

University of California

Irvine Foundation

Annual Financial Report

June 30, 2016

University of California Irvine Foundation
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Year Ended June 30, 2016

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Report of Independent Auditors

To the Board of Trustees of the
University of California, Irvine Foundation

We have audited the accompanying financial statements of the University of California, Irvine Foundation, a component unit of the University of California, which comprise the statement of net position as of June 30, 2016, and the related statement of revenues, expenses, and changes in net position and of cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the Foundation's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of California, Irvine Foundation as of June 30, 2016, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.



Emphasis of Matter

As discussed in Note 2 to the financial statements, the Foundation changed the manner in which it presents certain fair value hierarchy disclosures related to investments in fiscal 2016. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

The accompanying management's discussion and analysis on pages 3 through 6 are required by accounting principles generally accepted in the United States of America to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PricewaterhouseCoopers LLP

Irvine, CA
October 5, 2016

University of California Irvine Foundation

Management's Discussion and Analysis

June 30, 2016 (Unaudited)

The University of California Irvine Foundation (the "Foundation") was established in 1968 to encourage financial support through charitable gifts for the benefit of the University of California, Irvine ("UC Irvine"). The Foundation is governed by a local Board of Trustees comprised of the campus' closest alumni, friends, and community members. Gifts are also made to the campus through The Regents of the University of California and are not included in these statements.

The following discussion and analysis presents an overview of the financial performance of the Foundation for the fiscal year ended June 30, 2016, with selected comparative information for the year ended June 30, 2015. This discussion and analysis has been prepared by management and should be read in conjunction with the accompanying audited financial statements and footnotes. The financial statements, footnotes, and the discussion and analysis, were created by management and are the responsibility of management.

Introduction to the Financial Statements

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board Statements No. 34, *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended.

The financial statements include a Statement of Net Position; a Statement of Revenues, Expenses, and Changes in Net Position; and a Statement of Cash Flows. Notes to the financial statements and required supplementary information support these statements. All sections must be considered together to obtain a complete understanding of the financial position and changes in financial position of the Foundation.

Statement of Net Position

The Statement of Net Position includes all assets and liabilities of the Foundation, with the difference between the two reported as net position. Assets and liabilities are categorized as current or noncurrent on an accrual basis as of June 30, 2016. This statement also identifies major categories of restrictions on the net position of the Foundation.

Statement of Revenues, Expenses, and Changes in Net Position

The Statement of Revenues, Expenses, and Changes in Net Position presents the revenues earned and expenses incurred by the Foundation during the year ended June 30, 2016 on an accrual basis. Revenues and expenses on this statement are classified as operating or nonoperating.

Statement of Cash Flows

The Statement of Cash Flows presents the changes in the Foundation's cash and cash equivalents for the year ended June 30, 2016 summarized by operating, noncapital financing, and investing activities. The statement is prepared using the direct method of cash flows and, therefore, presents gross rather than net amounts for the year's activities.

Analytical Overview

The Foundation's financial position increased during the fiscal year ended June 30, 2016 as a result of an increased fundraising activities. The Foundation's total net position increased approximately \$22.1 million to \$380.2 million during the year ended June 30, 2016.

University of California Irvine Foundation
Management's Discussion and Analysis
June 30, 2016 (Unaudited)

The following discussion highlights the key financial aspects of the Foundation's activities:

Condensed Summary of Net Position
June 30, 2016 and 2015

	2016	2015
Current assets	\$ 21,726,276	\$ 19,863,722
Investment in land and building, net	-	177,000
Other noncurrent assets	360,958,659	340,708,691
Total assets	<u>382,684,935</u>	<u>360,749,413</u>
Current liabilities	694,498	709,949
Noncurrent liabilities	1,837,425	1,958,502
Total liabilities	<u>2,531,923</u>	<u>2,668,451</u>
Net position:		
Invested in capital assets	-	177,000
Restricted – nonexpendable	220,901,902	201,164,890
Restricted – expendable	156,328,908	154,724,255
Unrestricted	2,922,202	2,014,817
Total net position	<u>\$ 380,153,012</u>	<u>\$ 358,080,962</u>

Assets

Total current assets increased approximately \$1.9 million to \$21.7 million at June 30, 2016. The increase in current assets was due in large part to an increase in short-term investments as a result of an increase in contributions. That increase in contributions was offset by an increase in disbursements to campus.

Noncurrent assets increased approximately \$20.3 million to \$361.0 million at June 30, 2016. Long-term pledges receivable increased by approximately \$32.2 million. The fundraising efforts during the fiscal year resulted in \$11.5 million in additions to the permanent endowment. These increases were offset by the slight stock market decline which resulted in a net decrease in the fair value of investments of approximately \$9.2 million. These increases are also offset by the need for the Foundation to keep some of the endowment funds in current asset accounts to distribute for spending and capital calls on alternative investments.

Liabilities

Current liabilities consist of payables related to endowment investments, unallocated gifts requiring further documentation, and the current portion of liabilities to life beneficiaries. The noncurrent liabilities are related to the future payments estimated to be paid to the donor on charitable remainder trusts prior to the Foundation having access to the trust assets.

