reached $95 million, the highest amount since FY 2005.

Donors add so much to the experiences of our students by providing funds to make a U-M education affordable, international travel possible, and critical resources available.

This year, more than 11,000 students will receive financial aid thanks to donor gifts totaling nearly $53 million for endowed student support and nearly $13 million for expendable student support.

Almost 400 donors so far have made gifts to the President's Global Challenge that matches $1 for every $2 given. Donors contributed $9 million that was matched with $4.5 million. Funds are still available, and we expect to conclude the challenge

The Robert Aikens Commons and the Kirkland & Ellis Cafe, Law School

soon. U-M students are having extraordinary international experiences thanks to the commitment of President Mary Sue Coleman and the generosity of so many people.

Research support from donors makes astounding results possible. **A. Alfred Taubman (HLLD '91)** increased his support for the Taubman Medical Research Institute by $56 million, bringing his total commitment to that program to $100 million. This exceptional program now supports 15 scholars including seven Taubman Scholars, four Senior Taubman Scholars, and four Emerging Scholars. **Frances and Kenneth Eisenberg, Edith S. Briskin/S.K.S.Foundation**, and **The Marvin and Betty Danto Family Foundation** have joined with the Institute to support these Emerging Scholars who receive this support at a crucial time in their careers when they have identified highly promising, early-stage research projects that are not far enough along to attract the funding that typically goes to established projects. The Taubman Scholars are investigating such topics as breast cancer, Alzheimer's disease, obesity, prostate cancer, liver and pancreatic cancers, muscular dystrophies, kidney disease, ALS (Lou Gehrig's disease), and diabetes.

A. Alfred Taubman

This fall we are dedicating two amazing facilities made possible by the generosity of thousands of donors—the C.S. Mott Children's Hospital and Von Voigtlander Women's Hospital and the addition to the Law School. Scheduled to open in November, the new hospital facility is a $754 million project with a $75 million fundraising goal, and was the largest construction project in the state of Michigan. Fundraising for the project, led by **Athletic Director David (ABED '74) and Jan Brandon** and **Lloyd and Laurie (AB '86 DRBN) Carr**, including events like carwashes, runs, dinners, galas hosted by former U-M athletes and coaches, as well as generous gifts from individuals, has helped the Champions for Children Campaign near its goal. What a testimony to the fact that this facility has been so warmly embraced by the community it will serve!

The new Law School building has a stunning presence on State Street. This $102 million project is close to reaching its fundraising goal of $70 million as more than 400 donors stepped forward to make the building a reality with gifts from $10 to $10 million. This new four-story academic and administrative building will provide more space for a student body that has more than doubled—and a law faculty that has more than quadrupled—adding classrooms, clinics, student services, multipurpose spaces, and faculty and staff offices. Across the street, the Law Quadrangle now houses the spectacular **Robert Aikens** Commons and the **Kirkland & Ellis** Café with its beautiful glass roof.

Support from foundations reached an extremely high level this fiscal year. Gifts from these organizations totaled $50 million, surpassing FY 2010's total of $39 million by more than 25 percent.

Of particular note was a gift of $10 million from the **Wallace H. Coulter Foundation**, their culminating gift in support of an endowment for the Department of Biomedical Engineering in the College of Engineering that funds the Coulter Translational Research Partnership to help move biomedical breakthroughs from the laboratory to patient care. This follows an initial contribution of $5 million in 2006. So far the partnership has successfully launched 22 pilot projects and four biomedical startups. Projects have included a nanoscale technology that improves the effectiveness of infertility treatments; a disposable cartridge for rapid testing of bacterial infections; and a painless, non-invasive ultrasound process designed to improve the outcomes of prostate surgery.

Donors make extraordinary things happen. The university is the amazing place it is because of you. Thank you.

Jerry A. May

Jerry A. May
Vice President for Development

Development Highlights

"Henry Strachey served as secretary to the British delegation to America from 1775 to 1776, trying to negotiate a peace between England and the American colonies. These manuscripts will be a gold mine for scholars of the American Revolution. The Strachey papers give researchers another great reason to come to Ann Arbor."
— J. Kevin Graffagnino, Director of the Clements Library

- Dozens of individuals, foundations, and corporations contributed to match an anonymous donor's $150,000 challenge gift to purchase papers from the Sir Henry Strachey Collection and complete the library's Strachey holdings.

"Because of support from the Istock family's scholarship fund, I was able to focus my time and energy on my one true goal in school: to continue my professional and personal evolution as an informed and engaged educator."
— Amanda Ruud (AB '06, CERTT EDUC '11)

"The high cost of grad school can limit your career path because you have to worry more and more about salary. Having received the Istock Scholarship, I have more flexibility to pursue my dreams. And for that, I am very grateful."
— David McCarty (MBA '11)

"The Brehm Scholarship motivated me to do well in high school, and I can't thank the Brehms enough. The other Brehm scholars and I are very fortunate to be given this opportunity, and we're all trying to make the most of it."

- Senior Hussein Hamid is president of the Brehm Scholar Society. Since 2008, he and 30 other graduates of Fordson High School in Dearborn have received full-tuition scholarships funded by **William K. (BS '50, MS '52) and Dee Brehm**. Brehm Scholars who graduate from the university are also eligible for four more years of funding if admitted to the U-M Medical School.

"The Lawyers Club is a central aspect of the Michigan Law experience—where students meet, study, eat, interact, and learn together. This gift is an invaluable contribution to future students who will begin their legal careers in its rooms and halls."
— Ben Able (2L)

"It's a much-needed and much-appreciated gift that will help make the inside of the Lawyers Club just as amazing as the outside. I can honestly say I'm jealous of future students who will get to enjoy it in a finer form."
— Zach Zollinger (2L)

- Law School students will have greatly improved housing facilities in the 86-year-old Lawyers Club—including new roofs, safety features, energy efficiencies, and interior renovations—thanks to a gift from **Charles T. Munger (HLLD LAW '10)**.

Professor Hei-Wai Lee works with students

"The aim of the Initiative is to provide an in-depth exploration of sound financial decisions and personal accountability. Throughout the year, related efforts are being organized that foster the campus and community's understanding of financial literacy as it impacts businesses and individuals."
— Hei-Wai Lee, Professor of Finance, UM-Dearborn

- The **Betty F. Elliott** Initiative for Academic Excellence was launched in early 2010 by the University of Michigan-Dearborn's College of Business as a campus-wide exploration of critical business issues. With global economic crises, bankruptcies, and bailouts continuing to make headlines, financial literacy was chosen as the 2011–12 theme.

"The Richard Gilder American History Scholarship offers me the financial stability needed to pursue my degree. My heart is overcome with gratitude toward the Rachor Family Foundation for making it possible."
— Anthony DeOrnellas, UM-Flint

- The **Rachor Family Foundation** funds 18 scholarships at UM-Flint.

"Uganda was an amazing experience, and it simply would not have happened without the funding I received. It's been eye opening to see how the vast majority of the world lives."

- Chris LaFond (BS '04, MPH '06) spent four months analyzing HIV treatments thanks to the President's Global Challenge.

Student Profile

New Student Profile

The 6,116 first-year students who enrolled in September 2010 came from 50 states and almost 70 countries. They were selected from a group of 31,613 well-qualified applicants.

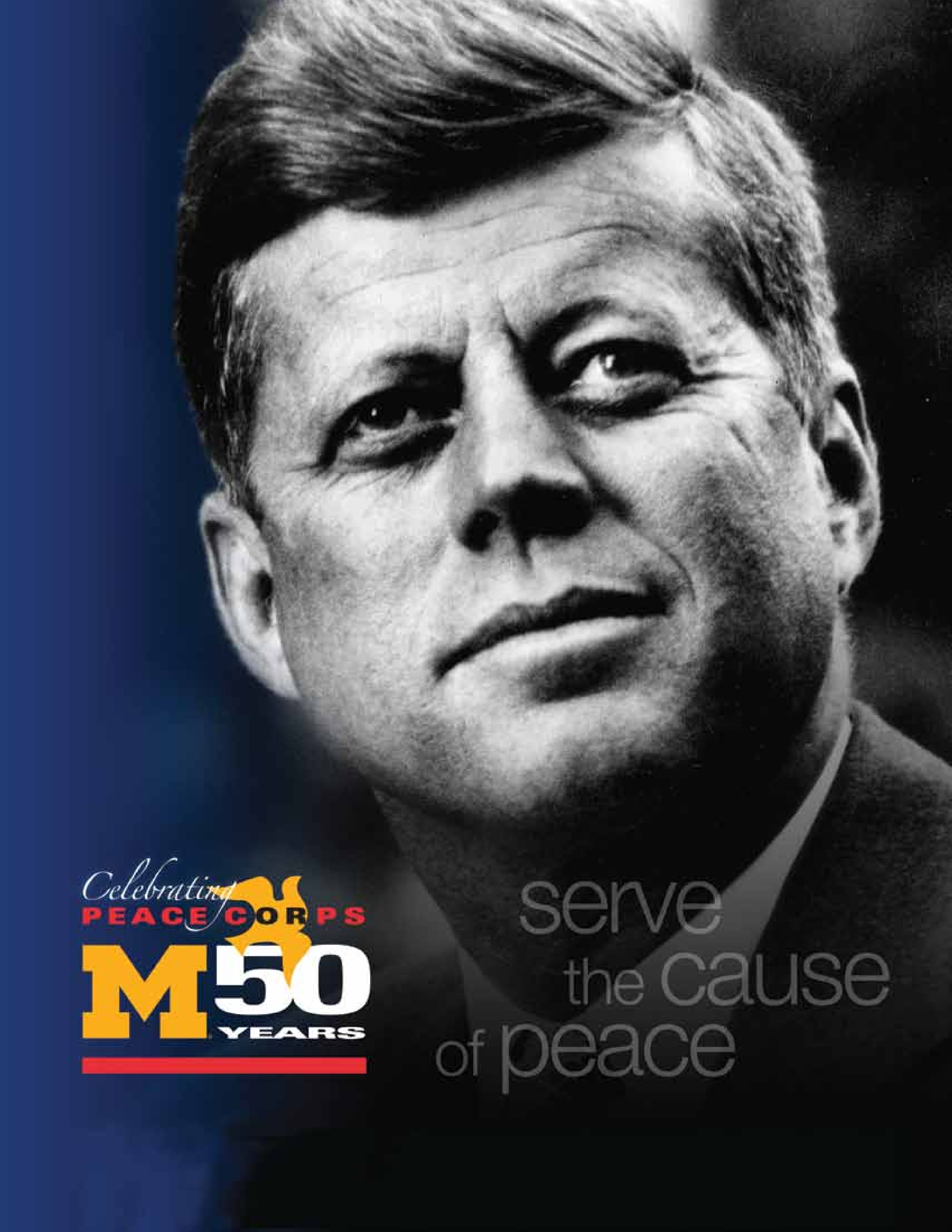
- 13% had a perfect 4.0 high school GPA
- 41% had 3.9 or higher GPA
- 84% ranked in the top 10% of their graduating class
- 50% had an ACT composite score between 30 and 36
- 48% scored between 650 and 800 on the verbal portion of the SAT, and 74% scored 650 or better on the math portion

2010 Fall Term Enrollment

	Undergraduate	Graduate/Professional	Total
ANN ARBOR	27,027	14,897	41,924
DEARBORN	7,224	1,661	8,885
FLINT	6,874	1,264	8,138
ALL CAMPUSES	41,125	17,822	58,947

2010–11 Degrees Granted

	Undergraduate	Graduate/Professional	Total
ANN ARBOR	6,553	5,361	11,914
DEARBORN	1,174	524	1,698
FLINT	921	395	1,316
ALL CAMPUSES	8,648	6,280	14,928


Celebrating
PEACE CORPS
M50
YEARS
serve
the cause
of peace

Leadership & Service

Peace Corps Celebrates 50th Anniversary

President Mary Sue Coleman and Peace Corps Director Aaron Williams sign a new Peace Corps partnership.

Well after midnight on October 14, 1960, presidential candidate John F. Kennedy arrived at the Michigan Union after a long day of campaigning. Speaking from the stone steps at the front of the Union, he challenged the more than 5,000 U-M students assembled there to dedicate themselves to global peace and justice by living and working in developing nations. Inspired by his impromptu speech, hundreds of U-M students signed a petition saying they would volunteer.

On November 6, just days before the election, three carloads of U-M students drove to Toledo, Ohio, to present the petitions to then-Senator Kennedy. On March 1, 1961, JFK, now president, signed an executive order that officially established the Peace Corps, the signature program that has defined international volunteer service for the past 50 years.

"It might still be just an idea but for the affirmative response of those Michigan students and faculty," wrote Sargent Shriver, JFK's brother-in-law and the Peace Corps' first director. Since 1960, nearly 200,000 Americans—including 2,200 U-M graduates—have lived abroad in the service of world peace, making a difference in the lives of others.

To commemorate the U-M origins of the Peace Corps, the university created a special website and hosted a month-long series of events. Among them was a 2:00 a.m. ceremony on October 14, 2010, on the same stone steps of the Union, 50 years to the hour that JFK made his world-changing speech.

To learn more about Peace Corps history at U-M and events commemorating the Corps' 50th anniversary, visit www.peacecorps.umich.edu.

- U-M is joining with Michigan State University to lead a federally funded effort to help Great Lakes-region residents anticipate and adapt to climate change. The new Great Lakes Regional Integrated Sciences and Assessments Center will focus on agriculture, watershed management, and natural resources-based recreation and tourism.

- **The Planet Blue Operations Team reported an 8 percent decrease in the amount of energy used for FY 2011 in 52 campus buildings, with a total savings of nearly $4 million annually.**

- **The William Davidson Institute is partnering with Washtenaw Community College to promote entrepreneurship among students at Al Quds College in Jordan. The goal of the project is to expand job opportunities and foster community development.**

- UM-Dearborn's community service personnel scholarship program has helped nearly 30 local police officers further their education. The program provides a 20 percent tuition credit for officers pursuing undergraduate or graduate degrees.

- UM-Flint earned special recognition from the Carnegie Foundation for the Advancement of Teaching by demonstrating their commitment to outreach, partnerships, and curricular engagement in the greater Flint community.

- **The Tillman Military Scholars program, which provides educational scholarships for veterans and active service members and their dependents, selected UM-Flint as one of five new partners for service to veterans. *G.I. Jobs* magazine named UM-Flint as a Military-Friendly School for 2011.**

- To ensure a healthier environment for faculty, staff, and students, U-M implemented a new smoke-free policy that became effective July 1, 2011. The policy affects all grounds and buildings on the three campuses.

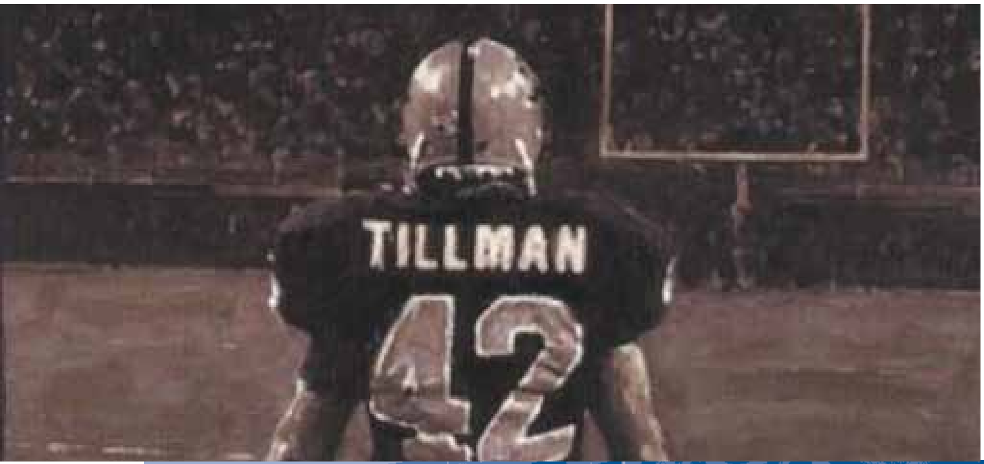
- Top managers and staff members gathered at the first-ever StaffWorks Technology and Best Practices Conference to share ideas on how to make technology best serve U-M's core missions going forward.

- Seeing a growing need for public health professionals, UM-Flint's Department of Public Health and Health Services is collaborating with the School of Public Health (on the Ann Arbor campus) to offer a master's in public health.

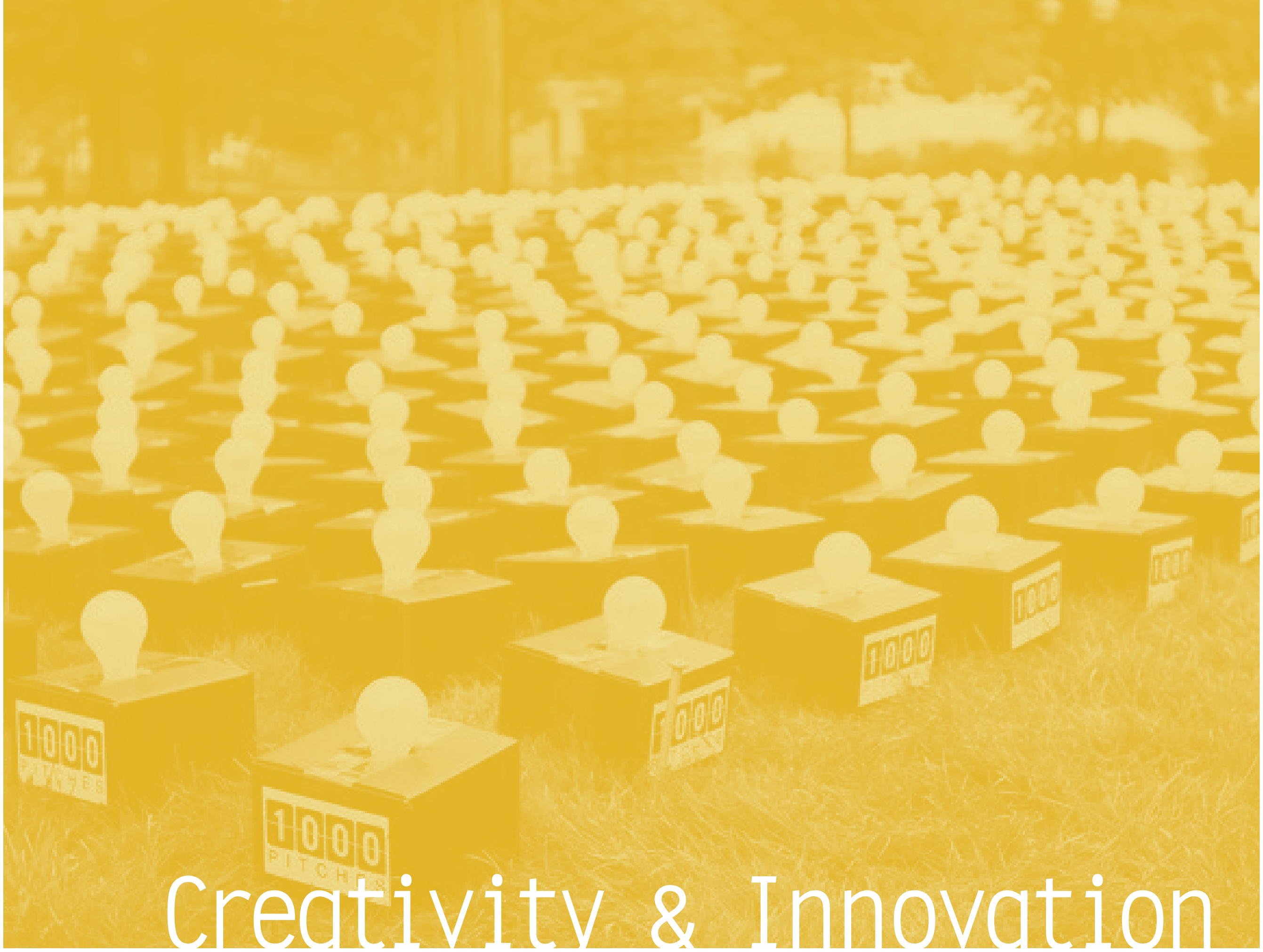
- The Women's Sports Foundation selected U-M to establish a joint research and policy center. The Women's Sports, Health, Activity, and Research and Policy Center generates interdisciplinary research on issues related to women's sports, health, gender identity, and kinesiology.

