FINANCIAL REPORT

FISCAL YEAR 2013

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HARVARD UNIVERSITY

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Message from the President

I write to report on Harvard University's financial results for fiscal 2013.

The past year was one of renewal and advancement. We formally launched the program to renovate our undergraduate Houses and saw the completion of the program's first project, as Old Quincy was transformed into Stone Hall in time to welcome students back to campus this fall. The Common Spaces initiative reached a milestone with the reconstruction of the Science Center Plaza, and significant progress was made in the building of a new art museum that, when it opens in Fall 2014, will increase access to our treasured collections and tie the resources of the museums more directly to teaching and learning in the classroom.

We also continued to move ahead with our new vision for Harvard's presence in Allston as the City of Boston approved our plans for development across the Charles River, including sites in Barry's Corner and on the Business School and Athletics campuses. The faculty of the School of Engineering and Applied Sciences has begun to articulate its vision for the Science Building that is at the center of our long-term plans for a more integrated, expansive and lively campus in Allston that will encourage innovation and foster connections on both sides of the river.

The first course offered by HarvardX went online in September of 2012 as we continued to expand the boundaries of teaching and learning beyond our campus; by March there were more than one million people around the world enrolled in courses through edX, the joint venture in digital learning launched with MIT. Our commitment to the arts was underscored as two American Repertory Theater productions moved from our theater to Broadway, while in Harvard's labs exciting breakthroughs were reported in the search for more effective treatments for diabetes, ALS and heart disease.

But all of this occurred at a time of seismic shifts for American higher education. At the same time that our faculty are reimagining the pedagogical experience in light of advances in technology, a faltering economy has raised questions in the public's mind about the value of a college education and every revenue stream upon which institutions of higher learning depend has come under pressure. Harvard has not been immune to these trends and we have to adapt.

Looking to the future, we launched the Harvard Campaign with the goal of raising $6.5 billion in new funds for the University over the next five years. The campaign is intended to support our most important priorities, enabling us to address the changing nature of knowledge, the rise of new technologies and the increasingly global context of higher education, as well as to advance our future in Allston and invest in financial aid for our students and resources for our faculty.

But the campaign is not a panacea for the significant challenges that we face. We will need to meet those challenges by acting thoughtfully and decisively as a community; we will adapt where circumstances demand it; and we will remain steadfast in defending the values that make Harvard an essential contributor to the pursuit of knowledge in the world.

Sincerely,

Drew Gilpin Faust

Drew Gilpin Faust
PRESIDENT

November 8, 2013

Financial Overview

From the Vice President for Finance and the Treasurer

We write to report on the University's financial position and results for the fiscal year ended June 30, 2013. The current year deficit of approximately $34 million is slightly less than 1% of the University's revenue – and in that context the deficit, while still meaningful, is manageable. However, the ability to stay in financial balance going forward depends in large part on an institutional commitment to cost management and an embrace of innovative revenue opportunities.

Colleges and universities around the country continue to face substantial pressure, and Harvard is no exception. The federal government's ongoing commitment to research funding is more uncertain than it was last year, and we have already begun to feel the chilling effects of the budget sequester on research grants. Net tuition, particularly at the undergraduate level, is likely to continue growing slowly due to Harvard's unwavering investment in grant aid for our students. And while the endowment had a strong year, with an investment return of 11.3%, we are ever mindful of the volatility of global financial markets and the resulting caution we must use in planning for future endowment distributions.

The combination of these pressures, which impacts substantially more than half of the University's total revenue, means we must continue to be aggressive and innovative in our financial management strategies. Harvard's position is strong both academically and financially, but remaining strong requires constant attention and vigilance, and a willingness to make changes in the near term that will position us competitively in the longer term.

Decisive actions taken over the past five years leave Harvard better positioned to weather the persistent uncertainty of our times. The global financial crisis created an opportunity to broadly reevaluate our approaches in many different realms, including:

- New, foundational policies for liquidity management and short-term investments that more closely integrate activities at Harvard Management Company (HMC) with activities in the University's Treasury function. This has resulted in an accumulation of cash held outside HMC that totaled approximately $1.5 billion at June 30, 2013, and a substantially improved ability to understand, identify and evaluate both risks and opportunities in our treasury and investment activities.

- A reduction in the University's outstanding debt. While we believe debt is an important enabler of growth, it currently constitutes an outsized proportion of the University's capital structure. From a high of $6.3 billion at June 30, 2011, Harvard's outstanding debt still stands at $5.7 billion. We are de-levering in a deliberate yet gradual manner in order to maintain flexibility.

- Deeper analytic insights regarding our budgets and the interaction between our budgets and capital plans. The University's governance reform efforts gave rise, beginning two years ago, to a new Finance Committee of the Corporation. The Finance Committee has engaged in close, in-depth collaboration with the University's management team on budgets and longer-term financial plans. The result of this highly productive engagement has been a more sophisticated understanding of the University's financial pressures, a closer tie between budgets and cash needs, and a clearer perspective on the degree to which our operating budgets should provide financing for our capital plans – particularly as those plans relate to the maintenance and renewal of existing facilities.