University of California Irvine Foundation
Management's Discussion and Analysis
June 30, 2016 (Unaudited)

Net Position increased by \$22.1 million in the current fiscal year, as reflected below:

Condensed Statement of Revenues, Expenses, and Changes in Net Position
Years ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Operating revenues		
Contributions	\$ 69,648,969	\$ 28,993,044
Other operating revenues	317,714	242,748
Total operating revenues	<u>69,966,683</u>	<u>29,235,792</u>
Operating expenses		
Disbursements to University of California, Irvine	52,049,881	45,470,146
Administrative and other operating expenses	2,064,552	1,146,713
Total operating expenses	<u>54,114,433</u>	<u>46,616,859</u>
Operating income (loss)	<u>15,852,250</u>	<u>(17,381,067)</u>
Nonoperating income		
Investment income, net	4,020,934	6,304,547
Net change in fair value on investments	(9,163,412)	10,544,234
Change in value of life income liabilities	(88,667)	(368,225)
Total nonoperating income (loss)	<u>(5,231,145)</u>	<u>16,480,556</u>
Contributions to permanent endowments	<u>11,450,945</u>	<u>14,644,613</u>
Increase/(Decrease) in net position	22,072,050	13,744,102
Net position, beginning of year	<u>358,080,962</u>	<u>344,336,860</u>
Net position, end of year	<u>\$ 380,153,012</u>	<u>\$ 358,080,962</u>

Revenues

Operating revenues increased from prior year by \$40.7 million to \$70.0 million. The increase is due to the overall increase in non-endowment contributions of \$9.5 million from the prior year and an increase in pledges receivable of \$29.4 million from the past fiscal year.

Operating expenses increased \$7.5 million to \$54.1 million for the year ended June 30, 2016. The increase is mostly due to the increase in disbursements to UC Irvine.

Nonoperating income decreased \$21.7 million to a total nonoperating loss of \$5.2 million for the year ended June 30, 2016. This decrease is reflective of the unfavorable investment performance during the year resulting in the net decrease in the fair value of investments of approximately \$9.2 million. In the prior year there were net gains on investments of \$10.5 million.

University of California Irvine Foundation
Management's Discussion and Analysis
June 30, 2016 (Unaudited)

Restricted Resources

Net Position of the Foundation includes funds that have legal restrictions on their use. Funds may be expendable for a specific purpose or they may be nonexpendable.

The following table summarizes which funds are restricted, the type of restriction, and the amount:

	<u>2016</u>	<u>2015</u>
Restricted funds at June 30		
Nonexpendable		
Endowments	\$ 220,887,956	\$ 201,148,238
Life income funds	13,946	16,652
Total nonexpendable	<u>\$ 220,901,902</u>	<u>\$ 201,164,890</u>
Expendable		
Endowments	\$ 35,705,468	\$ 59,712,689
Life income funds	1,248,216	1,334,178
Funds functioning as endowments	66,361,770	75,384,134
Gifts	53,013,454	18,293,254
Total expendable	<u>\$ 156,328,908</u>	<u>\$ 154,724,255</u>

University of California Irvine Foundation
Statement of Net Position
June 30, 2016

Assets

Current assets:

Cash and cash equivalents	\$ 2,152,139
Short-term investments	14,013,105
Current portion of pledges receivable, net of allowance of \$1,792,197	5,488,614
Other current assets	72,418

Total current assets	21,726,276
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Noncurrent assets:

Long-term investments	320,545,173
Pledges receivable, net of allowance of \$897,575	35,879,217
Assets held in charitable remainder trusts	3,278,596
Other noncurrent assets	1,255,673

Total noncurrent assets	360,958,659
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Total assets	\$ 382,684,935
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Liabilities and Net Position

Current liabilities:

Other current liabilities	\$ 515,489
Liabilities to life beneficiaries, current portion	179,009

Total current liabilities	694,498
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Noncurrent liabilities:

Liabilities to life beneficiaries, net of current portion	1,837,425
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Total liabilities	\$ 2,531,923
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Net Position:

Restricted:

Nonexpendable:

Endowments	\$ 220,887,956
Life income funds	13,946

Expendable:

Endowments	35,705,468
Funds functioning as endowments	66,361,770
Life income funds	1,248,216
Gifts	53,013,454

Unrestricted	2,922,202
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Total net position	\$ 380,153,012
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The accompanying notes are an integral part of these financial statements.

University of California Irvine Foundation
Statement of Revenues, Expenses and Changes in Net Position
Year Ended June 30, 2016

Operating revenues:	
Contributions	\$ 69,648,969
Other operating revenue	<u>317,714</u>
Total operating revenues	<u>69,966,683</u>
Operating expenses:	
Disbursements to University of California, Irvine	52,049,881
Administrative and other operating expenses	<u>2,064,552</u>
Total operating expenses	<u>54,114,433</u>
Operating income before other changes in net position	<u>15,852,250</u>
Nonoperating income:	
Investment income, net	4,020,934
Net change in fair value of investments	(9,163,412)
Change in value of annuity and life income liabilities	<u>(88,667)</u>
Total nonoperating income (expense)	<u>(5,231,145)</u>
Contributions for permanent endowments	<u>11,450,945</u>
Change in net position	22,072,050
Net position, beginning of year	<u>358,080,962</u>
Net position, end of year	<u>\$ 380,153,012</u>

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

University of California Irvine Foundation
Statement of Cash Flows
Year Ended June 30, 2016