- **In September 2010, U-M held an EarthFest to showcase sustainability efforts taking place on campus and in the surrounding communities. U-M musical and dance groups performed, local restaurants and farms gave out free food, and volunteers participated in a "trash sort," going through a single day's worth of trash from a U-M building to filter recyclables from traditional garbage.**

- **As part of its commitment to sustainability, U-M launched the Sustainable Office Program. Aimed at "greening" the workplace, this program focuses on encouraging sustainable behavior in such areas as energy, water, printer, and copier usage.**




POWERED
ADAM



Creativity & Innovation

MPowered 1,000 Pitches

MPowered's 1,000 Pitches was established to generate entrepreneurial ideas and to help students bring their ideas to the table.

Heated sneakers for cold winters. A mobile app for determining nearby restaurant options. A system for purifying water that doesn't use energy or oil. These were among the 3,031 submissions to the third annual 1,000 Pitches entrepreneurship competition, a contest designed to encourage students to generate and share ideas.

The largest student-run pitch competition in the world, 1,000 Pitches awards $1,000 in prize money to the student with the most innovative business or product idea in each of the following categories: the environment, health, mobile apps, tech and hardware, web and software, social entrepreneurship, consumer products, small business, and MProvements. Since the contest was launched three years ago, the number of pitches has tripled. The competition is one of many events and programs sponsored by MPowered Entrepreneurship, a student-led group focused on inspiring and empowering people to create. In partnership with the Center for Entrepreneurship, MPowered hosts the MPowered Career Fair, an annual job and internship event that brings together U-M students and representatives from small businesses and startups. The group also directs the Peer Mentorship Program, which provides students with mentors who will guide them through the entrepreneurial process.

In April, President Coleman met with 60 MPowered students to provide an update on U-M's efforts to support entrepreneurial endeavors on campus. She praised the group for their inventiveness and ideas and pointed out how unique they are, since many universities have some form of technology transfer office, but not a student-led organization designed to encourage entrepreneurial gusto.

- In FY 2011, U-M licensed more technologies to companies than ever before. The Office of Technology Transfer recorded 101 licenses and options, researchers reported 322 inventions and filed for 122 patents, and U-M helped launch 11 companies—eight of which have set up shop in Michigan.

- **U-M opened its Venture Accelerator in January at the North Campus Research Center. The office will provide lab space, office space, and business services for the Office of Tech Transfer's startup companies.**

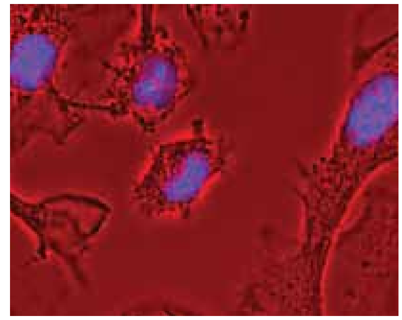
- U-M launched the "Innovate!" website (innovate.umich.edu), a refreshed version of the Innovation Economy website originally created in 2009. The site features university innovator profiles and news, reports, resources, and programs.

- Marshalling an increasing student interest in the social-impact investment space, the Zell Lurie Institute at the Ross School of Business launched the Social Venture Fund (SVF). The fund trains students to invest in and manage sustainable, for-profit enterprises that respond to societal needs.

- CSquared Innovations, a startup project based on technology developed in the labs of UM-Dearborn, won the top prize of $50,000 in the 2011 Clean Energy Prize business plan competition. CSquared Innovations has developed a faster, cheaper, laser-based method of making nano-structured materials and coatings for lithium-ion battery electrodes, solar cells, and industrial coatings.

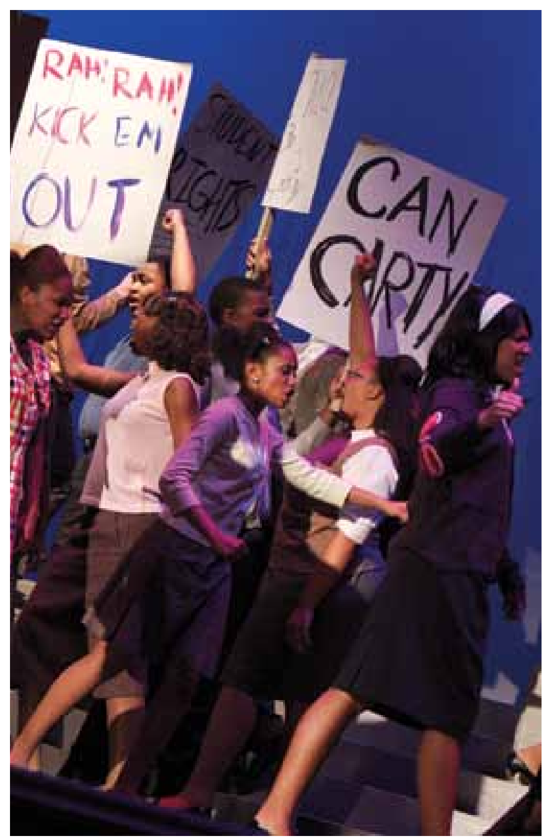
- UM-Dearborn established a Business Experiential Learning Laboratory, a new high-tech classroom in the College of Business that simulates a real-world trading room—complete with a crawling stock ticker, a six-time-zone world clock, and an eight-foot data wall with information streamed from Wall Street. The lab—called The BELL—will provide students with opportunities for hands-on training in an environment similar to what they will find in the business world

- **U-M history students and Detroit high school students who perform with Mosaic Youth Theatre of Detroit collaborated on a play—*Northern Lights 1966*. Their original work was performed by the Mosaic troupe at the Detroit Institute of Arts.**



- **U-M researchers have discovered that a protein (Lkb1) known to regulate cellular metabolism is also essential for normal cell division in blood-forming stem cells. This research could lead to new treatments for degenerative diseases.**

- University researchers have created the state's first human embryonic stem cell lines that carry the genes responsible for inherited disease. The achievement will enable scientists here to study the onset and progression of genetic disorders and to search for new treatments.



- **In September 2010, U-M launched the President's Advisory Committee on Public Art website (public-art.umich.edu) to provide a single source of information about public art on the Ann Arbor campus. The site features photos and brief descriptions of public artworks, maps for locating them, and information on the application process for submitting proposals for new works.**

- In February, U-M faculty members Michael Daugherty and Amy Ku'uleialoha Stillman received the music industry's top honors at the 53rd annual Grammy Awards. Daugherty won a Grammy for Best Classical Contemporary Composition, and Stillman earned her second Grammy for Best Hawaiian Music Album.

- The National Science Foundation awarded a $200,000 grant to UM-Dearborn's College of Engineering and Computer Science to acquire leading-edge technologies to establish a plug-in hybrid electric vehicle research and training laboratory.

- U-M will establish a new healthcare policy institute to enhance the health and wellbeing of local, national, and global populations through innovative, interdisciplinary health services research. The Institute for Healthcare Policy and Innovation is expected to become one of the largest of its kind in the nation.

- **Filmmakers continued to choose U-M for their production destination. Films made on campus recently include *The Double*, *The Ides of March*, and *Five Years of Engagement*. *The Ides of March*, a political thriller directed by George Clooney (shown here with local actress Talia Akiva), opened the prestigious Venice Film Festival in August.**

- **Top students from the School of Music, Theatre & Dance performed at the Kennedy Center in Washington, D.C., as part of the Millennium Stage Conservatory Project. This program introduces the best young musicians in the country to Washington audiences.**

- Sponsored by LSA, the theme semester for the fall 2010—"What Makes Life Worth Living?"—invited students and community members to explore this question and the answers offered over the centuries and around the globe.

- In April, 40 student ventures were featured at U-M's Student Startup Showcase. Held at the TechArb Student Startup Accelerator, the event celebrated the achievements of student entrepreneurs while connecting them with local venture capitalists and angel investors.

Excellence & Achievement

Symphony Band in China

The Michigan Symphony Band had the thrill of performing in China

Fifty years ago, U-M's Symphony Band visited Russia and the Middle East on a pioneering 15-week State Department tour. In May 2011, the band revived this tradition of international cultural diplomacy in support of President Mary Sue Coleman's China initiatives with a 23-day tour with 11 concerts in Hangzhou, Shanghai, Shenyang, Xi'an, Tianjin, and Beijing, closing with a gala performance in Los Angeles in Frank Gehry's Walt Disney Concert Hall.

U-M Director of Bands and Professor Michael Haithcock and 76 student musicians made friends and fans wherever they performed. "The concerts were deeply rewarding, yet the development of trust and understanding was our most important accomplishment. We returned home with a renewed sense of empowerment that the arts do indeed provide a common bond across humanity." said Haithcock.

The band featured new works by four U-M faculty composers: William Bolcom's *Concerto Grosso for Saxophone Quartet and Band* in which the counterpoint of Johann Sebastian Bach meets the blues; Michael Daugherty's iconic *Lost Vegas*; Bright Sheng's *Shanghai Overture for Band* that quotes two traditional Chinese melodies; and Kristin Kuster's *Two Jades*—a violin concerto inspired by Chinese artworks in U-M's Museum of Art and featuring U-M alumnus Xiang Gao, a Beijing native, as soloist.

School of Music, Theatre & Dance Dean Christopher Kendall summed up the tour saying, "I can't say enough about the performances, on stage and off, of our Symphony Band students. The concerts were consistently brilliant, living up to the observation made by many that this ensemble represents the top of the form."

- Five U-M professors were among 180 winners of Guggenheim Fellowships. They are: Arun Agrawal, School of Natural Resources and Environment; Jeffrey Gardner Heath, Linguistics; Mark Sheldon Mizruchi, Sociology and Business; Endi E. Poskovic, Art and Design; and Jennifer Ellen Robertson, Anthropology.

- Forty-three students were awarded Fulbright grants for 2010–11, the highest number in U-M's history. Recipients of Fulbright grants are selected on the basis of academic or professional achievement, as well as demonstrated leadership potential in their fields.

- Majors and programs focusing on sustainability experienced an explosive growth. Undergrad enrollment in the Program in the Environment more than doubled since 2005, and enrollment in the School of Natural Resources and Environment master's program and the dual-degree (MBA/MS) program offered through the Erb Institute also reached record numbers.

- **U-M's Solar Car Team won the American Solar Challenge for a sixth North American title. *Infinium* is believed to be the university's fastest solar car ever, reaching 100 mph in testing.**

- Research spending at U-M in 2010–11 grew 8.5 percent over the previous year to $1.2 billion, the third straight year the university has surpassed the billion-dollar milestone. Federally funded research spending at U-M rose 10 percent over the previous fiscal year, accounting for 67 percent of total research expenditures.

- **Two faculty members were named to the American Academy of Arts and Sciences. They are: Sharon Glotzer, chemical engineering, College of Engineering; and Scott Page, political science and economics, LSA.**

- **Dr. Eva Feldman, professor of neurology and research scientist at the Medical School, was named one of the "Michiganians of the Year" by the *Detroit News* for her research on potential therapies for amyotrophic lateral sclerosis and other neurologic diseases.**

- UM-Flint made The Princeton Review's 2011 edition of its book, *The Best 300 Business Schools*.

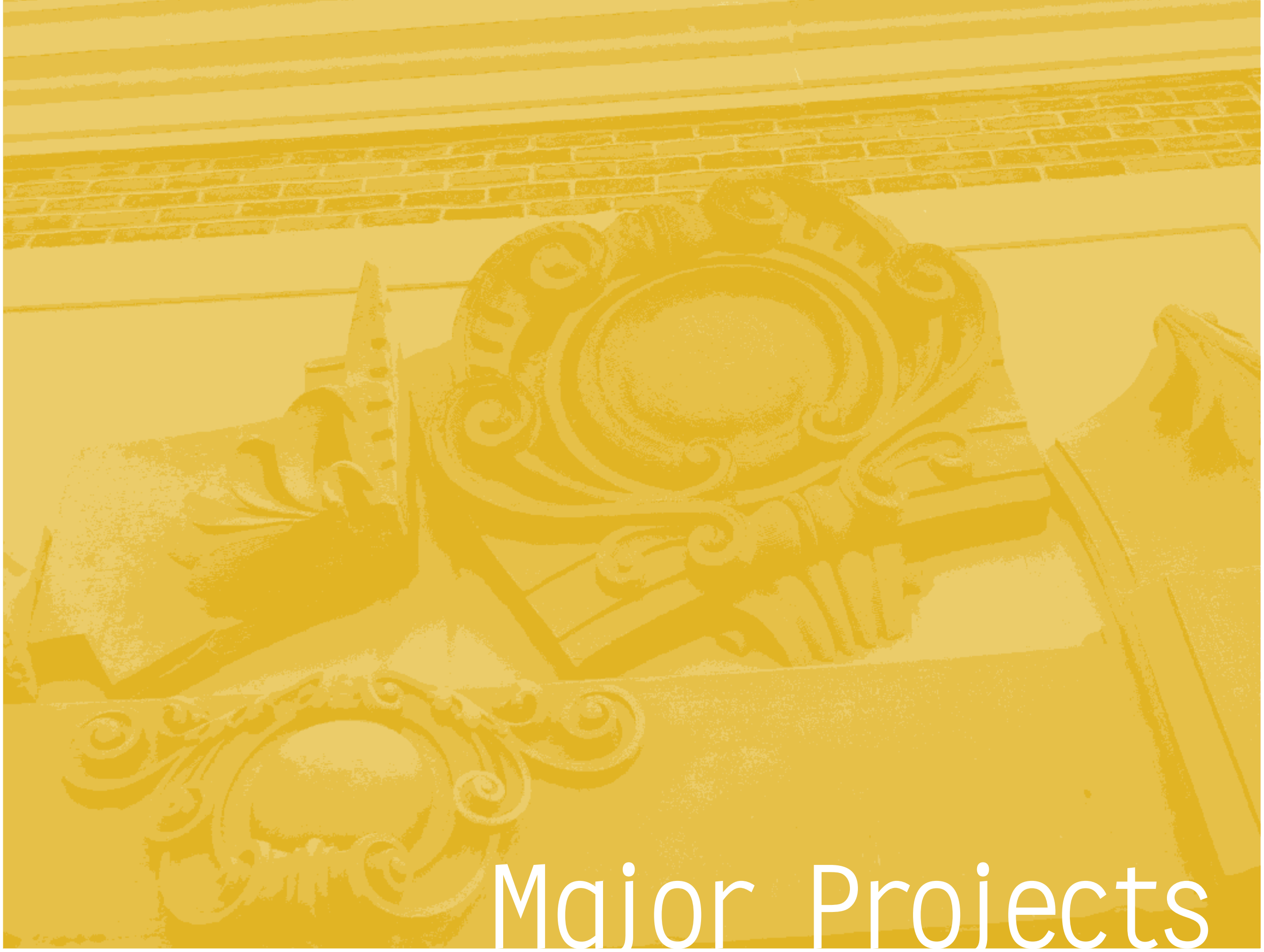
- Six faculty members were honored with Arthur F. Thurnau Professorships for their outstanding contributions to undergraduate education. They are: Amy Cohn, industrial and operations engineering, College of Engineering; Stephen DeBacker, mathematics, LSA; Mika LaVaque-Manty, political science and philosophy, LSA; Barry Rabe, public policy, Gerald R. Ford School of Public Policy, environmental policy, School of Natural Resources and Environment, and environment, LSA; Melanie Sanford, chemistry, LSA; and Colleen Seifert, psychology, LSA.

- **For the fourth consecutive year, U-M received a record number of applications from prospective freshmen. Overall, there were 31,613 applications for academic year 2010–11, compared with 29,965 in the previous year.**

- For the 17th consecutive year, *U.S. News & World Report* named U-M Hospitals and Health Centers one of "America's Best Hospitals." U-M placed 14th overall for the third year in a row and was the only hospital in Michigan to make the national honor roll. The magazine also named C.S. Mott Children's Hospital one of "America's Best Children's Hospitals."

- **Hundreds of visitors toured the North Quadrangle Residential and Academic Complex during a March 31 Community Open House. The event offered campus and community members an up-close look at North Quad's undergraduate residential spaces, high-tech classrooms and labs, faculty offices, dining hall, and abundant common areas.**

- UM-Flint was the fastest-growing state university in Michigan, with a 4.6 percent increase in enrollment.



Major Projects

Projects in Planning

Beal Avenue Water Main and North Campus Storm Relief System Upgrades

George Granger Brown Memorial Laboratories Mechanical Engineering Addition

Crisler Arena Expansion

Fuller Road Station

Institute for Social Research Addition

The Lawyers' Club Building and John P. Cook Building Renovation

Medical Science Unit II Integrative Physiology Department Renovations

Michigan Memorial Phoenix Laboratory Addition and Second Floor Renovation

North Campus Research Complex Building 16 Renovation for Health Services Research

North Campus Support Facility

University of Michigan Hospitals and Health Centers Programs

- Eisenhower Corporate Park West Orthotics and Prosthetics Center Expansion
- Parkview Medical Center and Scott and Amy Prudden Turner Memorial Clinic Building Demolition
- Simpson Circle Parking Structure Improvements
- University Hospital Computed Tomography Angiography
- University Hospital Kitchen Renovations for Room Service Protocol
- University Hospital Radiation Oncology Simulator Replacement

Yost Ice Arena Seating Replacement and Fan Amenities Improvement

Projects in Progress

Auxiliary Services Building Renovations for School of Art & Design | Work started December 2010 with an estimated completion date of September 2011. Financing is from investment proceeds.

Burton Memorial Tower Facade and Bell Tower Repairs | Work started September 2010 with an estimated completion date of December 2011. Financing is from general fund.

Central Campus Area Utility Tunnel Refurbishment | Work started March 2011 with an estimated completion date of March 2012. Financing is from utilities reserves.

Crisler Arena, Michigan Stadium, and Yost Ice Arena Scoreboard Replacement | Work started March 2011 with an estimated completion date of September 2011. Financing is from Athletic Department.

Crisler Arena Renovation | Work started December 2010 with an estimated completion date of March 2012. Financing is from Athletic Department.

James and Anne Duderstadt Center Air Barrier and Mechanical System Repairs | Work started August 2010 with an estimated completion date of August 2011. Financing is from general fund.

Golf Practice Facility | Work started October 2010 with an estimated completion date of September 2011. Financing is from Athletic Department and gifts.▼

Institute for Social Research Wing One Fire Suppression System | Work started June 2011 with an estimated completion date of July 2012. Financing is from Institute for Social Research and Office of the Provost.

Edward Henry Kraus Building Molecular, Cellular and Developmental Biology Laboratory Renovations | Work started March 2011 with an estimated completion date of December 2011. Financing is from College of LSA.

Law School Academic Building and Hutchins Hall Law School Aikens Commons Addition | Work started June 2009 with an estimated completion date of June 2012. Financing is from gifts, investment proceeds, and Law School.

C.C. Little Science Building Geological Sciences Laboratory Renovations | Work started April 2011 with an estimated completion date of December 2011. Financing is from College of LSA.

Alice Crocker Lloyd Hall Renovation | Work started February 2011 with an estimated completion date of September 2012. Financing is from Housing.

Modern Languages Building Second Floor and Basement Renovation | Work started January 2011 with an estimated completion date of September 2011. Financing is from College of LSA.

North Campus Chiller Plant Expansion | Work started August 2010 with an estimated completion date of December 2011. Financing is from utilities reserves and general fund.

▲

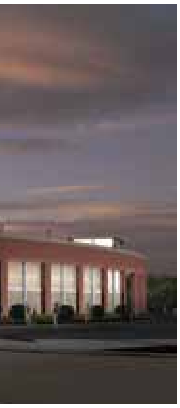
Player Development Center for Intercollegiate Basketball | Work started April 2010 with an estimated completion date of December 2011. Financing is from Athletic Department and gifts.

School of Social Work Building Atrium Level Renovations | Work started April 2011 with an estimated completion date of September 2011. Financing is from School of Social Work.