The progress we have achieved to date positions us well to face the challenges and opportunities ahead. It also gives us the confidence to move forward on critical strategic priorities for the University, including the renewal of Harvard's undergraduate Houses and resumed development of the University's Allston properties. Continuing to pursue our strategic imperatives notwithstanding the highly uncertain context in which we operate reflects Harvard's strength, as well as our success in taking an increasingly proactive rather than reactive approach toward managing our finances. And yet like most colleges and universities, we already have exhausted the easiest opportunities for budget improvement. As a result, we will face increasingly complicated yet unavoidable choices as we seek to cover more ground in cost management.

One area of opportunity relates to activities currently replicated in many parts of the University that might be done more efficiently in aggregation. For example, in the past two years we have pursued efficiencies by reconfiguring our library administration, integrating many aspects of IT operations, and initiating a project to unify the University's many student information systems. Strategic procurement is another promising realm where the sum of the University's parts can be leveraged far more effectively than each unit acting independently – with the result of cost savings, higher quality services, and an improved ability to manage vendor-related risks.

Culture change of this sort is hard for any large and decentralized organization. Changing Harvard's culture will require time, transparency, a willingness to make mistakes along the way, and the capacity to learn from them. Other changes, such as reducing the growth rate of our benefits costs, can be more difficult since they often are experienced at a more personal level. Yet these changes are inevitable and will allow us to protect the integrity of the high-quality teaching and research that has allowed Harvard to lead throughout the centuries. If we do not adapt to overcome the constraints of our circumstances, the future may well find Harvard at a disadvantage, less able to produce for the world the discoveries and graduates that have created such substantial value over time. But if we have the courage to make prudent decisions with our resources and operations, the current moment presents us with the possibility of reshaping that future.

Of course, Harvard's faculty, students and staff are not alone in this endeavor. The Harvard Campaign is a critical vehicle for maintaining and enhancing the University's strength. The Campaign was launched in September, and the impact of our pre-launch engagement can be seen in this year's financial report – most notably in the $792 million in cash receipts during fiscal 2013 (including an increase of nearly $50 million in current use giving), and the 36% increase (to $1.2 billion) in pledges receivable at June 30. We always appreciate the extraordinary generosity of those who care so deeply about the University, but at this particular time we are especially grateful for their ongoing support.

Our concerns about financial pressures in higher education and at Harvard are rooted in a deep underlying passion for what universities are and can be. By naming and addressing these pressures rather than ignoring them, Harvard can more quickly adapt to the very different context in which we find ourselves in order to preserve and even enhance our investment in our most important endeavors. And in doing so, we might bequeath to future generations an even more transformative and inspiring institution than the Harvard of today. Pursuing this aspiration has never been more important.

We hope this introduction provides you with a helpful context for evaluating the University's financial report.

Daniel S. Shore
VICE PRESIDENT FOR FINANCE AND
CHIEF FINANCIAL OFFICER

James F. Rothenberg
TREASURER

November 8, 2013

FINANCIAL OVERVIEW

The University ended fiscal 2013 with an operating deficit of $34 million compared to an operating deficit of $7.9 million in fiscal 2012. Despite the operating deficit, the University's net assets increased by $3.0 billion to $38.6 billion at June 30, 2013, driven mainly by positive endowment returns and an increase in giving.