Cash flows from operating activities:	
Contributions	\$ 36,202,981
Disbursements to University of California, Irvine	(52,049,881)
Payments to beneficiaries	(190,141)
Payments for administrative and other operating expenses	(2,059,834)
Other receipts	<u>403,686</u>
Net cash used in operating activities	<u>(17,693,189)</u>
Cash flows from noncapital financing activities:	
Contributions for permanent endowment	<u>11,197,359</u>
Net cash provided by noncapital financing activities	<u>11,197,359</u>
Cash flows from investing activities:	
Proceeds from sales and maturities of investments	133,813,964
Purchases of investments	(131,308,716)
Investment income, net of investment expense	<u>3,966,333</u>
Net cash provided in investing activities	<u>6,471,581</u>
Net increase in cash and cash equivalents	(24,249)
Cash and cash equivalents – beginning of year	<u>2,176,388</u>
Cash and cash equivalents – end of year	<u><u>\$ 2,152,139</u></u>
Reconciliation of operating income to net cash used in operating activities:	
Operating income	\$ 15,852,250
Adjustments necessary to reconcile operating income to net cash used in operating activities:	
Allowance for uncollectible receivables	(450,736)
Receipt of contributed securities	(4,089,224)
Changes in operating assets and liabilities:	
Pledges receivable	(28,906,026)
Other current liabilities	4,715
Liabilities to life beneficiaries	<u>(104,168)</u>
Net cash used in operating activities	<u><u>\$ (17,693,189)</u></u>
Supplemental noncash investing activities information:	
Gifts of marketable securities - operating	\$ 4,089,226
Gifts of marketable securities - permanent endowment	253,586

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

University of California Irvine Foundation

Notes to Financial Statements

June 30, 2016

1. **Organization**

The University of California Irvine Foundation (the "Foundation"), a California not-for-profit organization, was formed for the purpose of encouraging voluntary gifts, trusts, and bequests for the benefit of the University of California, Irvine ("UCI"). The Foundation provides financial support for various UCI schools and programs, including research grants, student scholarships, instructional support, equipment purchases, capital improvements, and education.

The Foundation is subject to the policies and procedures of The Regents of the University of California ("The Regents") and was established for the benefit of UCI. The Regents established administrative guidelines for the Foundation with regard to the Foundation's ability to conduct operations through its policy on campus foundations. The Regents' policy limits the ability of the Foundation to make certain expenditures and provides a general framework for its operations. The Foundation is considered a component unit of The Regents and was established solely to support the mission of UCI and, accordingly, is considered a governmental not-for-profit organization subject to reporting under the Governmental Accounting Standards Board ("GASB").

2. **Summary of Significant Accounting Policies**

Basis of Presentation

The financial statements of the Foundation are prepared in accordance with accounting principles generally accepted in the United States of America, including all applicable effective statements of the GASB, using the economic resources measurement focus and the accrual basis of accounting.

A summary of the significant accounting policies applied in the preparation of the accompanying financial statements is presented below:

Cash and Cash Equivalents

The Foundation considers all highly liquid investments including demand deposits with original maturities of three months or less to be cash and cash equivalents.

Investments

Investments are stated at fair value. The basis of determining the fair value of investments is the readily determinable sales price based on prices or quotations from a recognized exchange or utilizing an industry standard pricing service, where available. In the case of commingled funds, the fair value is determined based on the number of units held in the fund multiplied by the price per unit share as quoted. Private equities are valued at Net Asset Value (NAV) as reported by the general partners and fund managers. As private equities are not readily marketable, their estimated fair value is subject to uncertainty and therefore may differ from the fair value that would have been used had a ready market for such investments existed. The most recent NAV is adjusted for capital calls, distributions, and significant known valuation changes if any, of its related portfolio through June 30, 2016.

Short-term investments consist of money market accounts. Short-term investments are carried at cost, which approximates fair value. All endowment and trust investments are classified as noncurrent regardless of maturity due to restrictions limiting the Foundation's ability to use these investments.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

2. Summary of Significant Accounting Policies (Continued)

The net change in the fair value of investments represents both realized and unrealized gains and losses on investments.

Endowments

Endowments are managed in a unitized investment pool. Transactions within each individual endowment in the pool are based on the unit market value at the end of the month during which the transaction takes place for withdrawals and additions.

It is the goal of the Foundation that the total return from endowment investments should be adequate to meet the following objectives:

- Preserve investment capital and its purchasing power.
- Generate sufficient resources to meet spending needs (payout).
- Attain reasonable capital appreciation through prudent acceptance of risk to enhance the future purchasing power of the investment capital.

The UC Irvine Foundation follows the Uniform Prudent Management of Institutional Funds Act (UPMIFA). UPMIFA does not set specific expenditure limits; instead, a charity can spend the amount the charity deems prudent after considering the donors intent that the endowment continue permanently, the purpose of the fund, and relevant economic factors. The Foundation's board of trustees approved a 4.5% spending rate of the endowment fund's average unit market value for fiscal year 2016. For fiscal year 2016, the average unit market value is calculated using the closing unit market value on the last day of each of the 36 contiguous months, the last of which ended on June 30 of such fiscal year. This policy is consistent with the Endowment Investment and Spending Policy and Guidelines adopted by the Board of Trustees. Earnings in excess of the payout rate are retained in the endowments.

Assets Held in Charitable Remainder Trusts

The Foundation has been designated as the trustee or co-trustee for several charitable remainder trusts (the "Trusts"). The Trusts are established by donors to provide income, generally for life, to designated beneficiaries. Each year, beneficiaries receive payments based on a percentage of the Trust's fair value (standard unitrust) or the net income (net income unitrust) as specified in the trust agreement. Upon the death of the beneficiaries or termination of the Trusts, as defined, the remaining assets of the Trusts will become contributions to the Foundation, as stipulated in the trust agreements.

The Foundation recognizes the assets held in charitable remainder trusts at fair value. A liability is established for the estimated future payments to the donors or other beneficiaries. This liability is adjusted as benefit payments are made to the donors and beneficiaries each year and as life expectancies change. Fluctuations in the fair value of the related trust assets and any income earned on the trust assets affect this liability. These assets are administered by and invested with a third party.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

2. Summary of Significant Accounting Policies (Continued)

The Trusts are separate legal entities, created under the provisions of the Internal Revenue Code and applicable California state law. The Trusts have a calendar year-end as required under the Tax Reform Act of 1986 and are exempt from federal and California income taxes on investment income accumulated for future distributions and any net capital gains retained in the Trusts.