South Quadrangle Elevator Replacement | Work started November 2010 with an estimated completion date of September 2011. Financing is from Housing.

University of Michigan Hospitals and Health Centers Programs | Financing is from Hospitals and Health Centers.

- **C. S. Mott Children's and Von Voigtlander Women's Hospitals Replacement Project** | Work started February 2007 with an estimated completion date of November 2011. Financing is from Hospitals and Health Centers and gifts.
- **C. S. Mott Children's and Von Voigtlander Women's Hospitals Replacement Project Shell Space Completion Project** | Work started October 2010 with an estimated completion date of November 2011.
- **Multiple Buildings Pneumatic Tube System Upgrade** | Work started July 2010 with an estimated completion date of September 2011.



- **University Hospital Emergency Department Expansion** | Work started November 2010 with an estimated completion date of March 2012.

- **University Hospital Emergency Power System Improvements** | Work started January 2010 with an estimated completion date of December 2011.

- **University Hospital Medical Procedure Unit Expansion** | Work started May 2011 with an estimated completion date of June 2012.

Varsity Drive Building and Alexander G. Ruthven Museums Building Museum of Zoology Collection Relocation and Renovations | Work started April 2010 with an estimated completion date of December 2012. Financing is from investment proceeds.

Wolverine Tower Renovations for Business and Finance | Work started April 2010 with an estimated completion date of December 2011. Financing is from Business and Finance.

Projects Completed

Administrative Services Building Substation Replacement | Completed November 2010. Financed by investment proceeds.

Building Access Control Project | Completed June 2011. Financed by investment proceeds.

Central Campus Transit Center | Completed November 2010. Financed by federal transportation funds and federal American Recovery and Reinvestment Act of 2009 funds via the Ann Arbor Transportation Authority, with the university providing matching funds from Business and Finance, Parking, and utilities reserves.

Central Power Plant Water Treatment System Improvements | Completed March 2011. Financed by utilities reserves.

Couzens Hall Renovation | Completed June 2011. Financed by Housing and investment proceeds.

School of Education Building Renovations for the Brandon Professional Resource Center and Archive | Completed April 2011. Financed by gifts, School of Education, and investment proceeds.

Engineering Programs Building Addition | Completed December 2010. Financed by College of Engineering.

Thomas Francis, Jr., Public Health Building Infrastructure and Finishes Renewal | Completed October 2010. Financed by School of Public Health and investment proceeds.

Carl A. Gerstacker Building Molecular Beam Epitaxy Laboratory Renovation | Completed June 2011. Financed by College of Engineering.

Intercollegiate Soccer Stadium | Completed August 2010. Financed by Athletic Department and gifts.

Edward Henry Kraus Building Biology Laboratory Renovations | Completed August 2010. Financed by the College of LSA.

Kresge Complex Demolition | Completed December 2010. Financed by the Medical School.

Lorch Hall Building Envelope Repair | Completed September 2010. Financed by general fund.

Michigan Stadium Permanent Field Lights | Completed December 2010. Financed by Athletic Department.

Thompson Street Parking Structure Addition | Completed November 2010. Financed by Parking and investment proceeds.

University of Michigan Hospitals and Health Centers Programs | Financed by Hospitals and Health Centers.

- **A. Alfred Taubman Health Care Center Registration Area Renovations on Levels 1–3** | Completed July 2010.

- **University Hospital Central Sterile Supply Expansion** | Completed June 2011.

- **University Hospital Inpatient Adult Psychiatry Renovation** | Completed December 2010.

Management Responsibility for Financial Statements

THE UNIVERSITY OF MICHIGAN
OFFICE OF THE EXECUTIVE VICE PRESIDENT AND CHIEF FINANCIAL OFFICER

3014 FLEMING ADMINISTRATION BUILDING
ANN ARBOR, MICHIGAN 48109-1340
(734) 764-7272 FAX (734) 936-8730

September 12, 2011

The management of the University of Michigan (the "University") is responsible for the preparation, integrity, and fair presentation of the consolidated financial statements. The financial statements, presented on pages 51 to 79, have been prepared in conformity with accounting principles generally accepted in the United States of America and, as such, include amounts based on judgments and estimates by management.

The consolidated financial statements have been audited by the independent accounting firm PricewaterhouseCoopers LLP, which was given unrestricted access to all financial records and related data, including minutes of all meetings of the Board of Regents. The University believes that all representations made to the independent auditors during their audit were valid and appropriate. PricewaterhouseCoopers' audit opinion is presented on page 33.

The University maintains a system of internal controls over financial reporting, which is designed to provide reasonable assurance to the University's management and Board of Regents regarding the preparation of reliable published financial statements. Such controls are maintained by the establishment and communication of accounting and financial policies and procedures, by the selection and training of qualified personnel, and by an internal audit program designed to identify internal control weakness in order to permit management to take appropriate corrective action on a timely basis. There are, however, inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention of controls.

The Board of Regents, through its Finance, Audit and Investment Committee, is responsible for engaging the independent auditors and meeting regularly with management, internal auditors, and the independent auditors to ensure that each is carrying out their responsibilities and to discuss auditing, internal control, and financial reporting matters. Both internal auditors and the independent auditors have full and free access to the Finance, Audit and Investment Committee.

Based on the above, I certify that the information contained in the accompanying financial statements fairly presents, in all material respects, the financial condition, changes in net assets and cash flows of the University.

Timothy P. Slottow
Executive Vice President and Chief Financial Officer

Report of Independent Auditors

The Regents of the University of Michigan

In our opinion, the accompanying consolidated statements of net assets and the related consolidated statements of revenues, expenses and changes in net assets and of cash flows present fairly, in all material respects, the financial position of the University of Michigan (the "University") at June 30, 2011 and 2010, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The Management's Discussion and Analysis ("MD&A") on pages 34 through 50 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the MD&A. However, we did not audit the information and express no opinion on it.

PricewaterhouseCoopers LLP

September 12, 2011

PricewaterhouseCoopers LLP, 1900 St. Antoine Street, Detroit, MI 48226
T: (313) 394 6000, F: (313) 394 6555 www.pwc.com/us

Management's Discussion and Analysis (Unaudited)

Introduction

The following discussion and analysis provides an overview of the financial position of the University of Michigan (the "University") at June 30, 2011 and 2010 and its activities for the three fiscal years ended June 30, 2011. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

The University is a comprehensive public institution of higher learning with approximately 59,000 students and 7,100 faculty members on three campuses in southeast Michigan. The University offers a diverse range of degree programs from baccalaureate to post-doctoral levels through 19 schools and colleges, and contributes to the state and nation through related research and public service programs. The University also has a nationally renowned health system which includes three hospitals, 40 health centers, more than 120 outpatient clinics, the University's Medical School and Michigan Health Corporation, a wholly-owned corporation created to pursue joint venture and managed care initiatives. The University, in total, employs approximately 42,000 permanent employees and 12,000 temporary staff.

The University consistently ranks among the nation's top universities by various measures of quality, both in general academic terms, and in terms of strength of offerings in specific academic disciplines and professional subjects. Excellence in research is another crucial element in the University's high ranking among educational institutions. Research is central to the University's mission and permeates its schools and colleges. In addition to the large volume of research conducted within the academic schools, colleges and departments, the University has more than a dozen large-scale research institutes outside the academic units that conduct, in collaboration with those units, full-time research focused on long-term interdisciplinary matters. The University's Health System also has a tradition of excellence in teaching, advancement of medical science and patient care, consistently ranking among the best health care systems in the nation.

Financial Highlights

The University's financial position remains strong, with assets of $15.6 billion and liabilities of $4.7 billion at June 30, 2011, compared to assets of $13.8 billion and liabilities of $4.5 billion at June 30, 2010. Net assets, which represent the residual interest in the University's assets after liabilities are deducted, totaled $10.9 billion at June 30, 2011, as compared to $9.3 billion at June 30, 2010. Changes in net assets represent the University's results of operations and are summarized for the years ended June 30, 2011 and 2010 as follows:

(in millions)	2011	2010
Operating revenues and educational appropriations	$ 5,186.3	$ 4,949.3
Total operating and net interest expenses	5,463.8	5,245.6
	(277.5)	(296.3)
Net investment income	1,633.0	796.4
Gifts and other nonoperating revenues, net	205.8	198.3
Increase in net assets	$ 1,561.3	$ 698.4

Net assets increased $1.6 billion in fiscal 2011 and $698 million in fiscal 2010 primarily due to net investment income which totaled $1.6 billion and $796 million in fiscal 2011 and 2010, respectively.

Operating revenues and educational appropriations increased 5 percent, or $237 million, while total operating and net interest expenses increased 4 percent, or $218 million. The results of operations reflect the University's focus on maintaining its national standards academically, in research and in health care in a competitive recruitment environment for faculty and health care professionals. At the same time, the University is addressing declining base state appropriations and rising health care, regulatory and facility costs with aggressive cost cutting and productivity gains to help preserve access to affordable higher education for Michigan families.

Net investment income totaled $1.6 billion and $796 million in 2011 and 2010, respectively. The University invests its financial assets in pools with distinct risk and liquidity characteristics based on its needs, with most of its financial assets invested in two such pools. The University's working capital is primarily invested in relatively short duration, liquid assets, while the University's endowment is invested in an equity oriented long-term strategy that greatly benefitted from strong equity market performance last year. The success of this long-term investment strategy is evidenced by strong returns over sustained periods of time.

Using the Financial Statements

The University's financial report includes three financial statements: the Statement of Net Assets; the Statement of Revenues, Expenses and Changes in Net Assets; and the Statement of Cash Flows. These financial statements are prepared in accordance with Governmental Accounting Standards Board ("GASB") principles, which establish standards for external financial reporting for public colleges and universities.

Statement of Net Assets

The statement of net assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. The difference between total assets and total liabilities—net assets—is one indicator of the current financial condition of the University, while the change in net assets is an indication of whether the overall financial condition has improved or worsened during the year. A comparison of the University's assets, liabilities and net assets at June 30, 2011 and 2010 is summarized as follows:

(in millions)	2011	2010
Current assets	$ 2,095	$ 1,789
Noncurrent assets:		
Endowment, life income and other investments	8,122	6,807
Capital assets, net	5,193	4,956
Other	246	267
Total assets	15,656	13,819
Current liabilities	1,408	1,449
Noncurrent liabilities	3,324	3,007
Total liabilities	4,732	4,456
Net assets	$ 10,924	$ 9,363

The University continues to maintain and protect its strong financial foundation. This financial health, as reflected in the statement of net assets at June 30, 2011 and 2010, results from the prudent utilization of financial resources including careful cost controls, preservation of endowment funds, conservative utilization of debt and adherence to a long-range capital plan for the maintenance and replacement of the physical plant.

Current assets consist primarily of cash and cash equivalents, operating and capital investments and accounts receivable. Total current assets increased $306 million, to $2.1 billion at June 30, 2011, primarily due to increases in cash and investments. Cash, cash equivalents and operating investments totaled $981 million at June 30, 2011, which represents approximately two months of total expenses excluding depreciation.

Current liabilities consist primarily of accounts payable, accrued compensation, deferred revenue, commercial paper, the current portion of bonds payable and net long-term bonds payable subject to remarketing. Current liabilities totaled $1.4 billion at June 30, 2011 and 2010.

Endowment, Life Income and Other Investments

The University's endowment, life income and other investments increased $1.3 billion, to $8.1 billion at June 30, 2011. This increase primarily resulted from unrealized gains on investments, as well as the receipt of new endowment funds through gifts and transfers, offset by endowment distributions to beneficiary units for operations. The composition of the University's endowment, life income and other investments at June 30, 2011 and 2010 is summarized as follows:

(in millions)	2011	2010
Endowment investments	$ 7,835	$ 6,564
Life income investments	105	94
Noncurrent portion of insurance and benefits obligations investments	182	149
	$ 8,122	$ 6,807

The University's endowment funds consist of both permanent endowments and funds functioning as endowment. Permanent endowments are those funds received from donors with the stipulation that the principal remain inviolate and be invested in perpetuity to produce income that is to be expended for the purposes specified by the donors. Funds functioning as endowment consist of amounts (restricted gifts or unrestricted funds) that have been allocated by the University for long-term investment purposes, but are not limited by donor stipulations requiring the University to preserve principal in perpetuity. Programs supported by endowment funds include scholarships, fellowships, professorships, research efforts and other important programs and activities.

The University uses its endowment funds to support operations in a way that strikes a balance between generating a predictable stream of annual support for current needs and preserving the purchasing power of the endowment funds for future periods. The major portion of the endowment is maintained in the University Endowment Fund, a unitized pool which represents a collection of approximately 7,200 separate (individual) funds, the majority of which are restricted for specific purposes. The University Endowment Fund is invested in the University's Long Term Portfolio, a single diversified investment pool.

The endowment spending rule provides for distributions from the University Endowment Fund to the University entities that benefit from the endowment fund. Commencing with the quarter ending September 30, 2010, the annual distribution rate began to be reduced from 5 percent of the one-quarter lagged seven year moving average fair value of University Endowment Fund assets to 4.5 percent. This change is one element of an ongoing financial management strategy that has allowed the University to effectively weather the recent recession while avoiding drastic measures taken by many of our peer institutions, such as faculty hiring freezes, furloughs, program cuts or halting construction. To avoid negative impacts of this change on near-term budgets, endowment distributions are being managed toward the new rate by keeping quarter to quarter distributions per share unchanged and gradually moving toward the 4.5 percent rate when increases in share value would otherwise result in higher per share distributions. The length of the implementation period will depend on the actual investment returns and resulting changes in share values experienced during the implementation period.

To protect endowment principal in the event of a prolonged market downturn, distributions are limited to 5.3 percent of the current fair value of fund shares. Any capital gains or income generated above the endowment spending rate are reinvested so that in lean times funds will be available for distribution. In addition, departments may also use withdrawals from funds functioning as endowment to support capital expenditures and operations.

Endowment spending rate distributions totaled $266 million, $255 million and $244 million and withdrawals from funds functioning as endowment totaled $44 million, $5 million and $46 million in 2011, 2010 and 2009, respectively. Total spending rate distributions combined with withdrawals from funds functioning as endowment averaged 5.4 percent, 5.1 percent and 5.9 percent of the current year average fair value of the University Endowment Fund for 2011, 2010 and 2009, respectively. Over the past ten years, total spending rate distributions combined with withdrawals from funds functioning as endowment averaged 5.6 percent.

Capital and Debt Activities

One of the critical factors in continuing the quality of the University's academic, research and clinical programs is the development and renewal of capital assets. The University continues to implement its long-range plan to modernize its complement of older facilities, along with balanced investment in new construction.

Capital asset additions totaled $635 million in 2011, as compared to $695 million in 2010. Capital asset additions primarily represent replacement, renovation and new construction of academic, research, clinical, athletic and student residence facilities, as well as significant investments in equipment, including information technology. Current year capital asset additions were primarily funded with net assets and gifts designated for capital purposes of $410 million, as well as debt proceeds of $224 million and state capital appropriations of $1 million.

Construction in progress, which totaled $825 million at June 30, 2011, and $546 million at June 30, 2010, includes important new facilities for patient care, research, instruction, athletics and student residential life.

At June 30, 2011, construction continues on a new facility for C.S. Mott Children's Hospital and Von Voigtlander Women's Hospital to meet increasing patient demand and accommodate future research, education and clinical care innovations. The new state-of-the-art facility will further enhance specialty services for newborns, children and women, not offered anywhere else in Michigan, including programs for Level I pediatric trauma, pediatric liver transplant and craniofacial anomalies as well as high-risk pregnancy and specialty gynecological services. With a clinic building of nine floors and an inpatient building of twelve floors, the new facility will be approximately 1.1 million square feet. Opening in November 2011, the new facility will enable our world-renowned physicians and researchers to deliver world-class care and train tomorrow's generation of women's and children's specialists in the finest health care environment.

Construction projects also continue at the Law School. Legal education has changed considerably since Hutchins Hall, the main classroom and administrative building for the Law School, opened in 1933. Today's law students take a greater number of small classes, interact more with each other and with clients in supervised clinical settings and draw heavily on technology. Located across Monroe Street and south of the Law Quad, a new four-story academic and administrative building is under construction to meet these needs, as well as provide more space for a student body which has more than doubled since the last time the Law School added classroom space. In addition, the new, two-level Robert B. Aikens Commons will occupy the currently unused grassy area between Hutchins Hall and the Legal Research Building. This structure will include a main floor café and a lower level designed to facilitate student meetings and study groups. This project also includes life safety upgrades to Hutchins Hall and the Cook Library. These projects are scheduled to be completed in fiscal 2012.

The renovation of Alice Lloyd Hall is part of the University's residential life initiatives, a comprehensive multi-year plan to improve and expand the student residential experience. Like the deep renovations to Mosher Jordan, Stockwell and Couzens residence halls in previous years, the infrastructure of the building will be thoroughly upgraded, including high-speed network access to renovated bath facilities, accessibility improvements and new plumbing, heating, cooling, ventilation and fire detection and suppression systems. In addition, energy conservation measures will be implemented to improve the energy performance of the overall building, which was originally constructed in 1949. New spaces will be created in the vacated dining areas that are no longer needed since the Hill area Dining Center became operational in Fall 2008. The new and reorganized spaces within the facility will revitalize the residence hall and create spaces for living-learning and academic initiatives, student interaction and creation of community. This project is scheduled to be completed in Summer 2012.

Crisler Arena has only received minor renovations since its construction in 1967 and a significant renovation project is now underway to address its highest priority infrastructure needs. The seats in the lower and upper bowl of this multi-purpose venue will also be replaced, including modifications to meet the requirements of the Americans with Disabilities Act. A 57,000-square-foot Player Development Center will also be added to address the need for more functional training and practice space for the men's and women's basketball programs. The Center will connect to the east side of Crisler Arena and house two basketball practice courts, team locker areas, strength and conditioning space, athletic medicine space and coaching and staff offices. These projects are scheduled to be completed in fiscal 2012.

Renovation and expansion projects completed in 2011 include the Couzens Residence Hall and the Thompson Street Parking Structure. The comprehensive renovation of Couzens Residence Hall is part of the University's residential life initiatives to improve the residential facilities on campus and to strengthen the connections between living and learning. The Thompson Street Parking Structure addition is an integral part of the University's strategic plan to replace parking lost on central campus due to various construction projects and to provide for a growth in parking demand. This project added parking and office space to the west side of the existing structure. The expanded parking structure now accommodates 1,049 vehicles, an increase of 273 parking spaces. The office space addition provides 9,000 gross square feet of office and support space for Parking and Transportation Services and the Office of Budget and Planning, which previously utilized leased space.

In June 2009, the University completed the acquisition of the former Pfizer pharmaceutical research complex for approximately $114 million, which included liabilities of approximately $6 million that were assumed as part of the purchase. This investment, which was funded primarily with Health System resources, provides a transformational opportunity for the University to develop and utilize the 30 buildings and nearly 174 acres of land acquired. Known collectively as the North Campus Research Complex ("NCRC"), the nearly 2 million square feet of sophisticated laboratory facilities and administrative space will provide much needed space to help attract new research funding and faculty to the University. The unoccupied portion of the complex is classified as property held for future use and totaled $54 million and $84 million at June 30, 2011 and 2010, respectively.

During 2011, $30 million of the acquired property was placed in service, including two significant laboratory buildings with supporting office space. Significant improvements were not needed to prepare these facilities for occupancy. More than 160 office-based researchers moved to the NCRC to start the Institute for Healthcare Policy and Innovation. Co-location of the many health service research groups currently dispersed throughout the University is beneficial given the interdisciplinary nature of the challenges in health care delivery. More than 500 researchers could eventually join this Institute, with many more engaging virtually, making it one of the nation's largest concentrations of health care policy and services researchers.

The University's Office of Technology Transfer and Business Engagement Center relocated to the complex and started a Venture Accelerator which provides a continuous innovation pipeline for faculty to move their ideas from the lab bench into a commercial reality. In addition, several laboratory-based scientific cores initiated satellite activities at the NCRC, including the DNA sequencing core. The first laboratory-based researchers, from the cardiovascular center as well as new recruits to the oncology research program, also moved to the complex.