OPERATING REVENUE

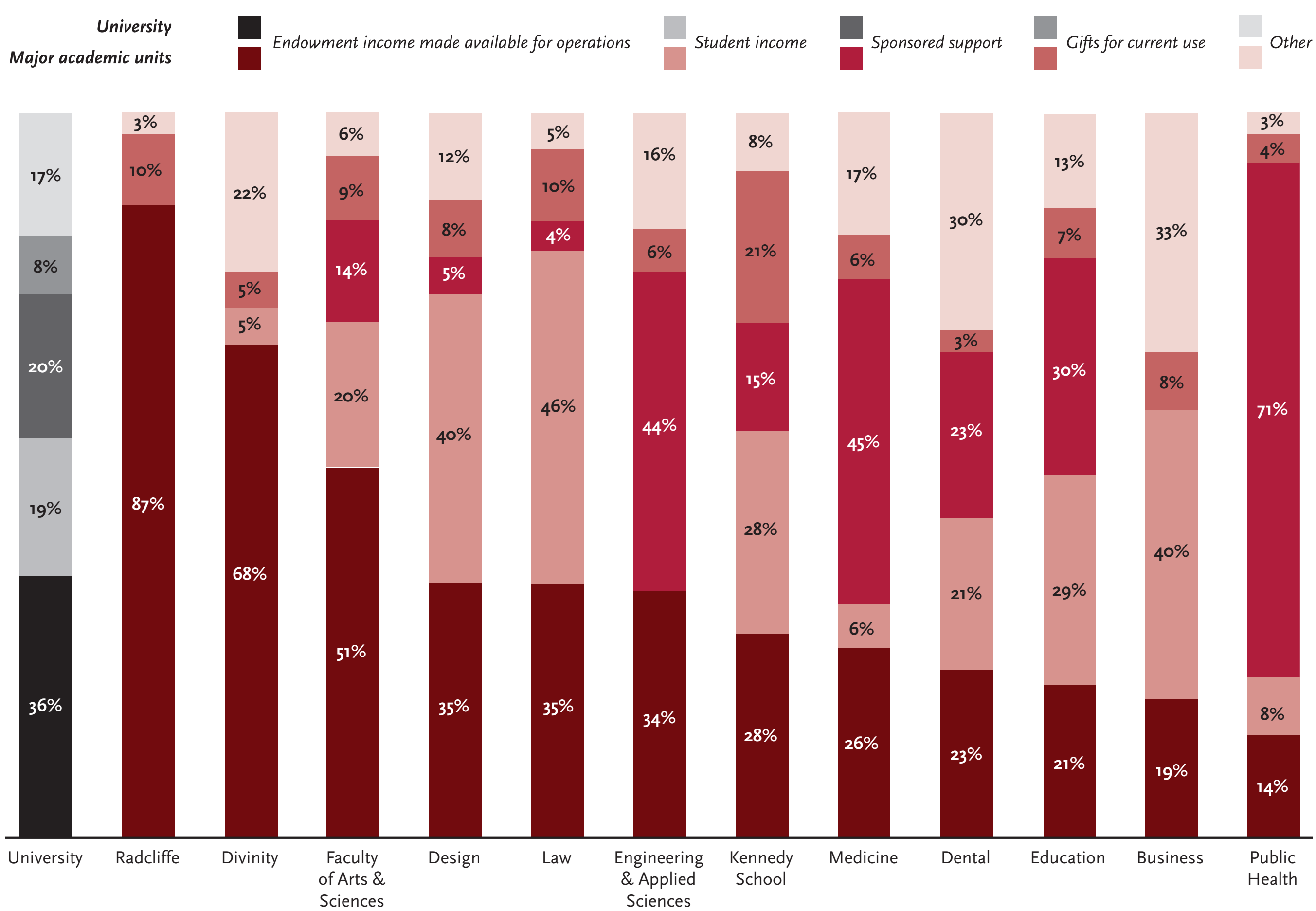
Total operating revenue increased 5% to $4.2 billion, due largely to the increased annual distribution from the endowment and a substantial increase in gifts for current use.

In fiscal 2013, the endowment distribution increased 5% to $1.5 billion. Growth in the endowment distribution was a result of the annual Corporation-approved increase, as well as the impact of new gifts. In the aggregate, Harvard's endowment payout rate (i.e., the dollars withdrawn annually for operations and for one-time or time-limited strategic purposes, as a percentage of the endowment's prior year-end market value) was 5.5%. This is in line with the University's targeted payout rate range of 5.0-5.5% and is consistent with the 5.5% payout rate in fiscal 2012.

Current use gifts increased by 17% from $289 million in fiscal 2012 to $339 million in fiscal 2013, and total cash receipts from giving, including gifts designated as endowment, increased 22% to $792 million (see Note 16 of the audited financial statements). As the University launches its first capital Campaign in more than a decade, it has seen a significant increase in giving. We are extremely grateful to our alumni and supporters for their extraordinary generosity.

The University's sponsored funding, including both federal and non-federal funds, increased by 1% to $845 million in fiscal 2013. Federal funding, which accounted for 77% of the total sponsored funding during fiscal 2013, declined 2% to $653 million in fiscal 2013 while non-federal funding increased 17% to $191 million in fiscal 2013.

FISCAL 2013 SOURCES OF OPERATING REVENUE



The decline in federal sponsored funding was anticipated due to the winding down of ARRA funding, as well as the initial impact of the federal budget sequester. The 17% increase in non-federal funding mitigated the effect of the decline in federal funding and was the result of an increase in support from foundations, state, local and foreign governments, and industry sponsors.

Total student revenue increased approximately 5% to $815 million in fiscal 2013. Net revenue from undergraduate students (i.e., undergraduate tuition, fees, board and lodging, less scholarships applied to student income) increased 4%, which reflects a 3% increase in tuition and fees combined with a modest increase in financial aid. The University's commitment to financial aid, which ensures that the cost of attendance is not a barrier to qualified students, resulted in approximately 60% of undergraduate students from the class of 2016 receiving grant aid awards. Graduate net student revenue increased by approximately 7% due to increases in tuition as well as enrollment increases at several of the University's graduate and professional programs.

OPERATING EXPENSES

Total operating expenses increased by 6% to $4.2 billion. Compensation expense (i.e. salaries, wages and benefits), which represents approximately half of the University's total operating expense, increased 4% from $2.0 billion in fiscal 2012 to $2.1 billion in fiscal 2013.

Salaries and wages increased by 4%, or $55 million, to $1.6 billion in fiscal 2013 mainly due to the University's merit increase programs.