In addition to the Trusts described above, the Foundation is designated as a beneficiary pursuant to a number of irrevocable trusts, which values will be recorded in the financial statements upon receipt of the actual contribution.

Pledges Receivable

Pledges receivable are written unconditional promises to make future gifts. The Foundation recognizes a receivable and contribution revenue at the time the pledge is made by the donor if the pledge is verifiable, measurable, probable of collection, and meets all applicable eligibility requirements. These eligibility requirements require 1) the Foundation to be stated as the recipient of the pledge; 2) the pledge is considered available for use and can be sold, disbursed, consumed, or invested for a term or in perpetuity; 3) any contingencies on the pledge are met; and 4) if a reimbursement of expenses, allowable costs have been incurred.

Pledge payments scheduled for collection within the next fiscal year are recorded as current assets. Pledge payments scheduled to be collected beyond one year are discounted to recognize the present value of the expected future cash flows. In subsequent years, this discount is accreted and recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any. In addition, an allowance for uncollectible pledges is recorded based on management's assessment of the collectability of outstanding pledges.

Conditional pledges, which depend on the occurrence of uncertain or specified future events, such as matching gifts from other donors, are recognized when the condition is met.

Pledges for endowments are not recorded as revenue or a pledge receivable at the time the pledge is made, as the funds are not available to be invested in perpetuity as specified by the donor. Revenue is recognized on payments on endowed pledges when the cash is received and is recorded in contributions to permanent endowments.

Noncash contributions are recorded at the appraised value of the asset at the date of donation. Fair value is determined based on appraisals or other third-party sources.

Donated Properties

Donations of securities, real estate, and other nonmonetary items are recorded at their fair value at the date of donation and are classified as investments on the statement of net position. Real estate currently listed for sale is recorded at the lower of the independently appraised value or fair value, less estimated selling expenses.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

2. Summary of Significant Accounting Policies (Continued)

Net Position

To ensure observance of limitations and restrictions placed on the use of resources available to the Foundation, net position and revenues, expenses, and gains and losses are classified and reported as follows, based on the existence or absence of donor-imposed restrictions:

Restricted – nonexpendable net position include permanent endowments. Such funds are generally subject to donor restrictions requiring that the principal be invested in perpetuity for the purpose of producing income that may be expended or added to principal in accordance with the donor's wishes. Income and change in fair value of endowment investments are classified as restricted-nonexpendable net position unless otherwise specified by the donor.

Restricted – expendable net position relate to contributions designated by donors for use by particular entities or programs or for specific purposes or functions of UCI. They also include funds functioning as endowments, which may include contributions restricted by Donors for the purpose of specific department expenditures. The principal of these funds can be utilized to cover anticipated short falls.

Unrestricted net position are those net positions of the Foundation that are not subject to donor-imposed restrictions.

The Foundation has adopted a policy of utilizing restricted – expendable funds, when available, prior to unrestricted funds.

Administrative and Other Operating Expenses

The Board of Trustees of the Foundation has established a policy whereby the Foundation's endowment accounts may be charged an administrative fee to reimburse the Foundation for operating expenses. During the year ended June 30, 2016, the endowment accounts were charged an administrative fee of 0.5% of the market value. In addition, for 6 months of the current fiscal year, UCI charged a one-time cost recovery fee of 5% on all gifts to cover UCI-wide fund-raising activities. As of January 1, 2016, UCI no longer charges the one-time cost recovery fee.

Classification of Current and Noncurrent Assets and Liabilities

The Foundation considers assets to be current that can reasonably be expected, as part of its normal business operations, to be converted to cash and be available for liquidation of current liabilities within 12 months of the statement of net position date. Liabilities that reasonably can be expected, as part of normal business operations, to be liquidated within 12 months of the statement of net position date are considered to be current. All other assets and liabilities are considered to be noncurrent.

Classification of Operating and Nonoperating Revenues and Expenses

The Foundation considers contributions to be operating revenues, as fund-raising is the primary activity of the Foundation. Nonoperating revenues consist of investment income, changes in the fair value of investments, and changes in the value of life income liabilities and related trust assets. Operating expenses consist primarily of disbursements to UCI and administrative expenses.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

2. Summary of Significant Accounting Policies (Continued)

Disbursements to UCI

During the year ended June 30, 2016, the Foundation transferred amounts to support the UCI campus as follows:

School of Medicine	\$ 15,913,948
Program in Nursing Science	8,032,868
Henry Samueli School of Engineering	5,549,716
Paul Merage School of Business	4,263,370
Other	3,851,263
Non-Academic units	3,498,182
School of Law	1,597,416
Office of Research	1,461,779
Physical Sciences	1,153,983
Biological Sciences	1,038,933
Claire Trevor School of the Arts	1,031,815
Donald Bren School of Information and Computer Science	998,541
Athletics	968,748
Social Sciences	875,918
Humanities	582,693
Social Ecology	477,788
UCI Libraries	226,304
UCI Medical Center	196,137
School of Education	165,731
Center for Neurobiology of Learning & Memory	161,744
Pharmaceutical Sciences	3,004
	<u>52,049,881</u>
	\$ 52,049,881

Income Taxes

The Foundation is an organization exempt from taxation under Section 501(c)(3) of the Internal Revenue Code and Section 23701d of the California Revenue and Taxation Code and is generally not subject to federal or state income taxes. However, the Foundation is subject to income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purpose for which it is granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the basic financial statements taken as a whole.