In aggregate, 300 people moved into the complex during 2011 and thousands more utilized the facilities for conferences and events throughout the year. The NCRC will support the growth of the University's translational research initiatives through the population of office space, laboratories and other facilities over the next several years.

The University takes its financial stewardship responsibility seriously and works hard to manage its financial resources effectively, including the prudent use of debt to finance capital projects. A strong debt rating is an important indicator of the University's success in this area. During April 2011, Moody's Investors Service, Inc. ("Moody's") affirmed its highest credit rating (Aaa) for bonds backed by a broad revenue pledge based on extremely strong credit fundamentals, including significant financial resources, strong market position and consistent operating performance derived from a well diversified revenue base. In May 2011, Standard & Poor's Ratings Services ("Standard & Poor's") also affirmed its highest credit rating (AAA) based on the University's national reputation for academic and research excellence, strong financial resources, positive financial performance, exceptional record of fundraising and manageable debt burden and capital plan. Only two other public universities have received the highest credit ratings from both Moody's and Standard & Poor's.

Long-term debt activity for the year ended June 30, 2011, and the type of revenue it is supported by, is summarized as follows:

(in millions)	Beginning Balance	Additions	Reductions	Ending Balance
Commercial Paper:				
General revenues	$ 87	$ 85	$ 81	$ 91
Bonds and Notes:				
General revenues	1,050	220	28	1,242
Hospital revenues	300		5	295
Faculty Group Practice revenues	65		3	62
Student residences revenues	2			2
	$ 1,504	$ 305	$ 117	$ 1,692

The University utilizes commercial paper, backed by a general revenue pledge, to provide interim financing for its capital improvement program. Outstanding commercial paper is converted to long-term debt financing, as appropriate, within the normal course of business. At June 30, 2011 and 2010, commercial paper totaled $91 million and $87 million, respectively, and is included in current liabilities.

During 2011, consistent with capital and debt financing plans, the University issued $212.3 million of fixed-rate taxable Build America Bonds (Series 2010D) and $7.2 million of fixed-rate tax-exempt general revenue bonds (Series 2010E) with a net original issue premium of $0.5 million. Bond proceeds, which totaled $220.0 million, were utilized to provide for capital projects and debt issuance costs.

The University maintains a combination of fixed and variable rate debt, which totaled $1.7 billion and $1.5 billion at June 30, 2011 and 2010, respectively. The University's fixed and variable rate debt at June 30, 2011 and 2010 is summarized as follows:

(in millions)	**2011**	**2010**
Variable rate:		
Commercial paper	$ 91	$ 87
Demand bonds	747	760
Fixed rate bonds	854	657
	$ 1,692	$ 1,504

In 2011, the University continued to increase its mix of fixed rate bonds relative to variable rate demand bonds. While fixed rate bonds typically have a higher effective rate of interest as compared to variable rate demand bonds, they reduce the volatility of required debt service payments and do not require liquidity support, such as letters of credit or guarantees.

Effective interest rates averaged 2.5 percent in 2011 and 2.0 percent in 2010, including the amortization of bond premiums and discounts and net of federal subsidies for interest on taxable Build America Bonds. Interest expense net of federal subsidies received for interest on taxable Build America Bonds and interest capitalized during construction totaled $26 million in 2011 and $27 million in 2010, while capitalized interest on debt financed construction in progress totaled $17.6 million and $5.6 million in 2011 and 2010, respectively.

The University's variable rate bonds are subject to remarketing and, in accordance with GASB Interpretation No. 1, are classified as current liabilities unless supported by long-term liquidity arrangements, such as lines of credit or standby bond purchase agreements, which could refinance the debt on a long-term basis. In the event that variable rate bonds are put back to the University by the debt holder, management believes that the bonds will be remarketed within a reasonable amount of time. The University's strong credit rating facilitates the remarketing of its debt. In addition, the University maintains three remarketing agents to achieve a wide distribution of its variable rate debt.

Obligations for Postemployment Benefits

In accordance with the provisions of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*, the University recognizes the cost of postemployment benefits during the periods when employees render their services. Using current actuarial assumptions, and presuming a continuation of the current level of benefits, the University's obligations for postemployment benefits totaled $1.64 billion and $1.61 billion at June 30, 2011 and 2010, respectively. Since a portion of retiree medical services will be provided by the University's Health System, this liability is net of the related margin and fixed costs of providing those services which totaled $239 million and $199 million at June 30, 2011 and 2010, respectively.

By implementing a series of health benefit initiatives over the past seven years, the University has favorably impacted its actuarial accrued liability for postemployment benefits by approximately $408 million as of June 30, 2011. These initiatives have included cost sharing changes, elimination of Medicare Part B reimbursements for certain retirees and adjustment of retirement eligibility criteria. At June 30, 2011, the recorded liability for net postemployment benefits obligations totaled $1.64 billion and the actuarial accrued liability totaled $1.18 billion. The University amortizes changes in actuarial assumptions, plan design and experience gains and losses over a 10-year closed period. Accordingly, the liability for net postemployment benefits obligations recorded in the statement of financial condition differs from the actuarial accrued liability by the unamortized portion of changes in actuarial assumptions, plan design and experience gains and losses.

In accordance with GASB Statement No. 45, the University's net obligations for postemployment benefits at June 30, 2011, do not reflect anticipated Medicare Part D prescription drug subsidies for future years of $139 million, which will offset a portion of future cash outlays.

Net Assets

Net assets represent the residual interest in the University's assets after liabilities are deducted. The composition of the University's net assets at June 30, 2011 and 2010 is summarized as follows:

(in millions)	2011	2010
Invested in capital assets, net of related debt	$ 3,575	$ 3,503
Restricted:		
Nonexpendable:		
Permanent endowment corpus	1,279	1,214
Expendable:		
Net appreciation of permanent endowments	1,312	924
Funds functioning as endowment	1,652	1,447
Restricted for operations and other	503	439
Unrestricted	2,603	1,836
	$ 10,924	$ 9,363

Net assets invested in capital assets represent the University's capital assets net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets. The $72 million increase reflects the University's continued development and renewal of its capital assets in accordance with its long-range capital plan.

Restricted nonexpendable net assets represent the historical value (corpus) of gifts to the University's permanent endowment funds. The $65 million increase primarily represents new gifts. Restricted expendable net assets are subject to externally imposed stipulations governing their use. This category of net assets includes net appreciation of permanent endowments, funds functioning as endowment and net assets restricted for operations, facilities and student loan programs. Restricted expendable net assets totaled $3.5 billion at June 30, 2011, as compared to $2.8 billion at June 30, 2010.

Although unrestricted net assets are not subject to externally imposed stipulations, all of the University's unrestricted net assets have been designated for various academic and research programs and initiatives, as well as capital projects. Unrestricted net assets at June 30, 2011 and 2010 totaled $2.6 billion and $1.8 billion, respectively. At June 30, 2011, unrestricted net assets included funds functioning as endowment of $3.5 billion offset by unfunded obligations for postemployment benefits of $1.6 billion. At June 30, 2010, unrestricted net assets included funds functioning as endowment of $2.9 billion offset by unfunded obligations for postemployment benefits of $1.6 billion. Unrestricted net assets at June 30, 2011 and 2010 also included other net resources of $700 million and $500 million, respectively.

Statement of Revenues, Expenses and Changes in Net Assets

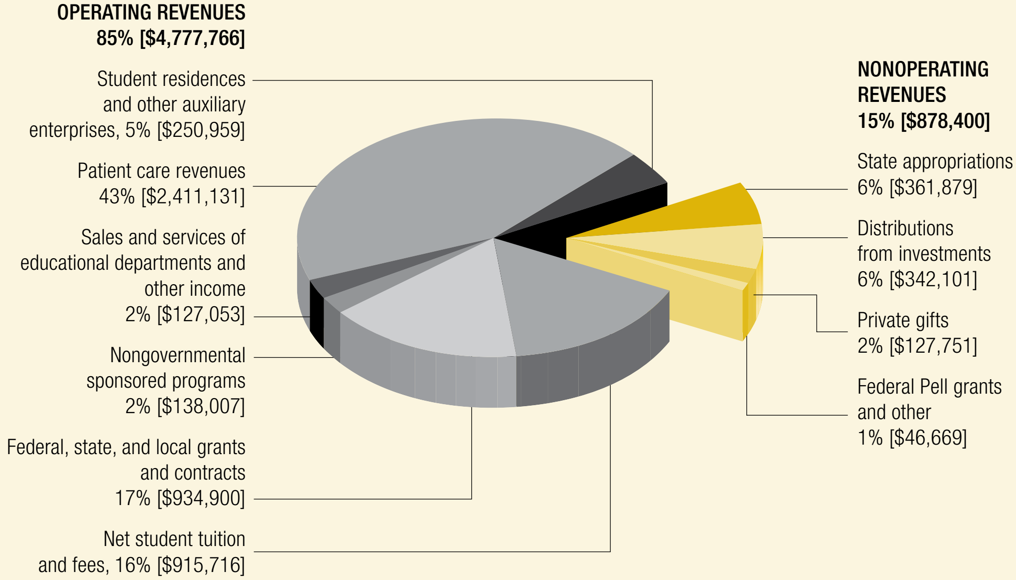
The statement of revenues, expenses and changes in net assets presents the University's results of operations. In accordance with GASB reporting principles, revenues and expenses are classified as either operating or nonoperating. A comparison of the University's revenues, expenses and changes in net assets for the three years ended June 30, 2011, is summarized as follows:

(in millions)	2011	2010	2009
Operating revenues:			
Student tuition and fees, net of scholarship allowances	$ 915.7	$ 863.9	$ 826.3
Sponsored programs	1,072.9	990.3	897.3
Patient care revenues, net	2,411.1	2,310.8	2,168.5
Other	378.1	372.2	344.4
	4,777.8	4,537.1	4,236.5
Operating expenses	5,437.8	5,218.8	5,042.1
Operating loss	(660.0)	(681.7)	(805.6)
Nonoperating and other revenues (expenses):			
State educational appropriations	361.9	362.1	373.8
State fiscal stabilization funds		10.1	
Federal Pell grants	46.7	39.9	24.9
Private gifts for operating activities	127.8	105.2	96.5
Net investment income (loss)	1,633.0	796.4	(1,851.9)
Interest expense, net	(33.1)	(30.0)	(25.1)
Federal subsidies for interest on Build America Bonds	7.1	3.3	
State capital appropriations	0.8	2.0	12.2
Endowment and capital gifts and grants	82.3	88.7	88.4
Other	(5.2)	2.4	(1.6)
Nonoperating and other revenues (expenses), net	2,221.3	1,380.1	(1,282.8)
Increase (decrease) in net assets	1,561.3	698.4	(2,088.4)
Net assets, beginning of year	9,363.0	8,664.6	10,753.0
Net assets, end of year	$ 10,924.3	$ 9,363.0	$ 8,664.6

One of the University's greatest strengths is the diverse streams of revenue that supplement its student tuition and fees, including private support from individuals, foundations and corporations, along with government and other sponsored programs, state appropriations and investment income. The University continues to aggressively seek funding from all possible sources consistent with its mission in order to supplement student tuition and prudently manage the financial resources realized from these efforts to fund its operating activities.

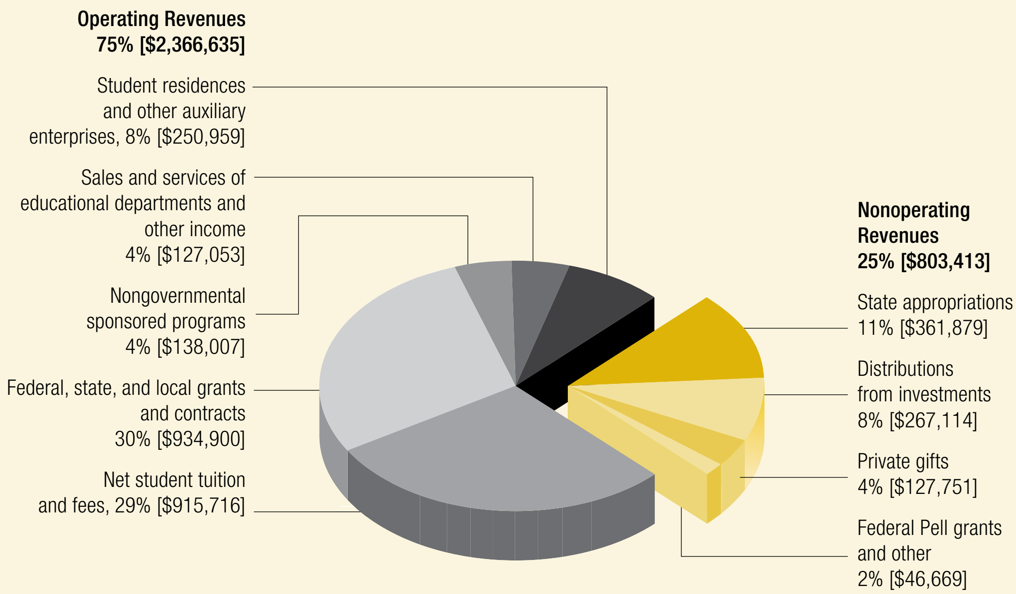
The following is a graphic illustration of revenues by source, both operating and nonoperating, which are used to fund the University's operating activities for the year ended June 30, 2011 (amounts are presented in thousands of dollars). Significant recurring sources of the University's revenues are considered nonoperating, as defined by GASB, such as state appropriations, distributions from investments, private gifts and federal Pell grants.

Fiscal Year 2011 Revenues for Operating Activities



The University measures its performance both for the University as a whole and for the University without its Health System and other similar activities. The exclusion of the Health System allows a clearer view of the operations of the schools and colleges, as well as central administration. The following is a graphic illustration of University revenues by source, both operating and nonoperating, which are used to fund operating activities other than the Health System, for the year ended June 30, 2011 (amounts are presented in thousands of dollars).

Fiscal Year 2011 Revenues for Operating Activities Excluding Revenues from the University's Health System



Tuition and state appropriations are the primary sources of funding for the University's academic programs. There is a relationship between the growth or reduction in state support and the University's ability to restrain tuition fee increases. Together, net student tuition and fees and base state appropriations increased 4 percent, or $52 million, to $1.3 billion in 2011, as compared to 2 percent, or $26 million, to $1.2 billion in 2010.

Downturns in state of Michigan tax revenues continue to put pressure on the state budget and base state educational appropriations continue to be constrained, decreasing 3 percent, or $12 million, over the past two years, to $362 million in 2011.

To maintain academic excellence and offset constrained base state appropriations, net student tuition and fees revenue increased 11 percent, or $89 million, over the past two years. For the three years ended June 30, 2011, net student tuition and fees revenue consisted of the following components:

(in millions)	2011	2010	2009
Student tuition and fees	$ 1,177.9	$ 1,097.5	$ 1,029.2
Scholarship allowances	(262.2)	(233.6)	(202.9)
	$ 915.7	$ 863.9	$ 826.3

In 2011, net student tuition and fees revenue increased 6 percent, or $52 million, to $916 million, which reflects a 7 percent, or $80 million, increase in gross tuition and fee revenues offset by a 12 percent, or $28 million, increase in scholarship allowances. Tuition rate increases in 2011 were 1.5 percent for resident undergraduate students, 3.0 percent for nonresident undergraduate students and 2.8 percent for most graduate students on the Ann Arbor campus, with a 3.9 percent tuition rate increase for all undergraduates and 2.9 percent increase for most graduate students on the Dearborn campus, and a 3.9 percent tuition rate increase for most undergraduate students on the Flint campus. The University also experienced significant growth in the number of students.

In 2010, net student tuition and fees revenue increased 5 percent, or $38 million, to $864 million, which reflects a 7 percent, or $68 million, increase in gross tuition and fee revenues offset by a 15 percent, or $30 million, increase in scholarship allowances. Tuition rate increases in 2010 were 5.6 percent for all undergraduate and most graduate students on the Ann Arbor campus, with a 6.7 percent tuition rate increase for all undergraduates and 3.1 percent increase for most graduate students on the Dearborn campus, and a 6.5 percent tuition rate increase for most undergraduate students on the Flint campus. The University also experienced modest growth in the number of students.

Despite constrained base state appropriations, the University's tuition increases have been among the lowest in the state and in the Big Ten, which reflects a commitment to affordable higher education for Michigan families. At the same time, the University has also increased scholarship allowances and scholarship and fellowship expenses, to benefit students in financial need.

In 2010, the University received $10 million from the State Fiscal Stabilization Fund program, a one-time appropriation under the American Recovery and Reinvestment Act of 2009. The U.S. Department of Education awarded state governors funds in exchange for a commitment to advance essential education reforms to benefit students from early learning through post-secondary education, including college. These funds were also awarded to help stabilize state and local government budgets in order to minimize and avoid reductions in education and other essential public services. The University used its allocation to provide financial aid to resident students.

While tuition and state appropriations fund a large percentage of University costs, private support is becoming increasingly essential to the University's academic distinction. Private gifts for other than capital and permanent endowment purposes totaled $128 million in 2011, as compared to $105 million in 2010 and $97 million in 2009.

The University receives revenues for sponsored programs from various government agencies and private sources, which normally provide for both direct and indirect costs to perform these sponsored activities. Revenues for sponsored programs increased 8 percent, or $83 million, to $1.1 billion in 2011, as compared to an increase of 10 percent, or $93 million, to $1.0 billion in 2010. A significant portion of the University's sponsored programs revenues relate to federal research and its growth in 2011 and 2010 is due in large part to federal stimulus funds from the American Recovery and Reinvestment Act of 2009, which totaled $128 million in 2011 and $60 million in 2010.

Patient care revenues are principally generated within the University's hospitals and ambulatory care facilities under contractual arrangements with governmental payers and private insurers. Patient care revenues increased 4 percent, or $100 million, to $2.4 billion in 2011, as compared to an increase of 7 percent, or $142 million, to $2.3 billion in 2010. The increased revenues for both years primarily resulted from a growth in both outpatient and inpatient volume, as well as increased reimbursement rates from third party payers.

Net investment income totaled $1.6 billion in 2011, as compared to net investment income of $796 million and net investment loss of $1.9 billion in 2010 and 2009, respectively. During 2011 and 2010, financial markets recovered from the impact of the global financial crisis in 2009. Equity and equity related investments across global markets performed particularly well in 2011, which helped the performance of the University's investment portfolio where all asset classes except fixed income and cash had double digit positive returns. In addition, the real estate segment of the University's investment portfolio experienced positive returns in 2011, after losses in 2010 and 2009.

In 2009, the financial market turmoil that followed the banking crisis in 2008 resulted in broad losses across the University's public and private equity and equity-like investments, with the largest losses occurring in areas that had experienced the greatest gains in the years preceding the crisis, such as real estate, energy and other alternative investments. Despite the losses in 2009, these assets remain the University's highest performing investments over longer time periods.

The University's endowment investment policies are designed to maximize long-term total return, while its income distribution policy is designed to preserve the value of the endowment and generate a predictable stream of spendable income.

Private gifts for permanent endowment purposes totaled $57 million in 2011, as compared to $60 million in 2010 and $61 million in 2009. Capital gifts and grants totaled $25 million in 2011, as compared to $29 million in 2010 and $28 million in 2009. Over the past three years, major capital gifts have been received in support of the University's wide-ranging building initiatives, which include the Health System, Intercollegiate Athletics, Law School and College of Engineering.

In addition to revenue diversification, the University continues to make cost containment an ongoing priority. This is necessary as the University continues to face significant financial pressures, particularly in the areas of compensation and benefits, which represent 66 percent of total expenses, as well as in the areas of energy, technology and ongoing maintenance of facilities and infrastructure.