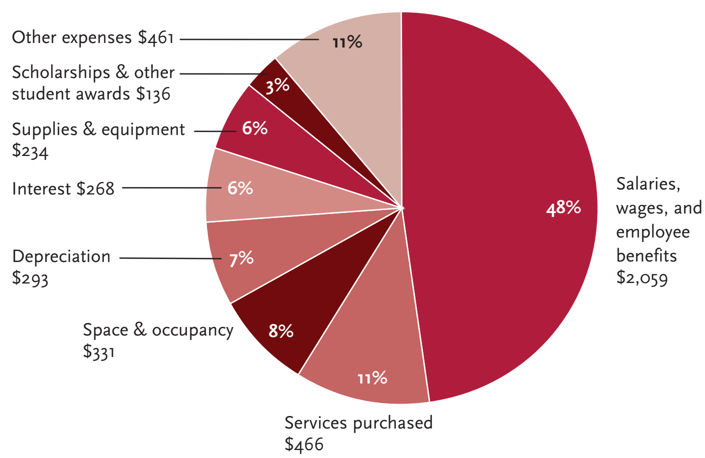
Employee benefits expense increased 6%, or $30 million, to $507 million. The increase was driven mainly by:

- Higher costs associated with active employee health plans, due to health care cost inflation and an increase in family enrollments;
- Employer contributions to defined contribution retirement plans as a result of increases in salary and wages on which the contribution is based, and;
- Higher annual expenses related to the University's defined benefit plans, due primarily to changes in actuarial assumptions.

The University's non-compensation expense increased 7% to $2.2 billion in fiscal 2013. The University increased expenditures on a number of strategic initiatives in fiscal 2013, including its edX collaboration with MIT, further development of its Allston properties, and the Harvard Campaign. These increases in non-compensation expense were offset in part by a $19 million decrease in interest expense, reflecting the reduction in debt outstanding during fiscal years 2012 and 2013.

FISCAL 2013 OPERATING EXPENSES

In millions of dollars



TOTAL OPERATING EXPENSES $4,248

BALANCE SHEET

Investments

In fiscal 2013, the endowment earned an investment return of 11.3%, and its value (after the impact of distributions from the endowment for operations and the addition of new gifts to the endowment during the year) increased from $30.7 billion at the end of fiscal 2012 to $32.7 billion at the end of fiscal 2013. More information can be found in the Message from the CEO of Harvard Management Company (HMC), found on page 8 of this report.

The University's holdings of liquid investments (e.g., cash and treasuries) outside of the General Investment Account (GIA) increased from $1.3 billion at June 30, 2012 to $1.5 billion at June 30, 2013. The GIA is managed by HMC and includes the endowment as well as a portion of the University's pooled operating funds. Over the past several years, the University has increased the amount of liquid, low risk investments held outside the GIA to ensure access to liquidity in situations of financial duress.

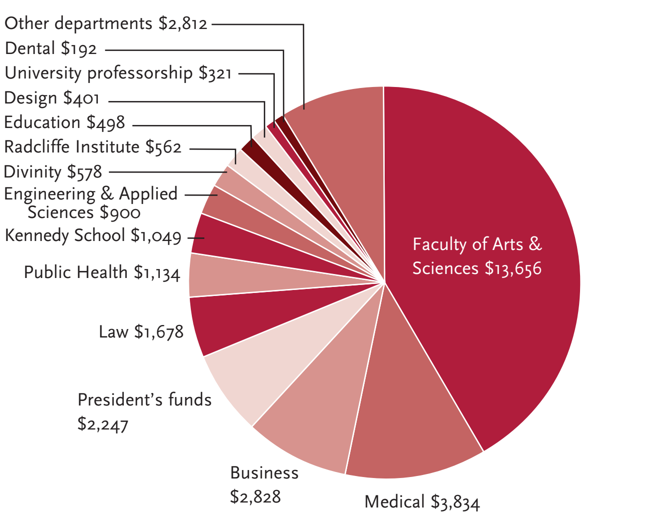
Debt

The University's outstanding debt decreased from $6.0 billion at June 30, 2012 to $5.7 billion at June 30, 2013. The weighted average interest rate of the portfolio was 4.7% at June 30, 2013, and the weighted average years to maturity was 17.1 years. In April 2013 the University refinanced its Series 2006A bonds with a total par amount of $402 million, lowering the interest rate from over 6% to below 4% and thereby reducing the University's projected long-term interest expense by over $10 million per year. The University is seeking to limit new debt over the next several years in order to avoid incremental interest expense and allow flexibility in the face of potential revenue and expense pressures on the University's budget.

The University's AAA/Aaa credit ratings with Standard & Poor's Ratings Services and Moody's Investors Service were re-affirmed in fiscal 2013. Additional detail regarding the University's debt portfolio can be found in Note 12 of the audited financial statements.