Use of Estimates

The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. These principles require management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

2. Summary of Significant Accounting Policies (Continued)

New Accounting Pronouncements

In February 2015, the GASB issued Statement No. 72, Fair Value Measurement and Valuation, effective for the Foundation's fiscal year beginning July 1, 2015. This statement addresses accounting and financial reporting issues related to fair value measurements. The definition of fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This Statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value measurements. The Foundation adopted this pronouncement effective July 1, 2015 and added all necessary disclosures (Note 5).

In March 2016, the GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*, effective for the Foundation's fiscal year beginning July 1, 2017. This statement addresses when irrevocable split-interest agreements constitute an asset for accounting and financial reporting purposes when the resources are administered by a third party. The Statement also provides expanded guidance for circumstances in which the government holds the assets. The Foundation is evaluating the effect that Statement No. 81 will have on its financial statements.

Reclassifications

Certain reclassifications have been made to the 2015 financial information to conform to the 2016 financial statement presentation.

3. Cash, Cash Equivalents, and Short-Term Investments

Cash, cash equivalents, and short-term investments are reported on the statement of net Position as follows:

Cash and cash equivalents	\$ 2,152,139
Short-term investments	<u>14,013,105</u>
	<u>\$ 16,165,244</u>

The Foundation manages a substantial amount of its short-term investments through The Regent's Short Term Investment Pool ("STIP"). Included in short-term investments are deposits in STIP of \$13,414,331 at June 30, 2016. STIP is a money market portfolio, which serves as the Foundation's core investment vehicle for expendable funds.

Other cash intended to meet operating needs is maintained in demand deposit accounts. All cash balances are minimized by sweeping available balances into investment accounts on an as needed basis. At June 30, 2016, the Foundation's cash and cash equivalent deposits, held in nationally recognized banking institutions, was \$2,070,096, which are insured by the Federal Deposit Insurance Corporation ("FDIC") up to \$250,000.

The Foundation does not have any exposure to foreign currency risk in demand deposit accounts.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

4. Investments

The composition of investments at June 30, 2016 is as follows:

Equity securities	
Domestic	\$ 26,687,830
	<u>26,687,830</u>
Equity securities	<u>26,687,830</u>
Commingled funds	
Absolute return funds	21,141,646
Balanced funds (General Endowment Pool)	122,227,764
U.S. equity funds	48,392,653
Non-U.S. equity funds	41,094,691
U.S. bond funds	24,077,037
Non-U.S. bond funds	6,043,237
Real Estate Investment trusts	4,476,692
Money market funds (Short Term Investment Pool)	13,414,331
	<u>13,414,331</u>
Commingled funds	<u>280,868,051</u>
Private equity	23,826,178
Real estate	2,177,000
Other	999,219
	<u>999,219</u>
Total investments	334,558,278
Less current portion	<u>(14,013,105)</u>
Total noncurrent investments	<u>\$ 320,545,173</u>

In accordance with GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, the Foundation's investments are reported by investment type at fair value in the composition of investments above. GASB 40 also requires the disclosure of various types of investment risks based on the type of investment, as well as stated policies adopted by the Foundation to manage those risks.

The Board of Trustees of the Foundation, as the governing board, is responsible for oversight of the Foundation's investments. Pursuant to The Regents' policies on campus foundations, the Board of Trustees for its campus foundation may determine that all or a portion of its investments will be managed by the Treasurer of The Regents. Asset allocation guidelines are provided to the Foundation by the Investment Committee of The Regents.

University of California Irvine Foundation

Notes to Financial Statements

June 30, 2016

4. Investments (Continued)

The Foundation holds significant investments in the form of fixed income securities in the United States government, and fixed income and equity securities in the utilities, oil and gas, financial services, consumer products and services, technology, health care, transportation, and energy industries. These funds are classified as part of the commingled funds. The investment guidelines also permit alternative investments in partnerships where the Foundation is a limited partner relying upon the expertise of experienced general partners. All limited partnerships in which the Foundation invests are subject to annual audits.

The STIP allows participants to maximize the returns on their short-term cash balances by taking advantage of the economies of scale of investing in a large pool with a broad range of maturities. Cash to provide for transfers to campus is invested in the STIP. The available cash in the endowment investment pools awaiting investment is also invested in the STIP.

Investments authorized by The Regents for the STIP include fixed-income securities with a maximum maturity of five and one-half years. In addition, The Regents have also authorized loans, primarily to faculty members residing in California, under the University's Mortgage Origination Program with terms up to 40 years.

The General Endowment Pool ("GEP") is an investment pool in which a large number of individual endowments participate in order to benefit from diversification and economies of scale. The GEP is a balanced portfolio, and is classified as commingled funds.

Investments authorized by The Regents for the GEP and other investment pools include equity securities, fixed-income securities, and certain other asset classes. The equity portion of the investment portfolios may include both domestic and foreign common and preferred stocks, actively managed and passive (index) strategies, along with a modest exposure to private equities. Private equities include venture capital partnerships, buy-outs, and international funds. The Regents' investment portfolios may include certain foreign currency denominated equity securities. The fixed-income portion of the investment portfolios may include both domestic and foreign securities, along with certain securitized investments, including mortgage-backed and asset-backed securities. Fixed-income investment guidelines permit the use of futures and options on fixed-income instruments in the ongoing management of the portfolios. Derivative contracts are authorized for portfolio rebalancing in accordance with The Regents' asset allocation policy and as substitutes for physical securities. Real estate investments are authorized for the GEP. Absolute return strategies, incorporating short sales, plus derivative or option positions to implement or hedge an investment position, are also authorized for the GEP.

The Absolute Return unitized program provides diversification benefits by offering returns that have low correlation to the performance of other asset classes. Investments authorized by The Regents for the Absolute Return portfolio include funds that invest primarily in Long/Short strategies (including U.S., dedicated Non-U.S., short bias, and global equities), Relative Value strategies (including equity market neutral, convertible bond arbitrage, and fixed income), Event Driven strategies (including distressed securities, special situations, capital structure arbitrage, relative value credit, and risk arbitrage strategies), and Opportunistic strategies (including macro and emerging markets).