A comparative summary of the University's expenses for the three years ended June 30, 2011, is as follows:

(in millions)	2011		2010		2009	
Operating:						
Compensation and benefits	$ 3,633.8	66%	$ 3,529.3	66%	$ 3,390.5	66%
Supplies and services	1,299.6	24	1,215.6	24	1,203.0	24
Depreciation	390.1	7	360.1	7	341.5	7
Scholarships and fellowships	114.3	2	113.8	2	107.1	2
	5,437.8	99	5,218.8	99	5,042.1	99
Nonoperating:						
Interest, net	26.0	1	26.7	1	25.1	1
	$ 5,463.8	100%	$ 5,245.5	100%	$ 5,067.2	100%

The University is committed to recruiting and retaining outstanding faculty and staff and the compensation package is one way to successfully compete with peer institutions and nonacademic employers. The resources expended for compensation and benefits increased 3 percent, or $105 million, to $3.6 billion in 2011, as compared to a 4 percent increase, or $139 million, to $3.5 billion in 2010. Of the 2011 increase, compensation increased 4 percent, to $2.8 billion, and employee benefits increased less than 1 percent, to $854 million. For 2010, compensation increased 5 percent, to $2.7 billion, and employee benefits increased 3 percent, to $851 million.

Health care benefits are one of the most significant employee benefits. Over the past several years, the University has implemented initiatives to better control its rate of increase, encourage employees to choose the lowest cost health care plan that meets their needs and share a larger portion of health care cost increases with employees.

Compared to most employers, the University is in an unique position to utilize internal experts to advise and guide its health care and drug plans. For example, the University utilizes a Pharmacy Benefits Advisory Committee, which consists of internal experts including Health System physicians, School of Pharmacy faculty and an on-staff pharmacist, to monitor the safety and effectiveness of covered medications as well as to optimize appropriate prescribing, dispensing and cost effective use of prescription drugs. The University also actively promotes and manages generic drug utilization and has achieved a 76 percent generic dispensing rate in 2011, as compared to 72 percent in 2010 and 71 percent in 2009.

The University continues to utilize its nationally recognized health policy experts to guide future health plan strategies. After careful review, a series of changes are being implemented to help the University maintain competitive active and retiree benefits while helping control the growth in costs.

During 2011, the University announced changes to eligibility requirements for retiree health benefits and the related amount of the University's contributions. These changes are based on the work of a committee on retiree health benefits that was formed to propose a means to maintain competitive retiree health benefits while helping address the acceleration of health benefits costs for current and future retirees and their dependents. To assist current employees with the transition, changes will be phased in gradually over the eight-year period January 1, 2013, through January 1, 2021.

Commencing January 1, 2013, the University will use a point system to determine retirement eligibility, where points represent the combination of age and years of service for full-time employees. The points needed for retirement will total 76 in 2013 and gradually be increased to 80 by 2021. During this time period, the University's contributions towards health care benefits for employees who retire in each of these years will gradually be reduced. Employees who retire after December 31, 2020, will need a minimum of 20 years of service to receive the maximum retiree health benefit contribution. Specifically, the University's contributions towards health care benefits will decrease from 87.5 percent for the retiree and 65 percent for any dependents for those employees who retire in 2013 to a maximum of 80 percent for the retiree and 50 percent for any dependents for those employees who retire in 2021. For new hires, the maximum University contribution upon retirement with 20 or more years of service will be 68 percent for the retiree and 26 percent for any dependents, commencing in 2013. These adjustments will keep the University's retiree benefits competitive with peer institutions while producing an estimated $9 million reduction in annual cash outlay by 2020 and an estimated $165 million reduction in annual cash outlay by 2040.

Effective January 1, 2010, the University commenced a new health benefits cost sharing program which is being phased in over two years. Once fully implemented, the University's overall contribution toward the health care of employees, retirees and dependents will be 70 percent of the total cost of premiums, co-pays and deductibles. Down from the current 80 percent overall contribution, the new target is more in line with average contributions of peer universities and health systems. The percentage applied to each individual depends on the plan choice and whether dependents are covered. Under the new structure, contribution amounts will be based on salary bands which are designed to lessen the impact on lower paid employees and retirees. In addition, the University's health premium contribution for part-time employees working between 20 and 31 hours per week will be reduced from 100 percent to 80 percent of the contribution made for full-time staff in the lowest salary band. Once fully implemented, these changes are expected to reduce the University's annual cash outlay for health care expenses by approximately $31 million.

In addition, beginning January 1, 2010, newly hired faculty and staff are subject to a one-year waiting period before receiving the University's 10 percent retirement savings plan contribution. This change results in annual savings of approximately $11 million.

The MHealthy initiative is a campus-wide effort to improve the health and well-being of faculty, staff and their dependents. During 2011, more than 20,000 employees participated in the MHealthy rewards program by completing a health risk assessment and at least one qualifying health and wellness program. Over 75 percent of all benefits-eligible employees have participated in at least one health risk assessment between 2009 and 2011. Data gathered from these assessments, as well as from aggregate medical claims, is used to monitor progress in addressing the greatest areas of community health risk.

These initiatives and programs reflect the reality of the national landscape, while remaining true to the commitment we make to our employees for a robust benefits package.

Supplies and services expenses increased 7 percent, or $84 million, to $1.3 billion in 2011, as compared to an increase of 1 percent, or $13 million, to $1.2 billion in 2010. The increases in 2011 and 2010 are primarily due to increases in patient care and sponsored research activities offset by aggressive cost cutting and productivity gains.

In addition to their natural (object) classification, it is also informative to review operating expenses by function. A comparative summary of the University's expenses by functional classification for the three years ended June 30, 2011 is as follows:

(in millions)	2011		2010		2009	
Operating:						
Instruction	$ 853.1	16%	$ 850.6	16%	$ 820.3	16%
Research	733.5	13	679.5	13	622.6	12
Public service	131.5	2	135.8	2	126.5	2
Institutional and academic support	486.3	9	485.0	9	485.2	10
Auxiliary enterprises:						
Patient care	2,285.2	42	2,182.7	42	2,112.4	42
Other	168.5	3	145.3	3	148.6	3
Operations and maintenance of plant	275.3	5	266.0	5	277.9	5
Depreciation	390.1	7	360.1	7	341.5	7
Scholarships and fellowships	114.3	2	113.8	2	107.1	2
	5,437.8	99	5,218.8	99	5,042.2	99
Nonoperating:						
Interest, net	26.0	1	26.7	1	25.1	1
	$ 5,463.8	100%	$ 5,245.6	100%	$ 5,067.2	100%

Instruction and public service expenses increased 4 percent, or $38 million, to $985 million in 2011, from $947 million in 2009. This increase is consistent with the modest level of growth in the related revenue sources offset by cost containment efforts.

To measure its total volume of research expenditures, the University considers research expenses, included in the above table, as well as research related facilities and administrative expenses, research initiative and start-up expenses and research equipment purchases. These amounts aggregated $1.2 billion in 2011, as compared to $1.1 billion in 2010 and $1.0 billion in 2009. This represents an increase of 22 percent, or $220 million, from 2009 to 2011 and includes the impact of stimulus funds from the American Recovery and Reinvestment Act of 2009.

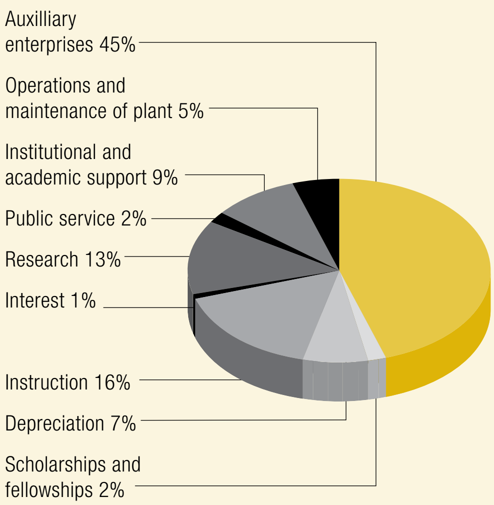
Patient-care expenses increased 8 percent, or $173 million, to $2.3 billion in 2011, from $2.1 billion in 2009. This increase is the result of increased patient activity, including costs of medical supplies and pharmaceuticals.

Total scholarships and fellowships provided to students aggregated $395 million in 2011, as compared to $365 million in 2010 and $327 million in 2009, an increase of 21 percent over the past two years. Tuition, housing and fees revenues are reported net of aid applied to students' accounts, while amounts paid directly to students are reported as scholarship and fellowship expense. Scholarships and fellowships for the three years ended June 30, 2011, are summarized as follows:

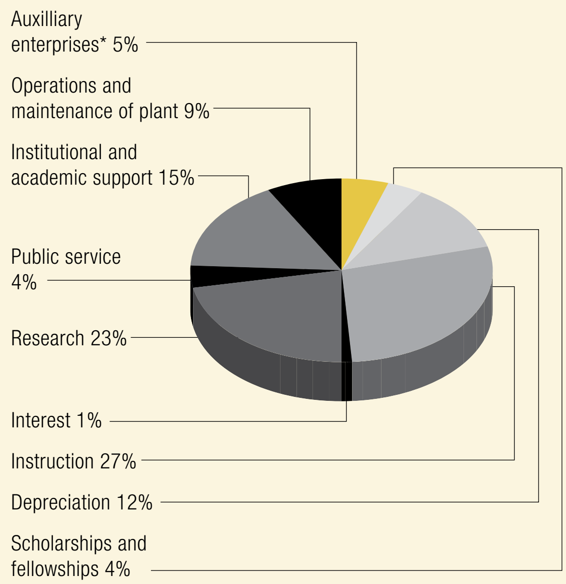
(in millions)	2011	2010	2009
Paid directly to students	$ 114.3	$ 113.8	$ 107.1
Applied to tuition and fees	262.2	233.6	202.9
Applied to University Housing	18.2	17.4	16.5
	$ 394.7	$ 364.8	$ 326.5

The following graphic illustrations present total expenses by function, with and without the University's Health System and other similar activities:

Fiscal Year 2011 Expenses by Function



Fiscal Year 2011 Expenses by Function Excluding Expenses from the University's Health System



*Excludes expenses from the University's Health System of $2.3 billion

Statement of Cash Flows

The statement of cash flows provides additional information about the University's financial results by reporting the major sources and uses of cash. A comparative summary of the statement of cash flows for the years ended June 30, 2011 and 2010 is as follows:

(in millions)	2011	2010
Cash received from operations	$ 4,806.5	$ 4,522.9
Cash expended for operations	(5,020.5)	(4,819.8)
Net cash used in operating activities	(214.0)	(296.9)
Net cash provided by investing activities	176.5	212.0
Net cash used in capital and related financing activities	(441.7)	(658.7)
Net cash provided by noncapital financing activities	601.1	579.8
Net increase (decrease) in cash and cash equivalents	121.9	(163.8)
Cash and cash equivalents, beginning of year	194.6	358.4
Cash and cash equivalents, end of year	$ 316.5	$ 194.6

Cash received from operations primarily consists of student tuition, sponsored program grants and contracts and patient care revenues. Significant sources of cash provided by noncapital financing activities, as defined by GASB, include state appropriations, state fiscal stabilization funds, federal Pell grants and private gifts used to fund operating activities.

Economic Factors That Will Affect the Future

The University continues to face significant financial challenges to its academic programs, stemming from the State's uncertain financial circumstances. Given the continuation of this difficult economic environment, it is noteworthy that the University maintains the highest credit ratings of Moody's (Aaa) and Standard & Poor's (AAA). Achieving and maintaining the highest credit ratings provides the University a high degree of flexibility in securing capital funds on the most competitive terms. This flexibility, along with ongoing efforts toward revenue diversification and cost containment, will enable the University to provide the necessary resources to support a consistent level of excellence in service to students, patients, the research community, the state and the nation.

A crucial element to the University's future continues to be a strong relationship with the state of Michigan. Historically, there has been a relationship between the growth, or reduction, of state support and the University's ability to control tuition increases. Over the past several years, the University has successfully addressed the realities of the state's difficult economy and, pursuant to a long-range plan, continues to work relentlessly to cut and mitigate operational costs in order to remain affordable and preserve access, while protecting the academic enterprise.

In fiscal 2012, the University faces a 15 percent, $54 million, reduction in state appropriations, the largest cut in state appropriations in the University's history. The Board of Regents has approved a budget for fiscal 2012 that fully absorbs this significant reduction in state appropriations while limiting the financial burden for students. Resident undergraduate tuition on the Ann Arbor campus will increase 6.7 percent and the University maintains a commitment to meet the full demonstrated financial need of resident undergraduate students with a 10.9 percent increase in centrally awarded financial aid for undergraduates. Resident undergraduate tuition on the Dearborn and Flint campuses will increase 6.9 percent and 6.8 percent, respectively. The University has been able to avoid the severe cuts and double-digit tuition increases experienced by institutions around the country because of its prudent long-term plan.

The University continues to execute its long-range plan to modernize and expand its complement of older facilities while adding key new facilities for instruction, research, patient care and residential life. This strategy addresses the University's growth and the continuing effects of technology on teaching, clinical and research activities. Authorized costs to complete construction and other projects totaled $623 million at June 30, 2011. Funding for these projects is anticipated to include $573 million from gifts, grants and net assets designated for capital purposes as well as future borrowings and $50 million from the utilization of unexpended debt proceeds. Economic pressures are expected to affect the State's future support.

The University's investment in the North Campus Research Complex is expected to result in significant economic benefits for both the University and the surrounding region by making strategic use of University resources and strengthening Michigan's life sciences industry. When fully developed, this complex could enable the University to create up to 3,000 new faculty and staff positions. Approximately 500 researchers and staff will move to the complex in 2012.

While the University's Hospitals and Health Centers are well positioned to maintain a strong financial position in the near term, ongoing constraints on revenue are expected due to fiscal pressures from employers and federal and state governments. Management believes that much of the payment pressure can be offset by growth in patient volume and continued efforts to contain certain costs.

The University will continue to employ its long-term investment strategy to maximize total returns, at an appropriate level of risk, while utilizing a spending rate policy to preserve endowment capital and insulate the University's operations from temporary market volatility.

As a labor-intensive organization, the University faces competitive pressures related to attracting and retaining faculty and staff. Moreover, consistent with the national landscape, the cost of the University's health benefits for its employees and retirees has increased dramatically over the past several years, with the increasing cost of medical care and prescription drugs of particular concern. To address these challenges, the University has successfully taken and will continue to take proactive steps to respond to the challenges of rising costs while protecting the quality of the overall benefit package.

U.S. health care reform will also influence benefits planning. Since the Affordable Care Act was signed into law in March 2010, new regulatory requirements will affect health plans, providers and employers alike. The implementation of the changes has begun and will span several years into the future, with most changes taking place by 2014. University experts are diligently reviewing and assessing the short and long-term impacts on our health plans and our health system to develop clear strategies and options for the future that will ensure compliance over the coming years of regulatory change. The University is also considering the benefits of a member engagement health plan design, which would include incentives for members to engage in health and well-being activities.

While it is not possible to predict the ultimate results, management believes that the University's financial condition will remain strong.

Financial Statements

Consolidated Statement of Net Assets

(in thousands)	June 30, 2011	2010
Assets		
Current Assets:		
Cash and cash equivalents	$ 316,534	$ 194,645
Operating investments	664,197	572,374
Investments for capital activities	369,687	305,386
Investments for student loan activities	50,162	41,033
Accounts receivable, net	452,611	461,622
Current portion of notes and pledges receivable, net	58,586	57,960
Current portion of prepaid expenses and other assets	82,435	52,468
Cash collateral held by agent	100,600	103,500
Total Current Assets	2,094,812	1,788,988
Noncurrent Assets:		
Endowment, life income and other investments	8,122,450	6,807,012
Notes and pledges receivable, net	194,359	211,642
Prepaid expenses and other assets	51,340	55,158
Capital assets, net	5,193,173	4,956,457
Total Noncurrent Assets	13,561,322	12,030,269
Total Assets	**$ 15,656,134**	**$ 13,819,257**
Liabilities and Net Assets		
Current Liabilities:		
Accounts payable	$ 167,153	$ 173,923
Accrued compensation and other	367,769	330,042
Deferred revenue	193,801	184,422
Current portion of insurance and benefits reserves	72,539	66,103
Current portion of obligations for postemployment benefits	53,638	51,629
Commercial paper and current portion of bonds payable	147,553	122,581
Long-term bonds payable subject to remarketing, net	274,895	384,550
Collateral held for securities lending	100,600	103,500
Deposits of affiliates and others	30,439	32,656
Total Current Liabilities	1,408,387	1,449,406
Noncurrent Liabilities:		
Accrued compensation	70,190	71,610
Insurance and benefits reserves	93,337	89,169
Obligations for postemployment benefits	1,583,014	1,556,479
Obligations under life income agreements	46,219	49,245
Government loan advances	90,904	88,555
Bonds payable	1,270,017	996,771
Deposits of affiliates and other	169,804	155,034
Total Noncurrent Liabilities	3,323,485	3,006,863
Total Liabilities	4,731,872	4,456,269
Net Assets:		
Invested in capital assets, net of related debt	3,574,878	3,502,716
Restricted:		
Nonexpendable	1,279,058	1,213,962
Expendable	3,467,232	2,810,016
Unrestricted	2,603,094	1,836,294
Total Net Assets	10,924,262	9,362,988
Total Liabilities and Net Assets	**$ 15,656,134**	**$ 13,819,257**

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE CONSOLIDATED FINANCIAL STATEMENTS.

Financial Statements

Consolidated Statement of Revenues, Expenses and Changes in Net Assets

(in thousands)	Year Ended June 30, 2011	2010
Operating Revenues		
Student tuition and fees	$ 1,177,897	$ 1,097,450
Less scholarship allowances	262,181	233,598
Net student tuition and fees	915,716	863,852
Federal grants and contracts	930,436	844,026
State and local grants and contracts	4,464	6,199
Nongovernmental sponsored programs	138,007	140,087
Sales and services of educational departments	124,235	139,992
Auxiliary enterprises:		
Patient care revenues (net of provision for bad debts of $89,466 in 2011 and $78,513 in 2010)	2,411,131	2,310,770
Student residence fees (net of scholarship allowances of $18,212 in 2011 and $17,441 in 2010)	90,232	85,725
Other revenues	160,727	143,666
Student loan interest income and fees	2,818	2,758
Total Operating Revenues	**4,777,766**	**4,537,075**
Operating Expenses		
Compensation and benefits	3,633,765	3,529,271
Supplies and services	1,299,651	1,215,684
Depreciation	390,071	360,089
Scholarships and fellowships	114,316	113,753
Total Operating Expenses	**5,437,803**	**5,218,797**
Operating loss	(660,037)	(681,722)
Nonoperating Revenues (Expenses)		
State educational appropriations	361,879	362,147
State fiscal stabilization funds		10,136
Federal Pell grants	46,669	39,905
Private gifts for other than capital and endowment purposes	127,751	105,167
Net investment income	1,632,968	796,399
Interest expense, net	(33,094)	(30,018)
Federal subsidies for interest on Build America Bonds	7,119	3,303
Total Nonoperating Revenues, Net	**2,143,292**	**1,287,039**
Income before other revenues (expenses)	1,483,255	605,317
Other Revenues (Expenses)		
State capital appropriations	843	2,002
Capital gifts and grants	24,907	29,143
Private gifts for permanent endowment purposes	57,451	59,595
Other	(5,182)	2,294
Total Other Revenues, Net	**78,019**	**93,034**
Increase in net assets	1,561,274	698,351
Net Assets, Beginning of Year	9,362,988	8,664,637
Net Assets, End of Year	**$ 10,924,262**	**$ 9,362,988**

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE CONSOLIDATED FINANCIAL STATEMENTS.