FAIR VALUE OF THE ENDOWMENT AS OF JUNE 30, 2013

In millions of dollars



TOTAL FAIR VALUE $32,690

Accrued Retirement Obligations

The University's accrued retirement obligations decreased by $302 million or 29% in fiscal 2013, and represented a $754 million liability at June 30, 2013. The valuation of these obligations is very sensitive to interest rates (i.e. higher interest rates result in a decrease in the liability). Rates increased meaningfully during fiscal 2013 after many years of decline and explain approximately half of the decrease. The remaining reduction is related both to changes in assumptions used in projecting the liability, and to our active management of the retiree medical plan. The University has made several plan changes in recent years, none of which meaningfully impacted the competitive positioning or breadth of the benefit offerings relative to peers but all of which, in the aggregate, have caused a reduction in our future obligation. We continue to dedicate attention to the management of this important area, and as of January 1, 2014 will be making further changes in the retiree medical plan. These changes are intended to better ensure a sustainable and competitive retiree medical benefit for the long term.

Capital Expenditures

The University invested $404.2 million in capital projects and acquisitions during fiscal 2013, an increase of 19% versus fiscal 2012. This enabled progress on several significant projects including:

- The Harvard Art Museums' renovation and expansion, which will result in greater accessibility to the University's world-renowned collections;
- Tata Hall, to support the Business School's portfolio of executive education programs;
- The completion of Stone Hall and commencement of construction for Leverett-McKinlock, the second test project in the broader renovation of Harvard undergraduate Houses; and,
- The Science Center Plaza, which supports the University's goal of creating new, engaging common spaces for the entire community.

This concludes the summary of the key financial highlights for fiscal 2013. We encourage you to read the audited financial statements and related notes for more information regarding the financial position and results of the University.

Message from the CEO of Harvard Management Company

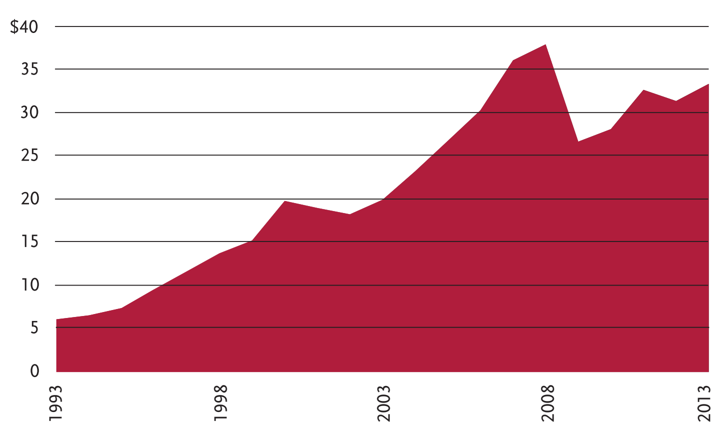
For the fiscal year ended June 30, 2013 the return on the Harvard endowment was 11.3% and the endowment was valued at $32.7 billion. The return exceeded our benchmark by a healthy 223 basis points. As I mark my fifth anniversary as the chief executive of the Harvard Management Company (HMC), I am very proud of the internal and external managers we have in place and the results they have achieved.

Thanks to this talented team we have made a strong recovery since the global economic downturn of 2008-2009, and our outperformance this year alone contributed about $600 million of additional value to the portfolio over and above the markets, net of all fees.

This also marks the fourth consecutive year in which HMC's return exceeded the Policy Portfolio benchmark. As we have noted previously, earning returns in excess of the markets as represented in the Policy Portfolio is not easily done and is not expected every year.

TOTAL VALUE OF THE ENDOWMENT (AFTER DISTRIBUTIONS)

In billions of dollars



Over the last three years the average annual return on the Harvard endowment has been 10.5%, compared with the average annual return on the Policy Portfolio of 9.1%.

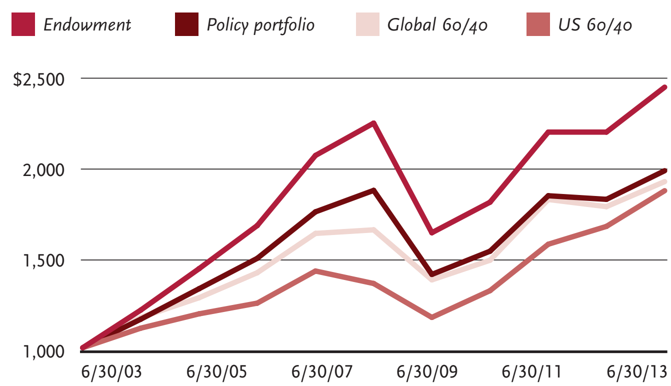
INVESTMENT RETURN
(ANNUALIZED FOR PERIODS GREATER THAN ONE YEAR)

	HMC	Benchmark	Relative
1 year	11.3%	9.1%	2.2%
3 years	10.5%	9.1%	1.4%
10 years	9.4%	7.2%	2.2%
20 years	12.0%	9.1%	2.9%

Longer term, the Harvard endowment under HMC's management has returned 9.4% over the last ten years and 12.0% over the last twenty years.