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

4. Investments (Continued)

The Foundation's investments in pools managed by The Regents are classified by investment type purposes as commingled balanced funds, commingled money market funds, commingled absolute return, or private equity depending on whether they are invested in the GEP, STIP, Absolute Return Unitized Program, or private equity, respectively.

Of the \$334.6 million of total investments, the portion of investments included in endowments is as follows:

Restricted	
Nonexpendable	
Endowments	\$ 220,887,956
Life income funds	13,946
	<u>220,901,902</u>
Total nonexpendable	
Expendable	
Endowments	35,705,468
Funds functioning as endowments	66,361,770
	<u>102,067,238</u>
Total expendable	
Total endowments	
	<u>\$ 322,969,140</u>

The components of the net change in fair value of investments for the year ended June 30, 2016 is as follows:

Net realized gains on sale of investments	\$ 23,010,511
Net unrealized (depreciation) on investments held at year-end	<u>(32,173,923)</u>
Net change in fair value of investments	<u>\$ (9,163,412)</u>

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

4. Investments (Continued)

Investment Risk Factors

There are many factors that can affect the value of investments. Some, such as custodial credit risk, concentration of credit risk, and foreign currency risk may affect both equity and fixed-income securities. Equity securities respond to such factors as economic conditions, individual company earnings performance, and market liquidity, while fixed-income securities are particularly sensitive to credit risks and changes in interest rates. The fixed-income securities are part of the commingled funds. The Foundation has established investment policies to provide the basis for the management of a prudent investment program appropriate to the particular fund type.

Credit Risk

Fixed-income securities are subject to credit risk, which is the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. The circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation, and/or adverse political developments. Certain fixed-income securities, including obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have credit risk.

A bond's credit quality is an assessment of the issuer's ability to pay interest on the bond, and ultimately, to pay the principal. Credit quality is evaluated by one of the independent bond-rating agencies, for example Moody's Investors Service (Moody's) or Standard and Poor's (S&P). The lower the rating, the greater the chance in the rating agency's opinion that the bond issuer will default, or fail to meet its payment obligations. Generally, the lower a bond's credit rating, the higher its yield should be to compensate for the additional risk.

The Foundation's investment in the Regents' STIP, which is considered to be an investment in an external investment pool and are "unrated." The investment guidelines for STIP recognize that a limited amount of credit risk, properly managed and monitored, is prudent and provides incremental risk-adjusted return over its benchmark (the benchmark for STIP is the 2-year Treasury note). No more than 5% of the total market value of the STIP portfolio may be invested in securities rated below investment grade (BB, BA, or lower). The average credit quality of the STIP must be A or better, and commercial paper must be rated A-1, P-1, or F-1.

The Regents recognize that credit risk is appropriate in balanced investment pools such as GEP, by virtue of the benchmark chosen for the fixed-income portion of those pools. That benchmark, the Citigroup Large Pension Fund Index (LPF) is comprised of approximately 30% high-grade corporate bonds, all of which carry some degree of credit risk. Credit risk in the GEP is managed primarily by diversifying across issuers, and portfolio guidelines mandate that no more than 10% of the market value of fixed income may be invested in issues with a credit rating below investment grade. Further, the weighted average credit rating must be A or higher.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

4. Investments (Continued)

Credit Risk (Continued)

The credit risk profile for fixed-income securities in commingled funds at June 30, 2016 is as follows:

Commingled funds	
U.S. bond funds – not rated	\$ 24,077,037
Non-U.S. bond funds – not rated	6,043,237
Money market funds – not rated	<u>13,414,331</u>
Total commingled funds	<u>\$ 43,534,605</u>

Custodial Credit Risk

Custodial credit risk is the risk that in the event of the failure of the custodian, the Foundation's investments may not be recovered.

The Foundation Board has chosen to primarily use the various pooled investment vehicles managed by The Regents' Treasurer as its core investments for the endowment and expendable funds, and for its trusts. These pools are considered to be investments in external pools and are not exposed to custodial credit risk because their existence is not evidenced by securities that exist in physical or book entry form. Similarly, the investment accounts held at the Foundation's custodian are also externally managed pools, and the assets are held in custody or trust and would not be available to the custodian's creditors because they are excluded from the assets of the custodian.

It is the policy of the Foundation that all other direct investments made by the Foundation are held in custodial accounts, and the securities are registered solely in the name of the Foundation. All investments are transacted with nationally reputable brokerage firms, offering protection by the Securities Investor Protection Corporation.

The Foundation minimizes cash balances by sweeping available balances into investment accounts on a regular basis. The majority of the cash balance not invested is maintained in The Regents' STIP fund. The STIP fund is managed by the Treasurer of The Regents. The Regents are responsible for managing the University's investments and establishing policy, which is carried out by the Treasurer. STIP in the cash equivalent category is considered to be an external investment pool and therefore is not subject to deposit custodial credit risk. Remaining cash is maintained in accounts that are established as segregated trusts, protected against any creditors of the bank, and in money market mutual funds. Although they are not insured and are uncollateralized, these accounts are held in the name of the Foundation. Accounts may also be maintained at FDIC insured banking institutions up to the insured level. There is no custodial credit risk or foreign currency risk associated with balances maintained at the banks' trust departments and investment in the STIP. The Foundation's policy is to limit all cash accounts to be 1) in separate custodial trust accounts and where the Foundation's assets are not available to the creditors of the bank, 2) in an agency cash sweep account with the University, or 3) at a credit card processor. A certain portion of the balance may occasionally be exposed to custodial risk due to unforeseen dividends and gifts deposited at fiscal year-end, but are rectified as soon as possible.