Consolidated Statement of Cash Flows

(in thousands)	Year Ended June 30, 2011	2010
Cash Flows from Operating Activities		
Student tuition and fees	$ 919,040	$ 866,513
Federal, state and local grants and contracts	932,002	838,436
Nongovernmental sponsored programs	136,619	134,956
Sales and services of educational departments and other	289,242	280,930
Patient care revenues	2,419,524	2,298,197
Student residence fees	90,448	85,768
Payments to employees	(2,772,856)	(2,678,274)
Payments for benefits	(814,083)	(800,175)
Payments to suppliers	(1,307,883)	(1,216,530)
Payments for scholarships and fellowships	(114,292)	(113,721)
Student loans issued	(11,460)	(11,016)
Student loans collected	16,847	15,280
Student loan interest and fees collected	2,818	2,758
Net Cash Used in Operating Activities	**(214,034)**	**(296,878)**
Cash Flows from Investing Activities		
Interest and dividends on investments, net	68,488	74,579
Proceeds from sales and maturities of investments	3,000,798	2,508,663
Purchases of investments	(2,785,120)	(2,438,641)
Net (increase) decrease in cash equivalents from noncurrent investments	(125,176)	59,090
Net increase in deposits of affiliates and others	17,541	8,328
Net Cash Provided by Investing Activities	**176,531**	**212,019**
Cash Flows from Capital and Related Financing Activities		
State capital appropriations	873	2,870
Private gifts and other receipts	35,395	39,488
Proceeds from issuance of capital debt	305,447	372,936
Principal payments on capital debt	(114,251)	(355,272)
Interest payments on capital debt, net of capitalized interest	(33,643)	(27,361)
Federal subsidies for Build America Bonds interest	6,296	2,062
Payments for bond refunding and related costs	(1,240)	(402)
Purchases of capital assets, including capitalized interest	(641,718)	(694,600)
Proceeds from sales of capital assets	1,129	1,594
Net Cash Used in Capital and Related Financing Activities	**(441,712)**	**(658,685)**
Cash Flows from Noncapital Financing Activities		
State educational appropriations	361,928	364,269
State fiscal stabilization funds	4,720	5,416
Federal Pell grants	46,669	39,705
Private gifts and other receipts	188,533	171,379
Student direct lending receipts	360,476	343,778
Student direct lending disbursements	(358,981)	(342,076)
Amounts received for annuity and life income funds	4,502	3,630
Amounts paid to annuitants and life beneficiaries and related expenses	(6,743)	(6,285)
Net Cash Provided by Noncapital Financing Activities	**601,104**	**579,816**
Net increase (decrease) in cash and cash equivalents	121,889	(163,728)
Cash and Cash Equivalents, Beginning of Year	194,645	358,373
Cash and Cash Equivalents, End of Year	**$ 316,534**	**$ 194,645**

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE CONSOLIDATED FINANCIAL STATEMENTS.

Financial Statements

Consolidated Statement of Cash Flows, continued

(in thousands)	Year Ended June 30, 2011	2010
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$ (660,037)	$ (681,722)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation expense	390,071	360,089
Changes in assets and liabilities:		
Accounts receivable, net	7,935	(22,156)
Prepaid expenses and other assets	(10,853)	(1,882)
Accounts payable	(335)	(1,817)
Accrued compensation and other	10,658	6,342
Deferred revenue	9,379	(3,097)
Insurance and benefits reserves	10,604	2,227
Obligations for postemployment benefits	28,544	45,138
Net cash used in operating activities	$ (214,034)	$ (296,878)

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE CONSOLIDATED FINANCIAL STATEMENTS.

Notes to Consolidated Financial Statements

June 30, 2011 and 2010

Note 1—Organization and Summary of Significant Accounting Policies

Organization and Basis of Presentation: The University of Michigan (the "University") is a state-supported institution with an enrollment of approximately 59,000 students on its three campuses. The financial statements include the individual schools, colleges and departments, the University of Michigan Hospitals and Health Centers, Michigan Health Corporation (a wholly-owned corporation created to pursue joint venture and managed care initiatives) and Veritas Insurance Corporation (a wholly-owned captive insurance company). While the University is a political subdivision of the state of Michigan, it is not a component unit of the State in accordance with the provisions of Governmental Accounting Standards Board ("GASB") Statement No. 14, *The Financial Reporting Entity*. The University is classified as a state instrumentality under Internal Revenue Code Section 115, and is also classified as a charitable organization under Internal Revenue Code Section 501(c)(3), and is therefore exempt from federal income taxes. Certain activities of the University may be subject to taxation as unrelated business income under Internal Revenue Code Sections 511 to 514.

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, as prescribed by GASB and the American Institute of Certified Public Accountants' Audit and Accounting Guide, *Audits of State and Local Governments*. The statements of net assets, revenues, expenses and changes in net assets and of cash flows are reported on a consolidated basis, and all intra-university transactions are eliminated as required by GASB. The University has the option of applying pronouncements issued by the Financial Accounting Standards Board ("FASB") after November 30, 1989, provided that such pronouncements do not conflict or contradict GASB pronouncements. The University has elected not to apply any FASB pronouncements issued after the applicable date.

The financial statements of all controlled organizations are included in the University's financial statements; affiliated organizations that are not controlled by, and not dependent on the University, such as booster and alumni organizations, are not included.

Net assets are categorized as:

- Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- Restricted:

  Nonexpendable—Net assets subject to externally imposed stipulations that they be maintained permanently. Such net assets include the corpus portion (historical value) of gifts to the University's permanent endowment funds and certain investment earnings stipulated by the donor to be reinvested permanently.

  Expendable—Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time. Such net assets include net appreciation of the University's permanent endowment funds that have not been stipulated by the donor to be reinvested permanently.
- Unrestricted: Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Regents. Substantially all unrestricted net assets are designated for academic and research programs and initiatives and capital programs.

Summary of Significant Accounting Policies: The accompanying financial statements have been prepared on the accrual basis. The University reports as a special purpose government entity engaged primarily in business type activities, as defined by GASB. Business type activities are those that are financed in whole or in part by fees charged to external parties for goods or services.

For purposes of the statement of cash flows, the University considers all highly liquid investments purchased with a maturity of three months or less, to be cash equivalents. Cash equivalents representing assets of the University's endowment, life income and other investments are included in noncurrent investments as these funds are not used for operating purposes.

Investments are reported in four categories in the statement of net assets. Investments reported as endowment, life income and other investments are those funds invested in portfolios that are considered by management to be of a long duration. Investments for student loan and capital activities are those funds that are intended to be used for these specific activities. All other investments are reported as operating investments.

Investments in marketable securities are carried at fair value, as established by the major securities markets. Purchases and sales of investments are accounted for on the trade date basis. Investment income is recorded on the accrual basis. Realized and unrealized gains and losses are reported in investment income.

Investments in nonmarketable limited partnerships are generally carried at fair value provided by the management of the investment partnerships as of March 31, 2011 and 2010, as adjusted by cash receipts, cash disbursements and securities distributions through June 30, 2011 and 2010, in order to provide an approximation of fair value at June 30. In addition, the carrying amount of these investments is adjusted for June 30 information from management of the investment partnerships when necessary to provide a reasonable estimate of fair value as of June 30, 2011 and 2010. Because these investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investments existed and such differences could be material.

Derivative instruments, such as financial futures, forward foreign exchange contracts and interest rate swaps held in investment portfolios, are recorded on the contract date and are carried at fair value using listed price quotations or amounts that approximate fair value. To facilitate trading in financial futures, the University is required to post cash or securities to satisfy margin requirements of the exchange where such futures contracts are listed. The University monitors the required amount of cash and securities on deposit for financial futures transactions and withdraws or deposits cash or securities as necessary.

Investments denominated in foreign currencies are translated into U.S. dollar equivalents using year-end spot foreign currency exchange rates. Purchases and sales of investments denominated in foreign currencies and related income are translated at spot exchange rates on the transaction dates.

Accounts receivable are recorded net of a provision for uncollectible accounts receivable. The provision is based on management's judgment of potential uncollectible amounts, which includes such factors as historical experience and type of receivable.

The University receives pledges and bequests of financial support from corporations, foundations and individuals. Revenue is recognized when a pledge representing an unconditional promise to pay is received and all eligibility requirements, including time requirements, have been met. In the absence of such a promise, revenue is recognized when the gift is received. Permanent endowment pledges do not meet eligibility requirements, as defined by GASB, and are not recorded as assets until the related gift is received.

Unconditional promises to give that are expected to be collected in future years are recorded at the present value of the estimated future cash flows. The discounts on these amounts are computed using risk-free interest rates applicable to the years in which the promises are made, commensurate with expected future payments. An allowance for uncollectible pledges receivable is provided based on management's judgment of potential uncollectible amounts. The determination includes such factors as prior collection history, type of gift and nature of fundraising.

Capital assets are recorded at cost or, if donated, at appraised value at the date of donation. Depreciation of capital assets is provided on a straight-line basis over the estimated useful lives of the respective assets, which primarily range from four to 40 years. The University does not capitalize works of art or historical treasures that are held for exhibition, education, research or public service. These collections are neither disposed of for financial gain nor encumbered in any means. Accordingly, such collections are not recognized or capitalized for financial statement purposes.

Deferred revenue consists primarily of cash received from grant and contract sponsors which has not yet been earned under the terms of the agreement. Deferred revenue also includes amounts received in advance of an event, such as student tuition and advance ticket sales related to future fiscal years.

Deposits of affiliates and others represent cash and invested funds held by the University as a result of agency relationships with various groups. Noncurrent deposits of affiliates represent the portion of endowment and similar funds held by the University on behalf of others.

The University holds life income funds for beneficiaries of the pooled income fund, charitable remainder trusts and the gift annuity program. These funds generally pay lifetime income to beneficiaries, after which the principal is made available to the University in accordance with donor intentions. All life income fund assets, including those held in trust, are recorded at fair value. The present value of estimated future payments due to life income beneficiaries is recorded as a liability.

For donor restricted endowments, the Uniform Prudent Management of Institutional Funds Act, as adopted in Michigan, permits the Board of Regents to appropriate amounts for endowment spending rule distributions as is considered prudent. The University's policy is to retain net realized and unrealized appreciation with the endowment after spending rule distributions. Net appreciation of permanent endowment funds, which totaled $1,312,000,000 and $924,000,000 at June 30, 2011 and 2010, respectively, is recorded in restricted expendable net assets. The University's endowment spending rule is further discussed in Note 2.

Student tuition and residence fees are presented net of scholarships and fellowships applied to student accounts, while stipends and other payments made directly to students are presented as scholarship and fellowship expenses.

Patient care revenues are reported net of contractual allowances and bad debt expenses. Patient care services are primarily provided through the University of Michigan Health System, which includes the Hospitals and Health Centers, the Faculty Group Practice of the University of Michigan Medical School and the Michigan Health Corporation. Patient care services are also provided through University Health Services, which provides health care services to students, faculty and staff and Dental Faculty Associates, which provides dental care services performed by faculty dentists.

Other auxiliary enterprise revenues primarily represent revenues generated by intercollegiate athletics, parking, student unions, university press and student publications.

The University's policy for defining operating activities as reported on the statement of revenues, expenses and changes in net assets are those that generally result from exchange transactions such as payments received for providing services and payments made for services or goods received. Nearly all of the University's expenses are from exchange transactions. Certain significant revenue streams relied upon for operations are recorded as nonoperating revenues, as defined by GASB, including state appropriations, state fiscal stabilization funds, federal Pell grants, gifts and investment income.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The most significant areas that require management estimates relate to self-insurance and benefits obligations.

Reclassifications: Certain prior year amounts have been reclassified to conform with current year presentations.

Note 2—Cash and Investments

Summary: The University maintains centralized management for substantially all of its cash and investments. With the exception of certain insurance reserves, charitable remainder trusts and other funds whose terms require separate management, the University invests its cash reserves and relatively short duration assets in the University Investment Pool ("UIP"). The University also collectively invests substantially all of the assets of its endowment funds (University Endowment Fund) together with a portion of its insurance and benefits reserves, charitable remainder trusts and gift annuity program in the Long Term Portfolio.

The UIP is invested together with the University's insurance and other benefits reserves in the Daily and Monthly Portfolios, which are principally invested in investment-grade money market securities, U.S. government and other fixed income securities and absolute return strategies. Balances in the UIP are primarily for operating expenses and capital projects. The funding for capital projects remains in current operating investments until amounts for specific capital projects are transferred for capital activities.

The longer investment horizon of the Long Term Portfolio allows for an equity-oriented strategy to achieve higher expected returns over time, and permits the use of less liquid alternative investments, providing for equity diversification beyond the stock markets. The Long Term Portfolio includes investments in domestic and non-U.S. stocks and bonds, commingled funds and limited partnerships consisting of venture capital, private equity, real estate, energy and absolute return strategies.

Authorizations: The University's investment policies are governed and authorized by University Bylaws and the Board of Regents. The approved asset allocation policy for the Long Term Portfolio sets a general target of 80 percent equities and 20 percent fixed income securities, within a permitted range of 65 to 90 percent for equities and 10 to 35 percent for fixed income securities. Since diversification is a fundamental risk management strategy, the Long Term Portfolio is broadly diversified within these general categories.

The endowment spending rule provides for distributions from the University Endowment Fund to the University entities that benefit from the endowment fund. Commencing with the quarter ending September 30, 2010, the annual distribution rate began to be reduced from 5 percent of the one-quarter lagged seven year moving average fair value of fund shares to 4.5 percent. Distributions are being managed toward the new rate by keeping quarter to quarter distributions per share unchanged and moving toward the 4.5 percent rate when increases in the value of fund shares would otherwise result in higher per share distributions. To protect endowment principal in the event of a prolonged market downturn, distributions are limited to 5.3 percent of the current fair value of fund shares. Distributions are also made from the UIP to University entities based on the 90-day U.S. Treasury Bill rate. The University's costs to administer and grow the University Endowment Fund and UIP are funded by investment returns.

Cash and Cash Equivalents: Cash and cash equivalents, which totaled $316,534,000 and $194,645,000 at June 30, 2011 and 2010, respectively, represent short-term money market investments in mutual funds, overnight collective funds managed by the University's custodian or short-term highly liquid investments registered as securities and held by the University or its agents in the University's name. Of its cash and cash equivalents, the University had actual cash balances in its bank accounts in excess of Federal Deposit Insurance Corporation ("FDIC") limits in the amount of $50,000 and $6,838,000 at June 30, 2011 and 2010, respectively. Under FDIC rules implemented during 2011, the University's noninterest-bearing transaction accounts have temporarily unlimited insurance coverage through December 31, 2012. The University does not require deposits to be collateralized or insured.

Investments: At June 30, 2011 and 2010, the University's investments, which are held by the University or its agents in the University's name, are summarized as follows:

(in thousands)	2011	2010
Cash equivalents, noncurrent	$ 247,650	$ 122,474
Fixed income securities	1,435,082	1,372,232
Commingled funds	1,571,478	1,379,961
Equity securities	1,002,151	819,510
Nonmarketable alternative investments	4,941,887	4,024,853
Other investments	8,248	6,775
	$ 9,206,496	$ 7,725,805

The University's investment strategy, like that of most other institutions, incorporates certain financial instruments that involve, to varying degrees, elements of market risk and credit risk in excess of amounts recorded in the financial statements. Market risk is the potential for changes in the value of financial instruments due to market changes, including interest and foreign exchange rate movements and fluctuations embodied in forwards, futures and commodity or security prices. Market risk is directly impacted by the volatility and liquidity of the markets in which the underlying assets are traded. Credit risk is the possibility that a loss may occur due to the failure of a counterparty to perform according to the terms of the contract. The University's risk of loss in the event of a counterparty default is typically limited to the amounts recognized in the statement of net assets and is not represented by the contract or notional amounts of the instruments.

Fixed income securities have inherent financial risks, including credit risk and interest rate risk. Credit risk for fixed income securities is the risk that the issuer will not fulfill its obligations. Nationally recognized statistical rating organizations ("NSROs"), such as Moody's and Standard & Poor's, assign credit ratings to security issues and issuers that indicate a measure of potential credit risk to investors. Fixed income securities considered investment grade are those rated at least Baa by Moody's and BBB by Standard & Poor's. To manage credit risk, the University specifies minimum average and minimum absolute quality NSRO ratings for securities held pursuant to its management agreements.

The University minimizes concentration of credit risk, the risk of a large loss attributed to the magnitude of the investment in a single issuer of fixed income securities, by diversifying its fixed income issues and issuers and holding U.S. Treasury securities which are considered to have minimal credit risk. The University also manages this risk at the account level by limiting each fixed income manager's holding of any non-U.S. government issuer to 5 percent of the value of the investment account.

Note 2—Cash and Investments, continued

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of fixed income securities. Effective duration, a commonly used measure of interest rate risk, incorporates a security's yield, coupon, final maturity, call features and other embedded options into one number expressed in years that indicates how price-sensitive a security or portfolio of securities is to changes in interest rates. The effective duration of a security or portfolio indicates the approximate percentage change in fair value expected for a one percent change in interest rates. The longer the duration, the more sensitive the security or portfolio is to changes in interest rates. The weighted average effective duration of the University's fixed income securities was 5.0 years at June 30, 2011, compared to 5.1 years at June 30, 2010. The University manages the effective duration of its fixed income securities at the account level, where fixed income managers generally may not deviate from the duration of their respective benchmarks by more than 25 percent.

The composition of fixed income securities at June 30, 2011 and 2010, along with credit quality and effective duration measures, is summarized as follows:

2011

(in thousands)	U.S. Government	Investment Grade	Non-Investment Grade	Not Rated	Total	Duration (in years)
U.S. Treasury	$ 96,076				$ 96,076	7.3
U.S. Treasury inflation protected	324,503				324,503	4.2
U.S. government agency	226,764				226,764	0.7
Mortgage backed		$ 27,941	$ 21,144		49,085	0.9
Asset backed		32,527	1,036		33,563	1.2
Corporate and other		677,307	17,525	$ 10,259	705,091	7.0
	$ 647,343	$ 737,775	$ 39,705	$ 10,259	$ 1,435,082	5.0

2010

(in thousands)	U.S. Government	Investment Grade	Non-Investment Grade	Not Rated	Total	Duration (in years)
U.S. Treasury	$ 92,098				$ 92,098	8.7
U.S. Treasury inflation protected	309,926				309,926	3.7
U.S. government agency	178,941				178,941	0.6
Mortgage backed		$ 24,696	$ 19,930		44,626	1.8
Asset backed		40,857	3,676		44,533	2.9
Corporate and other		680,954	13,235	$ 7,919	702,108	6.8
	$ 580,965	$ 746,507	$ 36,841	$ 7,919	$ 1,372,232	5.1

Of the University's fixed income securities, 97 percent were rated investment grade or better at June 30, 2011 and 2010, with 52 percent and 48 percent of these securities rated AAA/Aaa or better at June 30, 2011 and 2010, respectively.

Commingled (pooled) funds include Securities and Exchange Commission regulated mutual funds and externally managed funds, limited partnerships and corporate structures which are generally unrated and unregulated. Certain commingled funds may use derivatives, short positions and leverage as part of their investment strategy. These investments are structured to limit the University's risk exposure to the amount of invested capital. The composition of commingled funds at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Absolute return	$ 764,844	$ 700,300
U.S. equities	101,890	77,588
Non-U.S./global equities	681,154	585,743
U.S. fixed income	15,123	8,607
Other	8,467	7,723
	$ 1,571,478	$ 1,379,961

Commingled funds have liquidity (redemption) provisions, which enable the University to make full or partial withdrawals with notice, subject to restrictions on the timing and amount. Of the University's commingled funds at June 30, 2011 and 2010, approximately 76 percent and 80 percent are redeemable within one year, with 51 percent redeemable within 90 days for both years under normal market conditions. The remaining amounts are redeemable beyond one year, with redemption of certain funds dependent on disposition of the underlying assets.

Nonmarketable alternative investments consist of limited partnerships and similar vehicles involving an advance commitment of capital called by the general partner as needed and distributions of capital and return on invested capital as underlying strategies are concluded during the life of the partnership. There is no active secondary market for these alternative investments, which are generally unrated and unregulated, and the liquidity of these investments is dependent on actions taken by the general partner. The composition of these partnerships at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Private equity	$ 1,326,341	$ 1,085,145
Real estate	1,026,564	811,071
Absolute return	845,500	828,903
Energy	806,915	705,180
Venture capital	936,567	594,554
	$ 4,941,887	$ 4,024,853

The University's limited partnership investments are diversified in terms of manager selection and industry and geographic focus. At June 30, 2011 and 2010, no individual partnership investment represented 5 percent or more of total investments. The University's committed but unpaid obligation to these limited partnerships is further discussed in Note 13.

Absolute return strategies in the commingled funds and nonmarketable alternative investments classifications include long/short stock programs, merger arbitrage, intra-capital structure arbitrage and distressed debt investments. The goal of absolute return strategies is to provide, in aggregate, a return that is consistently positive and uncorrelated with the overall market.