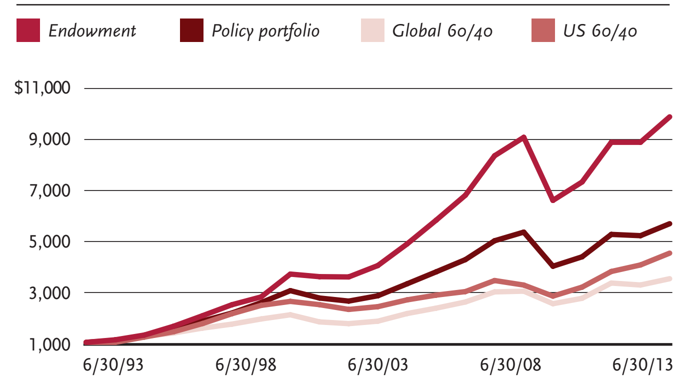
GROWTH OF $1,000 INVESTED IN ENDOWMENT VS. POLICY PORTFOLIO AND 60/40 PORTFOLIOS

TEN YEAR CUMULATIVE RETURNS



GROWTH OF $1,000 INVESTED IN ENDOWMENT VS. POLICY PORTFOLIO AND 60/40 PORTFOLIOS

TWENTY YEAR CUMULATIVE RETURNS

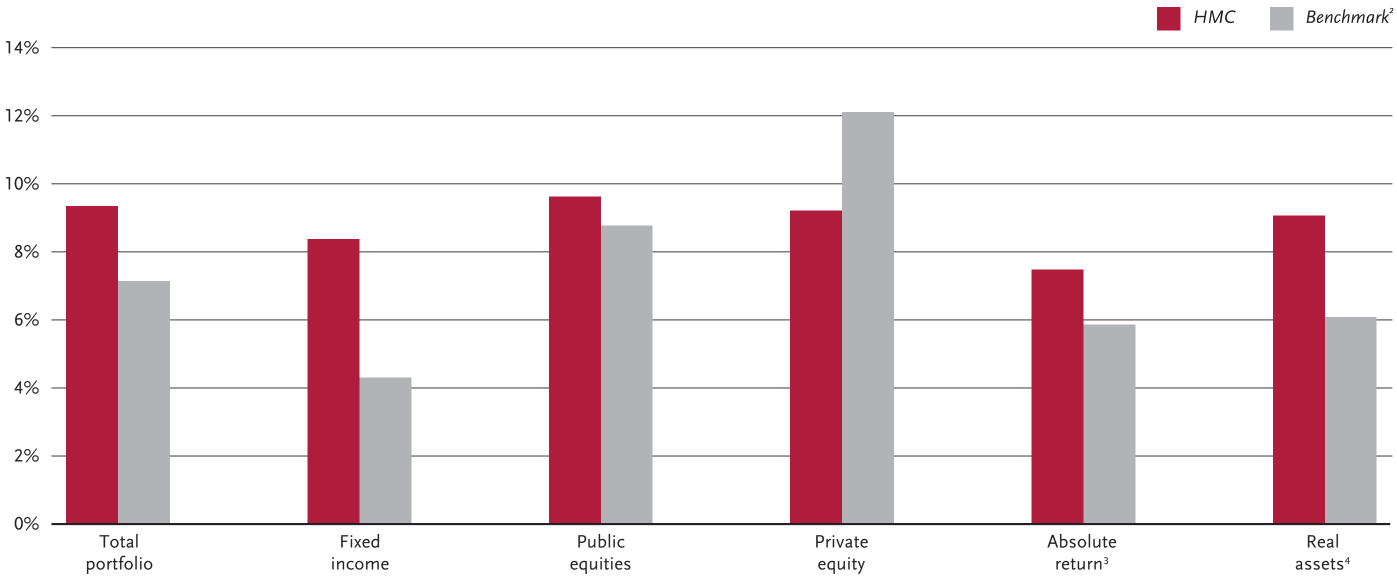


We continue to manage the Harvard endowment with three primary objectives: growth, sufficient liquidity and appropriate risk management. The aspirations of Harvard University, as well as the ongoing challenges presented by the markets, require that we be constantly attentive to all three. The entire team at HMC is attuned to these goals and aligned with our mission: to achieve strong, sustainable long-term investment returns in support of the outstanding institution that is Harvard.