There is minimal custodial credit risk for fixed income securities at June 30, 2016.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

4. Investments (Continued)

Concentration of Credit Risk

Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers, thereby exposing the organization to greater risks resulting from adverse economic, political, regulatory, geographic, or credit developments.

The U.S. and non-U.S. equity portions of The Regents and the Foundation portfolios may be managed either passively or actively. For the portion managed passively, the concentration of individual securities is exactly equal to their concentration in the benchmark. While some securities have a larger representation in the benchmark than others, The Regents consider that passive management results in an absence of concentration of credit risk. For the portion managed actively, portfolio guidelines do not specifically address concentration risk, but do state that the U.S. equity asset class in the aggregate will be appropriately diversified to control overall risk and will exhibit portfolio characteristics similar to the asset class benchmark (including concentration of credit risk). Concentration risk for individual portfolios is monitored relative to their individual benchmarks and agreed-upon risk parameters.

Investment guidelines addressing concentration of credit risk related to the fixed-income portion of The Regents portfolios include a limit of no more than 3% of the portfolio's market value to be invested in any single issuer (except for securities issued by the U.S. Treasury or its agencies). These same guidelines apply to the STIP.

The Foundation's investment policy includes a limit of no more than 5% of the portfolio's assets to be invested in any single issuer. At June 30, 2016, the Foundation did not hold a single investment that was greater than 5% of the portfolio.

Interest Rate Risk

Interest rate risk is the risk that the value of fixed-income securities will decline because of changing interest rates. The prices of fixed-income securities with a longer time to maturity, measured by effective duration, tend to be more sensitive to changes in interest rates and, therefore, more volatile than those with shorter durations. Effective duration is the approximate change in price of a security resulting from a 100 basis point (1 percentage point) change in the level of interest rates, rather than a measure of time.

Interest rate risk for the STIP is managed by constraining the maturity of all individual securities to be less than five and one-half years. There is no restriction on weighted average maturity of the portfolio as it is managed relative to the maturity structure of the liabilities, that is, the liquidity demands of the investors. The nature and maturity of individual securities in the STIP allow for the use of weighted average maturity as an effective risk management tool, rather than the more complex measure, effective duration.

Portfolio guidelines for the fixed-income portion of GEP limit weighted average effective duration to plus or minus 20% of the effective duration of the benchmark (Citigroup Large Pension Fund). This constrains the potential price movement due to interest rate changes of the portfolio to be similar to that of the benchmark.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

4. Investments (Continued)

Interest Rate Risk (Continued)

The effective duration for fixed-income securities held in commingled funds at June 30, 2016 is as follows:

	<u>Fair value</u> <u>June 30, 2016</u>	<u>average</u> <u>maturity</u>
Commingled funds – U.S. bond funds	\$ 24,077,037	4.9
Commingled funds – non-U.S. bond funds	6,043,237	7.0
Commingled funds – UC STIP	13,414,331	1.3

Foreign Currency Risk

Foreign currency risk is the possibility that changes in exchange rates between the U.S. dollar and foreign currencies could adversely affect a deposit or investment's fair value. The Regent's strategic asset allocation policy for GEP includes an allocation to non-US equities. These equity investments are not hedged; therefore, foreign currency risk is an essential part of the investment strategy. Their portfolio guidelines for fixed-income securities also allow exposure to non-U.S. dollar-denominated bonds up to 10% of total the portfolio market value. Exposure to foreign currency risk from these securities is permitted and it may be fully or partially hedged using forward foreign currency exchange contracts. Under the investment policies, such instruments are not permitted for speculative use or to create leverage.

Commingled funds

Various currency denominations

Balanced funds	34,447,043
Non-U.S. bond	<u>3,541,337</u>

Total exposure to foreign currency risk	<u>\$ 37,988,380</u>
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Alternative Investment Risks

Alternative investments include ownership interests in a wide variety of partnership and fund structures that may be domestic, off-shore or foreign. Generally there is little or no regulation of these investments by the Securities and Exchange Commission or U.S. state attorneys general. These investments employ a wide variety of strategies including absolute return, hedge, venture capital, private equity and other strategies. Investments in this category may employ leverage to enhance the investment return. Underlying investments can include financial assets such as marketable securities, non-marketable securities, derivatives, and synthetic and structured instruments; real assets; tangible and intangible assets; and other funds and partnerships. Generally, these investments do not have a ready market or may not be traded without approval of the general partner or fund management.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

5. Fair Value

Fair value is defined in the accounting standards as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Assets and liabilities reported at fair value are organized into a hierarchy based on the levels of inputs observable in the marketplace that are used to measure fair value. Inputs are used in applying the various valuation techniques and take into account the assumptions that market participants use to make valuation decisions. Inputs may include price information, credit data, liquidity statistics, and other factors specific to the financial instrument. Observable inputs reflect market data obtained from independent sources. In contrast, unobservable inputs reflect the entity's assumptions about how market participants would value the financial instrument.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used for financial instruments measured at fair value on a recurring basis:

Level 1 – Prices based on unadjusted quoted prices in active markets that are accessible for identical assets or liabilities are classified as Level 1. Level 1 investments include equity securities, assets held in charitable remainder trusts, and other publicly traded securities.

Level 2 – Quoted prices in the markets that are not considered to be active, dealer quotations, or alternative pricing sources for similar assets or liabilities for which all significant inputs are observable, either directly or indirectly are classified as Level 2. Level 2 investments include fixed- or variable-income securities, commingled funds, certain derivatives, real estate, and other assets that are valued using market information.