The University participates in non-U.S. developed and emerging markets through commingled funds invested in non-U.S./global equities and absolute return strategies. Although substantially all of 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 the investment returns. In addition, a portion of the University's equity securities and nonmarketable alternative investments are denominated in foreign currencies, which must be settled in local (non-U.S.) currencies. Forward foreign currency contracts are typically used to manage the risk related to fluctuations in currency exchange rates between the time of purchase or sale and the actual settlement of foreign securities. Various investment managers acting for the University also use forward foreign exchange contracts in risk-based transactions to carry out their portfolio strategies.

Foreign exchange risk is the risk that investments denominated in foreign currencies may lose value due to adverse fluctuations in the value of the U.S. dollar relative to foreign currencies. The value of the University's non-U.S. dollar holdings net of outstanding forward foreign exchange contracts at June 30, 2011 and 2010 totaled $1,224,168,000, or 13 percent of total investments and $906,342,000, or 12 percent of total investments, respectively, and is summarized as follows:

(in thousands)	2011	2010
Euros	$ 642,096	$ 419,172
British pounds sterling	175,837	125,487
Canadian dollar	104,274	28,938
Japanese yen	60,682	83,596
Other	241,279	249,149
	$ 1,224,168	$ 906,342

The University manages foreign exchange risk through the use of forward foreign currency contracts and manager agreements that provide minimum diversification and maximum exposure limits by country and currency.

The Daily and Monthly Portfolios held positions in bond futures at June 30, 2011 and 2010. Bond futures are used to adjust the duration of cash equivalents and the fixed income portion of the portfolios. To meet trading margin requirements, the University had U.S. government securities and cash with a fair value of $5,016,000 and $4,422,000 at June 30, 2011 and 2010, respectively, on deposit with its futures contract broker as collateral.

The Long Term Portfolio and the Monthly Portfolio participate in a short-term, fully collateralized, securities lending program administered by the University's master custodian. Together, the Portfolios had $103,600,000 and $115,500,000 in securities loans outstanding at June 30, 2011 and 2010, respectively. At loan inception, an approved borrower must deliver collateral of cash, securities or letters of credit to the University's lending agent equal to 102 percent of fair value for domestic securities and 105 percent for foreign securities. Collateral positions are monitored daily to ensure that borrowed securities are never less than 100 percent collateralized. At June 30, 2011, collateral of $107,900,000 (104 percent of securities on loan) includes invested cash of $100,600,000, University payables of $7,100,000 and U.S. government securities of $200,000, while at June 30, 2010, collateral of $119,800,000 (104 percent of securities on loan) includes invested cash of $103,500,000, University payables of $7,500,000 and U.S. government securities of $8,800,000. Cash collateral held by the University's lending agent, along with the offsetting liability to return the collateral at loan termination, are recorded in the statement of net assets. To conform with current year presentation, the 2010 statement of net assets has been revised to reflect the recording of these items. Neither the University nor its securities lending agent has the ability to pledge or sell securities received as collateral unless a borrower defaults; accordingly, noncash collateral is not recorded in the statement of net assets. Securities loans may be terminated upon notice by either the University or the borrower.

Note 3—Accounts Receivable

The composition of accounts receivable at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Patient care	$ 430,378	$ 436,818
Sponsored programs	80,997	82,464
State appropriations, educational and capital	65,796	65,875
Student accounts	22,858	21,626
Other	40,234	35,999
	640,263	642,782
Less provision for uncollectible accounts receivable	187,652	181,160
	$ 452,611	$ 461,622

Note 4—Notes and Pledges Receivable

The composition of notes and pledges receivable at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Notes:		
Federal student loan programs	$ 89,271	$ 94,432
University student loan funds	21,012	20,756
Other	542	734
	110,825	115,922
Less allowance for doubtfully collectible notes	3,100	2,800
Total notes receivable, net	107,725	113,122
Gift pledges outstanding:		
Capital	102,246	112,790
Operations	60,680	61,764
	162,926	174,554
Less:		
Allowance for doubtfully collectible pledges	9,643	6,925
Unamortized discount to present value	8,063	11,149
Total pledges receivable, net	145,220	156,480
Total notes and pledges receivable, net	252,945	269,602
Less current portion	58,586	57,960
	$ 194,359	$ 211,642

The principal repayment and interest rate terms of federal and university loans vary considerably. The allowance for doubtfully collectible notes only applies to University funded notes and the University portion of federal student loans, as the University is not obligated to fund the federal portion of uncollected student loans. Federal loan programs are funded principally with federal advances to the University under the Perkins and various health professions loan programs.

Payments on pledges receivable at June 30, 2011, are expected to be received in the following years ended June 30 (in thousands):

2012	$ 49,552
2013-2016	89,772
2017 and after	23,602
	$ 162,926

As discussed in Note 1, permanent endowment pledges do not meet eligibility requirements, as defined by GASB, until the related gift is received. Accordingly, permanent endowment pledges totaling approximately $59,374,000 and $68,580,000 at June 30, 2011 and 2010, respectively, are not recognized as assets in the accompanying financial statements. In addition, bequest intentions and other conditional promises are not recognized as assets until the specified conditions are met because of uncertainties with regard to their realizability and valuation.

Note 5—Capital Assets

Capital assets activity for the years ended June 30, 2011 and 2010 is summarized as follows:

2011

(in thousands)	Beginning Balance	Additions	Retirements	Ending Balance
Land	$ 93,964	$ 401		$ 94,365
Land improvements	102,274	4,961	$ 386	106,849
Infrastructure	213,772	3,819		217,591
Buildings	5,862,797	224,893	65,719	6,021,971
Construction in progress	545,595	279,312		824,907
Property held for future use	84,339	(30,516)		53,823
Equipment	1,623,287	128,267	122,840	1,628,714
Library materials	449,842	23,572		473,414
	8,975,870	634,709	188,945	9,421,634
Less accumulated depreciation	4,019,413	390,071	181,023	4,228,461
	$ 4,956,457	$ 244,638	$ 7,922	$ 5,193,173

2010

(in thousands)	Beginning Balance	Additions	Retirements	Ending Balance
Land	$ 89,217	$ 4,747		$ 93,964
Land improvements	97,743	4,857	$ 326	102,274
Infrastructure	200,271	13,501		213,772
Buildings	5,112,648	760,634	10,485	5,862,797
Construction in progress	786,480	(240,885)		545,595
Property held for future use	114,029	(29,690)		84,339
Equipment	1,509,299	160,590	46,602	1,623,287
Library materials	428,609	21,522	289	449,842
	8,338,296	695,276	57,702	8,975,870
Less accumulated depreciation	3,710,798	360,089	51,474	4,019,413
	$ 4,627,498	$ 335,187	$ 6,228	$ 4,956,457

The increase in construction in progress of $279,312,000 in 2011 represents the amount of capital expenditures for new projects of $562,924,000 net of capital assets placed in service of $283,612,000. The decrease in construction in progress of $240,885,000 in 2010 represents the amount of capital assets placed in service of $845,404,000 net of capital expenditures for new projects of $604,519,000. Interest of $17,599,000 and $5,640,000 was capitalized in 2011 and 2010, respectively.

Property held for future use represents the unoccupied portion of the North Campus Research Complex. The University acquired this property in June 2009 for $114,029,000, including liabilities assumed in the purchase. During 2011 and 2010, $30,516,000 and $29,690,000, respectively, of the acquired property was placed in service.

Note 6—Long-term Debt

Long-term debt at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Commercial Paper:		
Tax-exempt, variable rate (.20%)*	$ 85,450	$ 81,110
Taxable, variable rate (.22%)*	5,740	6,095
General Revenue Bonds:		
Series 2010A, taxable–Build America Bonds, 4.926% to 5.593% through 2040	163,110	163,110
Series 2010C, 2.00% to 5.00% through 2027	183,240	184,225
unamortized premium	15,997	17,635
Series 2010D, taxable–Build America Bonds, 1.051% to 5.333% through 2041	212,345	
Series 2010E, 5.00% through 2012	7,200	
unamortized premium	324	
Series 2009A, 2.00% to 5.00% through 2029	91,020	95,310
Series 2009B, variable rate (.23%)* through 2039	118,710	118,710
unamortized premium	7,189	7,668
Series 2009D, taxable–Build America Bonds, 5.155% to 6.172% through 2030	89,815	89,815
Series 2008A, variable rate (.03%)* through 2038	105,810	105,810
Series 2008B, variable rate (.03%)* to fixed via swap through 2026 and variable rate 2027 through 2028	111,865	115,205
Series 2005A, 5.00% through 2018	22,060	26,345
unamortized premium	1,054	1,472
unamortized loss on extinguishment	(118)	(175)
Series 2002, variable rate (.06%)* to fixed via swap through 2018 and variable rate 2019 through 2032	100,715	106,775
General Revenue Refunding Bonds:		
Series 2003, 3.50% to 5.00% through 2015	11,825	18,000
unamortized premium	310	614
unamortized loss on extinguishment	(51)	(106)
Hospital Revenue Bonds:		
Series 2007A, variable rate (.03%)* through 2038	26,195	26,195
Series 2007B, variable rate (.05%)* through 2038	44,310	44,310
Series 2005A, variable rate (.03%)* through 2036	69,315	69,315
Series 2005B, variable rate (.05%)* to fixed via swap through 2026	65,360	68,705
Hospital Revenue Refunding Bonds:		
Series 2002A, 5.00% to 5.25% through 2022	45,990	47,585
unamortized premium	405	672
unamortized loss on extinguishment	(1,482)	(1,755)
Series 1998A-2, variable rate (.03%)* to fixed via swap through 2025	44,670	44,670
Medical Service Plan Revenue Bonds:		
Series 1995A, variable rate (.04%)* through 2028	26,200	26,200
Series 1991, 7.05% capital appreciation through 2012	2,120	4,099
Medical Service Plan Revenue Refunding Bonds:		
Series 1998A-1, variable rate (.03%)* to fixed via swap through 2022	33,980	34,345
Housing Energy Conservation HUD Loan, 3.00% through 2021	1,792	1,943
	1,692,465	1,503,902
Less:		
Commercial paper and current portion of bonds payable	147,553	122,581
Long-term bonds payable subject to remarketing, net	274,895	384,550
	$ 1,270,017	$ 996,771

*Denotes variable rate at June 30, 2011

The variable rate portions of bonds payable have remarketing features which allow bondholders to put debt back to the University. Accordingly, variable rate bonds payable are classified as current unless supported by long-term liquidity agreements, such as lines of credit or standby bond purchase agreements, which can refinance the debt on a long-term basis. The classification of the University's variable rate bonds payable at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	**2011**	**2010**
Variable rate bonds payable subject to remarketing	$ 747,130	$ 760,240
Less:		
Current principal maturities	14,725	13,110
Long-term liquidity agreements:		
Unsecured lines of credit	150,000	150,000
Standby bond purchase agreements	307,510	212,580
Long-term bonds payable subject to remarketing, net	$ 274,895	$ 384,550

The University's available line of credit and standby bond purchase agreements, which expire between August 2012 and July 2013, were entirely unused at June 30, 2011.

In connection with certain issues of variable rate debt, the University has entered into various floating-to-fixed interest rate swaps to convert all or a portion of the associated variable rate debt to synthetic fixed rates to protect against the potential of rising interest rates. The fair value, significant terms and other information about the University's interest rate swaps are discussed in Note 7.

Long-term debt activity, and the type of revenue it is supported by, for the year ended June 30, 2011, is summarized as follows:

(in thousands)	Beginning Balance	Additions	Reductions	Ending Balance
Commercial Paper:				
General revenues	$ 87,205	$ 85,450	$ 81,465	$ 91,190
Bonds and Notes:				
General revenues	1,050,413	219,997	27,990	1,242,420
Hospital revenues	299,697		4,934	294,763
Faculty Group Practice revenues	64,644	216	2,560	62,300
Student residences revenues	1,943		151	1,792
	$ 1,503,902	$ 305,663	$ 117,100	$ 1,692,465

The University maintains a combination of variable and fixed rate debt, with effective interest rates that averaged approximately 2.5 percent and 2.0 percent in 2011 and 2010, respectively, including the amortization of bond premiums and discounts and net of federal subsidies for interest on taxable Build America Bonds. The University utilizes commercial paper to provide interim financing for its capital improvement program. The Board of Regents has authorized the issuance of up to $200,000,000 in commercial paper backed by a general revenue pledge. Outstanding commercial paper debt is converted to long-term debt financing, as appropriate, within the normal course of business.

During 2011, the University issued $219,545,000 of General Revenue Bonds with a net original issue premium of $452,000. Total bond proceeds of $219,997,000 were utilized to provide $218,757,000 for capital projects and $1,240,000 for debt issuance costs. General Revenue Bonds issued in 2011 include $212,345,000 of fixed rate taxable Build America Bonds (Series 2010D) and $7,200,000 of fixed rate tax-exempt bonds (Series 2010E).

Note 6—Long-term Debt, continued

During 2010, General Revenue Bonds issued include $163,110,000 of fixed rate taxable Build America Bonds (Series 2010A) and $184,225,000 of fixed rate tax-exempt bonds (Series 2010C). Variable rate bonds refunded with proceeds from this debt issuance include $100,000,000 of Series 1995A Hospital Revenue Bonds, $23,925,000 of Series 2007A Hospital Revenue Bonds, $55,925,000 of Series 2007B Hospital Revenue Bonds and $21,400,000 of Series 1995A Medical Service Plan Revenue Bonds. In 2010, the University also refunded $46,070,000 of variable rate Series 2005B General Revenue Bonds, utilizing a portion of proceeds from the Series 2009A (fixed rate) and Series 2009B (variable rate) General Revenue Bonds issued in 2009, and extinguished $56,000,000 of variable rate Series 1992A Hospital Revenue Refunding Bonds.

Debt obligations are generally callable by the University and mature at various dates through fiscal 2041. Principal maturities and interest on debt obligations, based on scheduled bond maturities, for the next five years and in subsequent five-year periods are as follows:

(in thousands)	Principal	Interest*	Total
2012	$ 144,706	$ 39,852	$ 184,558
2013	61,896	38,122	100,018
2014	50,186	36,886	87,072
2015	51,381	35,871	87,252
2016	47,876	34,780	82,656
2017-2021	257,282	155,768	413,050
2022-2026	302,155	117,440	419,595
2027-2031	295,660	71,766	367,426
2032-2036	283,025	40,860	323,885
2037-2041	174,670	14,758	189,428
	1,668,837	$ 586,103	$ 2,254,940
Plus unamortized premiums, net	23,628		
	$ 1,692,465		

*Interest on variable rate debt is estimated based on rates in effect at June 30, 2011; amounts do not reflect federal subsidies to be received for Build America Bonds interest

If all variable rate bonds were put back to the University and existing unsecured lines of credit and standby bond purchase agreements were not extended upon their current expiration dates, the total principal payments due in 2012 would increase to $419,601,000, total principal payments due in 2013 would increase to $262,691,000 and total principal payments due in 2014 would increase to $270,871,000. Accordingly, principal payments due in subsequent years would be reduced to $32,161,000 in 2015; $27,811,000 in 2016; $153,297,000 in 2017 through 2021; $163,825,000 in 2022 through 2026; $158,235,000 in 2027 through 2031; $86,780,000 in 2032 through 2036; and $93,565,000 in 2037 through 2041. There would not be a significant impact on annual interest payments due to the low variable rate of interest on these bonds.

Note 7—Derivative Instruments

Derivatives held by the University are recorded at fair value in the statement of net assets in accordance with GASB Statement No. 53, Accounting and Financial Reporting for Derivative Instruments. For hedging derivative instruments that are effective in significantly reducing an identified financial risk, as defined by the Statement, the corresponding change in fair value is deferred and included in the statement of net assets. For all other derivative instruments, changes in fair value are reported as net investment income (loss).

Derivative instruments held by the University at June 30, 2011 and 2010 are summarized as follows:

(in thousands)	2011 Notional Amount	2011 Fair Value	2010 Notional Amount	2010 Fair Value
Investment Derivative Instruments:				
Investment portfolios:				
Futures	$ 393,232	$ 54	$ 284,993	$ 3,058
Foreign currency forwards	772,286	2,085	368,749	(3,254)
Other	81,045	(198)	71,522	(744)
	$ 1,246,563	$ 1,941	$ 725,264	$ (940)
Floating-to-fixed interest rate swap on debt	$ 46,085	$ (2,468)	$ 52,145	$ (3,266)
Effective Cash Flow Hedges:				
Floating-to-fixed interest rate swaps on debt	$ 239,160	$ (28,612)	$ 246,210	$ (32,658)

The University utilizes bond futures in its investment portfolios to adjust the duration of cash equivalents and fixed income securities, while foreign currency forward contracts are utilized to settle securities and transactions denominated in foreign (non-U.S. dollar) currencies and manage foreign exchange risk. Other derivative instruments in the University's investment portfolios consist primarily of interest rate swaps, credit default swaps, total return swaps and forward security purchase or sale commitments and are used to carry out investment and portfolio strategies.

In connection with certain issues of variable rate debt, the University has entered into various floating-to-fixed interest rate swaps to convert all or a portion of the associated variable rate debt to synthetic fixed rates to protect against the potential of rising interest rates. The fair value represents the estimated amount that the University would pay to terminate the swap agreements at the statement of net assets date, taking into account current interest rates and creditworthiness of the underlying counterparty. The notional amount represents the underlying reference of the instrument and does not represent the amount of the University's settlement obligations.

In accordance with GASB Statement No. 53, an interest rate swap is considered an effective cash flow hedge if the swap payments received substantially offset the payments made on the associated debt and changes in fair value are deferred. An interest rate swap that is not considered an effective cash flow hedge, in accordance with the provisions of this Statement, is deemed to be an investment derivative instrument and changes in fair value are recorded as net investment income (loss).

At June 30, 2011 and 2010, the fair value of floating-to-fixed interest rate swaps associated with the University's variable rate debt is a liability of $31,080,000 and $35,924,000, respectively, and is included in the statement of net assets as part of noncurrent other liabilities. The majority of the University's interest rate swaps qualify as effective hedges as defined by GASB Statement No. 53. The corresponding deferred asset for the fair value of swaps deemed effective cash flow hedges totaled $28,612,000 and $32,658,000, at June 30, 2011 and 2010, respectively.

Note 7—Derivative Instruments, continued

The change in fair value of derivative instruments, which includes realized gains and losses on positions closed, for the years ended June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Investment Derivative Instruments:		
Investment portfolios:		
Futures	$ 12,026	$ 19,320
Foreign currency forwards	3,378	8,458
Other	762	(717)
	$ 16,166	$ 27,061
Floating-to-fixed interest rate swap on debt	$ 798	$ (927)
Effective Cash Flow Hedges:		
Floating-to-fixed interest rate swaps on debt	$ 4,046	$ (9,359)

The University's interest rate swaps, along with their associated variable rate debt and significant terms, are summarized below.

The floating-to-fixed interest rate swap associated with the Series 2008B General Revenue Bonds has a notional amount of $95,150,000 and $98,490,000 at June 30, 2011 and 2010, respectively, covering a portion of the principal outstanding and the notional amount decreases as principal on the underlying bonds is repaid. Effective from April 1, 2008, the University makes payments based on a fixed rate of 3.105 percent and receives variable rate payments from the swap counterparty based on 68 percent of One-Month USD LIBOR, until the swap terminates in April 2026. The University has the option to terminate the swap upon five business day written notice and payment of the fair market compensation for the value of the swap. This swap is considered an effective hedge at June 30, 2011 and 2010 and has a fair value of ($7,607,000) and ($9,187,000), respectively.

The floating-to-fixed interest rate swap associated with the Series 2005B Hospital Revenue Bonds has a notional amount of $65,360,000 and $68,705,000 at June 30, 2011 and 2010, respectively, tied to the outstanding balance of the bonds. Effective from December 1, 2005, the University makes payments based on a fixed rate of 3.229 percent and receives variable rate payments from the swap counterparty based on 68 percent of the One-Month USD LIBOR, until the bonds mature in December 2025. The University has the option to terminate the swap upon five business day written notice and payment of the fair market compensation for the value of the swap. This swap is considered an effective hedge at June 30, 2011 and 2010 and has a fair value of ($5,404,000) and ($6,539,000), respectively.