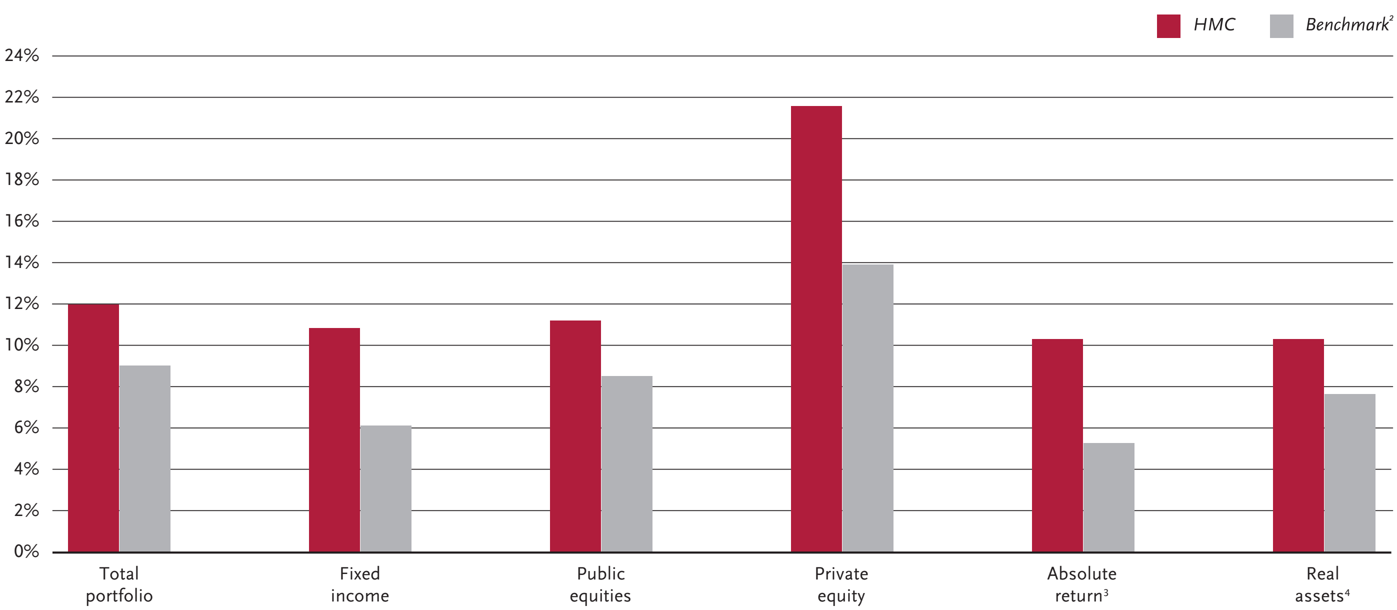
HISTORICAL CONTEXT

HMC's sole focus for its nearly 40 year history has been the investment and stewardship of the endowment – the University's largest financial asset. The perpetual nature of the University creates an unusually long-term horizon for us as investors of the endowment portfolio. This perspective has encouraged us to be innovative as investment managers – from our early investments in venture capital and private equity in the 1970s and

ANNUALIZED TEN YEAR PERFORMANCE BY ASSET CLASS[1]



ANNUALIZED TWENTY YEAR PERFORMANCE BY ASSET CLASS[1]



1 *Returns are calculated on a time-weighted basis with the exception of private equity and real assets, which are calculated on a dollar-weighted basis. Returns are net of all internal management fees and expenses.*
2 *Individual benchmarks are representative of each asset class and are approved by the Board of Directors of HMC.*
3 *Absolute return asset class includes high yield.*
4 *Real assets consist of investments in real estate, natural resources, and publicly traded commodities.*

1980s, to the development of our expertise in timberland and natural resources in the 1990s and 2000s, to our focused strategies in absolute return and public markets during the most recent decade.

As we maintain our focus on the long term, we are constantly aware that financial markets and investors are always evolving: correlations may change over time, previously inefficient markets may get crowded and less attractive, new areas for opportunity may develop.

In the five years since my return to HMC we have continued to evolve the Policy Portfolio. These changes in our Policy Portfolio allocations reflect our growth, liquidity and risk management objectives while allowing us to continue to maintain a high degree of diversification. Specifically, since 2008 we have: added to our Policy Portfolio allocation in equities (increasing growth potential), removed our negative allocation to cash (increasing liquidity), and reduced our allocation to fixed income following a 20 year bull market (managing risk). We have also replaced a portion of our publicly traded commodities with more stable and attractive natural resources.

DISCUSSION OF FISCAL YEAR 2013

During short-term periods, we expect to experience volatility in different regions and asset categories in our portfolio. Last year was a good example. The nominal returns on the broad markets in which we actively invest ranged from 20.6% for the S&P 500 to -8.0% for the Dow Jones Commodities Index. While any investor would welcome a circumstance in which all markets went up at the same time, we are diversified precisely because we know that is not likely to happen.

There was significant variation across regions in fiscal year 2013. US equities rebounded strongly as the US economy showed small but repeated signs of recovery and growth. Housing markets recovered from their lows, consumer confidence improved, and unemployment crept slowly but surely lower.

Outside of the US, markets responded positively in Europe and in developed foreign markets as the threat of a collapse of the European Union became less pronounced. However, emerging markets did not perform as well, on average gaining only 2% to 3% for the year. While the "risk-off" move by some market participants was quite acute toward the end of the fiscal year, we still believe strongly that emerging markets will be an important area for substantial growth. In fact, over the past two and a half decades since emerging market indices first appeared, emerging markets equities have delivered an average annual return 400 basis points greater than the return on developed markets.