Level 3 – Investments classified as Level 3 have significant unobservable inputs, as they trade infrequently or not at all. The inputs into the determination of fair value of these investments are based upon the best information in the circumstance and may require significant management judgment. Level 3 investments include private equity investments.

Net Asset Value (NAV) – Investments whose fair value is measured at NAV are excluded from the fair value hierarchy. Investments of non-governmental entities that do not have a readily determinable fair value may be valued at NAV. Investments measured at NAV included hedge funds, private equity investments, and commingled funds.

Not Leveled – Cash and cash equivalents are not measured at fair value and, thus, are not subject to the fair value disclosure requirements.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

5. Fair Value (Continued)

The following tables summarize the investments and other assets reported at fair value within the fair value hierarchy as of June 30, 2016:

	2016					Total
	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Net Asset Value (NAV)	Not Leveled	
	Equity securities:	26,089,834	-	-	-	
Commingled funds	79,323,379	-	-	225,370,850	-	304,694,229
Real Estate	-	2,177,000	-	-	-	2,177,000
Other investments	-	-	-	-	999,219	999,219
Assets held in charitable remainder trust	3,278,596	-	-	-	-	3,278,596
Total investments and assets held in charitable remainder trusts	108,691,809	2,177,000	-	225,370,850	1,597,215	337,836,874

The Foundation addresses the nature and risks of the investments and whether the investments are probable of being sold at amounts different from the NAV per share (or its equivalent).

	Fair Value	Unfunded Commitments	Redemption terms and restrictions
			Not eligible for redemption and semi-annual with 95 day notice. For securities eligible for redemptions there is a 3 year lock-up on capital calls with 13 months remaining on the lock-up. For securities not eligible for redemption the underlying assets are estimated to be liquidated within 5 years.
Absolute return and hedge funds	21,141,646	-	
Commingled funds	180,403,026	-	The redemption terms vary from no restrictions up to 30 days written notice
Private equities	23,826,178	35,982,258	Not eligible for redemption. Estimated to be liquidated in 0-15 years.
Total	225,370,850		

6. Real Estate

As of June 30, 2016, the Foundation held real estate previously contributed as part of endowment and restricted funds. Donated real estate at June 30, 2016 is classified within long-term investments and is comprised of the following:

Land and building - Endowment	\$ 2,000,000
Land and building - Restricted	<u>177,000</u>
	<u>\$ 2,177,000</u>

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

6. Real Estate (Continued)

Land and building – Endowment

The building represents a 50% undivided interest in a commercial building that was donated to the Foundation, along with the land, during the year ended June 30, 1998. Upon donation of the building, the Foundation became party to a noncancelable operating lease, previously in effect. The building lease is set to terminate during December 2019.

Land and building – Restricted

The land represents a 50% interest in an undivided leased fee interest and the land associated with the building. Both plots of land were donated to the Foundation during the year ended June 30, 1998. The land, representing an undivided leased fee interest, is subject to a noncancelable ground lease that is set to terminate during June 2020.

Total rental income earned under such leases during the year ended June 30, 2016 was \$125,364, of which \$90,000 is included in investment income and \$35,364 is included in other operating income in the accompanying financial statements.

Future minimum rental income under noncancelable leases as of June 30, 2016 is as follows:

Payments through June 30,	
2017	126,528
2018	126,528
2019	126,528
2020	81,528
	81,528
	\$ 461,112

7. Pledges Receivable

Pledges receivable at June 30, 2016 are as follows:

Pledges receivable	
For operations	\$ 10,383,736
For capital projects	35,488,209
	35,488,209
Total pledges receivable	\$ 45,871,945

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

7. Pledges Receivable (Continued)

These pledges are expected to be collected in future years, as follows:

Payments through June 30,		
2017		\$ 7,280,812
2018		6,978,623
2019		5,267,510
2020		5,445,000
2021		4,265,000
2022-2030		<u>16,635,000</u>
		45,871,945
Less amounts representing discounted cash flows		<u>(1,814,342)</u>
Present value of pledges receivable		44,057,603
Less current portion of allowance for uncollectible pledges		(1,792,197)
Less non-current portion of allowance for uncollectible pledges		<u>(897,575)</u>
		<u><u>\$ 41,367,831</u></u>

Pledges from one donor represent 70% of pledges receivable at June 30, 2016. One percent of the pledges receivable are from Foundation Trustees.

The Foundation discounts the noncurrent portion of pledges receivable when the contribution is initially recognized and does not revise the rate subsequently. The rate is determined by calculating the average of the annualized return rate of the STIP, which was 1.2% as of June 30, 2016.

An allowance for potentially uncollectible pledges of \$2,689,772 was recorded as of June 30, 2016.

8. Liabilities to Life Beneficiaries

Changes in liabilities to life beneficiaries during the current fiscal year are summarized as follows:

	<u>Balance at</u> <u>June 30, 2015</u>	<u>Additions</u>	<u>Decreases</u>	<u>Balance at</u> <u>June 30, 2016</u>
Liabilities to life beneficiaries	\$ 2,157,680	\$ 48,895	\$ (190,141)	\$ 2,016,434

9. Related Party Transactions

UCI provides facilities and various financial, administrative, and other services to the Foundation. No value has been determined for these services, and as such, no amounts have been reflected in the accompanying financial statements. UCI pays vendors on behalf of the Foundation, which totaled approximately \$1.1 million and is included in the accompanying statements of revenues, expenses, and changes in net Position.

University of California Irvine Foundation
Notes to Financial Statements
June 30, 2016

10. Commitments

The Foundation's Board of Directors has approved alternative investment commitments of approximately \$36.0 million as of June 30, 2016.