The floating-to-fixed interest rate swap associated with the Series 2002 General Revenue Bonds has a notional amount of $46,085,000 and $52,145,000 at June 30, 2011 and 2010, respectively, covering a portion of the principal outstanding and the notional amount decreases as principal on the underlying bonds is repaid. Effective from June 1, 2007, the University makes payments based on a fixed rate of 3.5375 percent and receives variable rate payments from the swap counterparty based on 68 percent of One-Month USD LIBOR, through April 1, 2009, and 63 percent of the Five-Year USD LIBOR Swap Rate for the balance of the term, through April 2018. The University has the option to terminate the swap upon five business day written notice and payment of the fair market compensation for the value of the swap. This swap is not considered an effective hedge at June 30, 2011 and 2010 and has a fair value of ($2,468,000) and ($3,266,000), respectively.

The floating-to-fixed interest rate swap associated with the Series 1998A-2 Hospital Revenue Refunding Bonds has a notional amount of $44,670,000 at June 30, 2011 and 2010 tied to the outstanding balance of the bonds. Effective from May 14, 1998, the University makes payments based on a fixed rate of 4.705 percent and receives variable rate payments from the swap counterparty based on the floating Securities Industry and Financial Markets Association (SIFMA) Municipal Index through the final maturity dates of the underlying bonds in December 2024. The counterparty has the option of terminating the swaps if for any 180-day period the average variable rate is more than 7.0 percent. This swap is considered an effective hedge at June 30, 2011 and 2010 and has a fair value of ($10,218,000) and ($11,088,000), respectively.

The floating-to-fixed interest rate swap associated with the Series 1998A-1 Medical Service Plan Revenue Refunding Bonds has a notional amount of $33,980,000 and $34,345,000 at June 30, 2011 and 2010, respectively, tied to the outstanding balance of the bonds. Effective from May 14, 1998, the University makes payments based on a fixed rate of 4.685 percent and receives variable rate payments based on the floating Securities Industry and Financial Markets Association (SIFMA) Municipal Index through the final maturity dates of the underlying bonds in December 2021. The counterparty has the option of terminating the swaps if for any 180-day period the average variable rate is more than 7.0 percent. This swap is considered an effective hedge at June 30, 2011 and 2010 and has a fair value of ($5,383,000) and ($5,844,000), respectively.

Using rates in effect at June 30, 2011, the projected cash flows for the floating-to-fixed interest rate swaps deemed effective hedges in accordance with the provisions of GASB Statement No. 53, along with the debt service requirements of the associated variable rate debt, are summarized as follows:

	Variable Rate Bonds		Swap	Total
(in thousands)	Principal	Interest	Payments, Net	Payments
2012	$ 9,045	$ 89	$ 8,293	$ 17,427
2013	11,680	84	7,931	19,695
2014	12,155	80	7,544	19,779
2015	12,665	76	7,130	19,871
2016	13,195	71	6,708	19,974
2017-2021	70,845	280	26,489	97,614
2022-2026	109,575	119	9,389	119,083
	$ 239,160	$ 799	$ 73,484	$ 313,443

By using derivative financial instruments to hedge exposures to changes in interest rates, the University is exposed to termination risk and basis risk. There is termination risk with floating-to-fixed interest rate swaps because the University or swap counterparty may terminate a swap if the other party fails to perform under the terms of the contract or its credit rating falls below investment grade. Termination risk is the risk that the associated variable rate debt no longer carries a synthetic fixed rate and if at the time of termination a swap has a negative fair value, the University is liable to the counterparty for payment equal to the swap's fair value. The University is also exposed to basis risk because some of the variable payments paid to the University by the counterparties are based on a percentage of LIBOR. Basis risk is the risk that changes in the relationship between SIFMA and LIBOR may impact the synthetic fixed rate of the variable rate debt. The University is not exposed to credit risk because the swaps have negative fair values.

The University is required to post collateral for certain floating-to-fixed interest rate swaps if the fair value of the swap reaches a minimum threshold. Based on the University's current credit ratings, the thresholds are $26,000,000 for the swap associated with the Series 1998A-2 Hospital Revenue Refunding Bonds, $27,000,000 for the swap associated with the Series 2005B Hospital Revenue Bonds and $7,000,000 for the swap associated with the Series 1998A-1 Medical Service Plan Revenue Refunding Bonds. There are no collateral requirements for the other two swaps. During 2011, the University was required to post collateral of $1,061,000 for less than 90 days for the interest rate swap associated with the Series 1998A-1 Medical Service Plan Revenue Refunding Bonds.

Note 8—Self-Insurance

The University is self-insured for medical malpractice, workers' compensation, directors and officers' liability, property damage, auto liability and general liability through Veritas Insurance Corporation, a wholly-owned captive insurance company. The University is also self-insured for various employee benefits through internally maintained funds.

Claims and expenses are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Those losses include an estimate of claims that have been incurred but not reported and the future costs of handling claims. These liabilities are generally based on actuarial valuations and are reported at present value, discounted at a rate of 6 percent.

Changes in the total reported liability for insurance and benefits obligations for the years ended June 30, 2011 and 2010 are summarized as follows:

(in thousands)	2011	2010
Balance, beginning of year	$ 155,272	$ 153,045
Claims incurred and changes in estimates	427,272	396,414
Claim payments	(416,668)	(394,187)
Balance, end of year	165,876	155,272
Less current portion	72,539	66,103
	$ 93,337	$ 89,169

Note 9—Postemployment Benefits

The University provides retiree health and welfare benefits, primarily medical, prescription drug, dental and life insurance coverage, to eligible retirees and their eligible dependents. Substantially all of the approximately 35,000 full-time permanent University employees may become eligible for these benefits if they reach retirement age while working for the University. For employees retiring on or after January 1, 1987, contributions toward health and welfare benefits are shared between the University and the retiree and can vary based on date of hire, date of retirement, age and coverage elections.

The University also provides income replacement benefits, retirement savings contributions and health and life insurance benefits to substantially all permanent University employees that are enrolled in a University sponsored long-term disability plan and qualify, based on disability status while working for the University, to receive basic or expanded long-term disability benefits. Contributions toward the expanded long-term disability plan are shared between the University and employees and vary based on years of service, annual base salary and coverage elections. Contributions toward the basic long-term disability plan are paid entirely by the University.

These postemployment benefits are provided through single-employer plans administered by the University. The Executive Vice Presidents of the University have the authority to establish and amend benefit provisions of the plans.

The University's annual postemployment benefits expense is actuarially determined in accordance with the parameters of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. Projections of benefits are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided and announced future changes at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point.

The University implemented GASB Statement No. 45 in 2008 and elected to amortize its initial unfunded actuarial accrued liability over one year, the minimum period allowed by the Statement. The University also elected to amortize subsequent changes in actuarial assumptions, plan design and experience gains and losses over a ten year closed period. Therefore, the liability for net postemployment benefits obligations recorded in the statement of financial condition will differ from the actuarial accrued liability by the unamortized portion of changes in actuarial assumptions, plan design and experience gains and losses. At June 30, 2011, the recorded liability for net postemployment benefits obligations and the actuarial accrued liability totaled $1,636,652,000 and $1,183,036,000, respectively.

Changes in the total reported liability for postemployment benefits obligations for the years ended June 30, 2011 and 2010 are summarized as follows:

2011

(in thousands)	Retiree Health and Welfare	Long-term Disability	Total
Balance, beginning of year	$ 1,468,563	$ 139,545	$ 1,608,108
Service cost	40,808	2,791	43,599
Amortization of assumption changes, plan changes, and actuarial losses	(63,307)	(405)	(63,712)
Interest cost	89,289	10,997	100,286
Payments of current premiums and claims	(36,958)	(14,671)	(51,629)
Balance, end of year	1,498,395	138,257	1,636,652
Less current portion	41,142	12,496	53,638
	$ 1,457,253	$ 125,761	$ 1,583,014

2010

(in thousands)	Retiree Health and Welfare	Long-term Disability	Total
Balance, beginning of year	$ 1,428,800	$ 134,170	$ 1,562,970
Service cost	43,340	6,196	49,536
Amortization of assumption changes, plan changes, and actuarial (gains) losses	(58,647)	2,448	(56,199)
Interest cost	91,443	10,734	102,177
Payments of current premiums and claims	(36,373)	(14,003)	(50,376)
Balance, end of year	1,468,563	139,545	1,608,108
Less current portion	36,958	14,671	51,629
	$ 1,431,605	$ 124,874	$ 1,556,479

Note 9—Postemployment Benefits, continued

Since a portion of retiree medical services will be provided by the University's Health System, the liability for postemployment benefit obligations is net of the related margin and fixed costs of providing those services which totaled $239,012,000 of actuarial accrued liability at June 30, 2011, and $198,665,000 at June 30, 2010. In accordance with GASB Statement No. 45, the University's liability for postemployment benefit obligations at June 30, 2011, is not reduced by the anticipated Medicare Retiree Drug Subsidy for future periods of approximately $139,000,000 on an actuarial accrued liability basis.

The annual required contribution represents a level of funding that an employer is projected to need in order to prefund its obligations for postemployment benefits over its employees' years of service and totals $102,158,000 and $114,552,000 at June 30, 2011 and 2010, respectively. The University has no obligation to make contributions in advance of when insurance premiums or claims are due for payment and currently pays for postemployment benefits on a pay-as-you-go basis. The University's obligations for postemployment benefits at June 30, 2011, 2010 and 2009, as a percentage of covered payroll of $2,665,924,000, $2,551,273,000 and $2,456,343,000, was 61, 63 and 64 percent, respectively.

The University's liability for postemployment benefits obligations was calculated using the projected unit credit method. Significant actuarial methods and assumptions used in the valuation for years ended June 30, 2011 and 2010 are as follows:

2011

	Retiree Health and Welfare	Long-term Disability
Discount Rate	6.08%	7.88%
Inflation Rate	3.0%	3.0%
Immediate/Ultimate Medical Trend Rate	7.0%-7.5%/5.0%	7.0%/5.0%
Immediate/Ultimate Rx Trend Rate	7.0%/5.0%	7.0%/5.0%
Expected Retirement Age (Faculty/Staff/Union)	66/62/61	Not Applicable
Mortality/Termination Table	RP-2000 Generational	2005 SOA Life Waiver (Modified)

2010

	Retiree Health and Welfare	Long-term Disability
Discount Rate	6.4%	8.0%
Inflation Rate	3.0%	3.0%
Immediate/Ultimate Medical Trend Rate	9.0%-7.5%/5.0%	9.0%-7.5%/5.0%
Immediate/Ultimate Rx Trend Rate	7.5%/5.0%	7.5%/5.0%
Expected Retirement Age (Faculty/Staff/Union)	66/62/61	Not Applicable
Mortality/Termination Table	RP-2000 Projected to 2015	2005 SOA Life Waiver (Modified)

During fiscal 2011, the University announced changes to eligibility requirements for retiree health benefits and the related amount of the University's contributions. To assist current employees with the transition, changes will be phased in gradually over the eight-year period January 1, 2013, through January 1, 2021.

Note 10—Retirement Plan

The University has a defined contribution retirement plan for all qualified employees through the Teachers Insurance and Annuity Association - College Retirement Equities Fund ("TIAA-CREF") and Fidelity Management Trust Company ("FMTC") mutual funds. All regular and supplemental instructional and primary staff are eligible to participate in the plan based upon age and service requirements. Participants maintain individual contracts with TIAA-CREF, or accounts with FMTC, and are fully vested.

Eligible employees generally contribute 5 percent of their pay and the University generally contributes an amount equal to 10 percent of employees' pay to the plan. Effective January 1, 2010, the University contribution commences after an employee has completed one year of employment. Participants may elect to contribute additional amounts to the plans within specified limits that are not matched by University contributions. Contributions and covered payroll under the plan (excluding participants' additional contributions) for the three years ended June 30, 2011, are summarized as follows:

(in thousands)	2011	2010	2009
University contributions	$ 214,905	$ 215,905	$ 208,707
Employee contributions	$ 108,981	$ 106,389	$ 102,705
Payroll covered under plan	$ 2,665,924	$ 2,551,273	$ 2,456,343
Total payroll	$ 2,802,045	$ 2,698,219	$ 2,580,373

Note 11—Net Assets

The composition of net assets at June 30, 2011 and 2010 is summarized as follows:

(in thousands)	2011	2010
Invested in capital assets, net of related debt	$ 3,574,878	$ 3,502,716
Restricted:		
Nonexpendable:		
Permanent endowment corpus	1,279,058	1,213,962
Expendable:		
Net appreciation of permanent endowments	1,312,282	923,832
Funds functioning as endowment	1,652,381	1,447,176
Restricted for operations and other	502,569	439,008
Unrestricted	2,603,094	1,836,294
	$ 10,924,262	$ 9,362,988

Unrestricted net assets, as defined by GASB, are not subject to externally imposed stipulations; however, they are subject to internal restrictions. For example, unrestricted net assets may be designated for specific purposes by action of management or the Board of Regents. All of the unrestricted net assets, which totaled $2,603,094,000 and $1,836,294,000 at June 30, 2011 and 2010, respectively, have been designated for academic and research programs and initiatives and capital programs.

Note 12—Federal Direct Lending Program

The University distributed $358,981,000 and $342,076,000 for the years ending June 30, 2011 and 2010, respectively, for student loans through the U.S. Department of Education ("DoED") federal direct lending program. These distributions and related funding sources are not included as expenses and revenues in the accompanying financial statements. The statement of net assets includes a receivable of $624,000 at June 30, 2011, for DoED funding received subsequent to distribution and a payable of $871,000 at June 30, 2010, for DoED funding received in advance of distribution.

Note 13—Commitments and Contingencies

Authorized expenditures for construction and other projects unexpended as of June 30, 2011, were $623,086,000. Of these expenditures, approximately $572,545,000 will be funded by internal sources, gifts, grants and future borrowings and the remaining $50,541,000 will be funded using unexpended debt proceeds.

Under the terms of various limited partnership agreements approved by the Board of Regents or by University officers, the University is obligated to make periodic payments for advance commitments to venture capital, private equity, real estate, energy and absolute return strategies. As of June 30, 2011, the University had committed, but not paid, a total of $2,006,229,000 in funding for these alternative investments. Based on historical capital calls and discussions with those managing the limited partnerships, outstanding commitments for such investments are anticipated to be paid in the following years ended June 30 (in thousands):

2012	$ 493,411
2013	396,757
2014	351,120
2015	279,368
2016	209,539
2017 and beyond	276,034
	$ 2,006,229

These commitments are generally able to be called prior to an agreed commitment expiration date and therefore may occur earlier or later than estimated.

The University has entered into operating leases for space, which expire at various dates through 2027. Outstanding commitments for these leases are expected to be paid in the following years ended June 30 (in thousands):

2012	$ 30,849
2013	21,891
2014	12,795
2015	8,750
2016	5,975
2017-2021	7,228
2022-2026	2,801
2027	87
	$ 90,376

Operating lease expenses totaled $33,529,000 and $34,523,000 in 2011 and 2010, respectively.

Substantial amounts are received and expended by the University under federal and state programs and are subject to audit by cognizant governmental agencies. This funding relates to research, student aid, patient care and other programs. The University believes that any liabilities arising from such audits will not have a material effect on its financial position.

The University is a party to various pending legal actions and other claims in the normal course of business, and is of the opinion that the outcome thereof will not have a material adverse effect on its financial position.

Note 14—Segment Information

A segment is an identifiable activity reported as a stand-alone entity for which one or more revenue bonds are outstanding. A segment has a specific identifiable revenue stream pledged in support of revenue bonds and has related expenses, gains and losses, assets and liabilities that are required by an external party to be accounted for separately. The University has one segment that meets the reporting requirements of GASB.

The University of Michigan Hospitals and Health Centers ("HHC") operates health care facilities and programs in southeastern Michigan, providing hospital care, ambulatory care and other health services. HHC serves as the principal teaching facility for the University of Michigan Medical School. The faculty of the Medical School provides substantially all physician services to HHC through its Faculty Group Practice.

HHC's outstanding debt, referred to as Hospital Revenue Bonds and Hospital Revenue Refunding Bonds, was issued pursuant to a Master Indenture Agreement, dated May 1, 1986. These bonds are solely payable from, and secured by, a pledge of hospital gross revenues, as defined in the Master Indenture. The University, as permitted by the Master Indenture, has further defined hospital gross revenues pledged to exclude revenues deemed to be associated with the Faculty Group Practice.

Condensed financial information for HHC, before the elimination of certain intra-University transactions, as of and for the years ended June 30, 2011 and 2010 is as follows:

Notes to Consolidated Financial Statements

Note 14—Segment Information, continued

(in thousands)	2011	2010
Condensed Statement of Net Assets		
Assets:		
Current assets	$ 357,509	$ 393,830
Noncurrent assets	2,793,939	2,455,854
Total assets	$ 3,151,448	$ 2,849,684
Liabilities:		
Current liabilities	$ 292,503	$ 281,385
Noncurrent liabilities	1,108,267	966,483
Total liabilities	1,400,770	1,247,868
Net assets:		
Invested in capital assets, net of related debt	702,096	670,052
Restricted:		
Nonexpendable	2,899	2,868
Expendable	100,672	92,463
Unrestricted	945,011	836,433
Total net assets	1,750,678	1,601,816
Total liabilities and net assets	$ 3,151,448	$ 2,849,684
Condensed Statement of Revenues, Expenses and Changes in Net Assets		
Operating revenues	$ 1,990,214	$ 1,912,425
Operating expenses other than depreciation expense	(1,793,016)	(1,716,696)
Depreciation expense	(144,238)	(135,887)
Operating income	52,960	59,842
Nonoperating revenues, net	198,307	105,238
Net income before transfers	251,267	165,080
Transfers to other University units, net	(102,405)	(100,573)
Increase in net assets	148,862	64,507
Net assets, beginning of year	1,601,816	1,537,309
Net assets, end of year	$ 1,750,678	$ 1,601,816
Condensed Statement of Cash Flows		
Net cash provided by operating activities	$ 201,706	$ 196,653
Net cash provided by investing activities	31,529	85,533
Net cash used in capital and related financing activities	(168,976)	(257,400)
Net cash used in noncapital financing activities	(99,263)	(59,246)
Net decrease in cash and cash equivalents	(35,004)	(34,460)
Cash and cash equivalents, beginning of year	155,815	190,275
Cash and cash equivalents, end of year	$ 120,811	$ 155,815

Note 15—Operating Expenses by Function

Operating expenses by functional classification for the years ended June 30, 2011 and 2010 are summarized as follows:

2011

(in thousands)	Compensation and Benefits	Supplies and Services	Depreciation	Scholarships and Fellowships	Total
Instruction	$ 746,347	$ 106,790			$ 853,137
Research	486,677	246,847			733,524
Public service	86,891	44,597			131,488
Academic support	183,866	37,150			221,016
Student services	66,669	18,478			85,147
Institutional support	130,979	49,194			180,173
Operations and maintenance of plant	39,142	236,149			275,291
Auxiliary enterprises	1,893,194	560,446			2,453,640
Depreciation			$ 390,071		390,071
Scholarships and fellowships				$ 114,316	114,316
	$ 3,633,765	$ 1,299,651	$ 390,071	$ 114,316	$ 5,437,803

2010

(in thousands)	Compensation and Benefits	Supplies and Services	Depreciation	Scholarships and Fellowships	Total
Instruction	$ 739,459	$ 111,102			$ 850,561
Research	463,421	216,079			679,500
Public service	96,469	39,295			135,764
Academic support	183,306	43,182			226,488
Student services	67,277	16,837			84,114
Institutional support	134,366	40,066			174,432
Operations and maintenance of plant	42,291	223,708			265,999
Auxiliary enterprises	1,802,682	525,415			2,328,097
Depreciation			$ 360,089		360,089
Scholarships and fellowships				$ 113,753	113,753
	$ 3,529,271	$ 1,215,684	$ 360,089	$ 113,753	$ 5,218,797

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as of June 30, 2011

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