Fiscal 2013 Performance by Asset Class

	HMC	Benchmark	Relative
Public equities	16.3%	14.5%	1.8%
Private equity	11.0	10.6	0.4
Fixed income	3.3	(3.4)	6.7
Absolute return	13.2	6.8	6.4
Real assets	7.0	7.2	(0.2)
TOTAL ENDOWMENT	**11.3%**	**9.1%**	**2.2%**

We are pleased to note that our performance relative to the market was once again positive in most asset categories and in total. Multiple studies have shown that 80% of active asset managers underperform their markets, failing to add value for their investors over what would have been earned by a relevant index fund. The 223 basis points of excess return earned by HMC this year versus our Policy Portfolio puts our team in a small minority of successful active investment managers. In addition, HMC's nominal return of 11.3% puts us well ahead of the HFRI Fund of Funds Index (comprised of a large group of hedge fund managers), which returned 7.3% last year.

As in prior years, we would like to highlight a few areas within our portfolio for further discussion of our performance and management philosophy.

Public Equities

	HMC	Benchmark	Relative
Domestic equity	26.6%	21.3%	5.3%
Foreign equity	20.5	18.9	1.6
Emerging markets	2.3	2.9	(0.6)
TOTAL PUBLIC EQUITIES	**16.3%**	**14.5%**	**1.8%**

Domestic equity was a stand-out performer during the last fiscal year, on both a nominal and a relative basis. The US stock market continued a steep recovery as economic indicators improved. Our internal and external managers in domestic equity added value, on average, relative to the markets, some by a wide margin. Foreign equity also performed well, though not as well as US equity, driven by a somewhat improved outlook (or at least the perception that we have reached a bottom) for Japan and parts of Europe. Emerging markets underperformed expectations this fiscal year, with Brazil down 14%, India down 4% and China barely positive, up 1.8%. Notwithstanding, we remain convinced that over time emerging markets is an area that will deliver strong positive returns for a portfolio like ours that can withstand short-term volatility.

Private Equity

	HMC	Benchmark	Relative
TOTAL PRIVATE EQUITY	**11.0%**	**10.6%**	**0.4%**

I would characterize our private equity performance this year as fair. Private equity (which includes venture capital) returned 11.0% for the year, a strong nominal return, but well below the return on public market equity, and only slightly above our benchmark. When we invest in private equity, we lock up Harvard's money for multiple years. In exchange for that lock-up we expect to earn returns over time that are in excess of the public markets – an "illiquidity premium." Over the last ten years however, our private equity and public equity portfolios have delivered similar returns. While this asset class still presents unique opportunities for attractive returns, it has gotten much more crowded and there is less of an illiquidity premium. As a result, we are actively focused on honing our private equity strategy to maintain the highest concentration in the very best managers with the greatest potential to add value.

Fixed Income

	HMC	Benchmark	Relative
Domestic bonds	2.7%	(1.6)%	4.3%
Foreign bonds	2.3	(5.0)	7.3
Inflation-indexed bonds	1.9	(4.8)	6.7
TOTAL FIXED INCOME	**3.3%**	**(3.4)%**	**6.7%**

For most of the year our portfolio was underweight relative to the Policy Portfolio in terms of its exposure to fixed income. This was a good thing, as fixed income returns were negative on a nominal basis. However, we had significant success in our internal fixed income active strategies during fiscal year 2013, leading to a very strong return relative to the fixed income markets for our portfolio. Internal fixed income trading has been a strength of HMC for many years. Our team's expertise in interest rates and relative value across global fixed income markets allows us to find mispriced opportunities in US and international bonds.

Absolute Return

	HMC	Benchmark	Relative
TOTAL ABSOLUTE RETURN	**13.2%**	**6.8%**	**6.4%**

Our absolute return portfolio, comprised entirely of external managers, includes multi-strategy hedge funds, single strategy hedge funds, and some special situations. This portfolio is anchored by very strong and experienced managers who constantly improve their game to deliver above-industry returns. We have also added a collection of newer managers over the last several years with focused strategies in niche areas that are designed not to be correlated with public markets. Although the hedge fund world has become more crowded with both managers and investors, we are pleased with the current composition of this portfolio.

Real Assets

	HMC	Benchmark	Relative
Real estate	10.6%	8.8%	1.8%
Natural resources	5.1	7.6	(2.5)
Public commodities	(4.1)	(3.0)	(1.1)
TOTAL REAL ASSETS	**7.0%**	**7.2%**	**(0.2)%**

We continue to favor well-chosen investments in real assets because of the long-term supply/demand imbalances in these markets, specialized expertise required to complete often-complicated deals, and the sometimes unique nature of the assets we can acquire. As an experienced investor in real assets we believe HMC can perform significantly better than the average investor over time. However, valuation changes and return realizations in these areas will be lumpy.

In real estate, our new investment strategy focused on direct deals performed exceptionally well, generating a return of 15.8%, while our legacy fund investments returned 5.3%. This speaks to the innovative yet disciplined nature of our new HMC real estate team, who have pursued and closed numerous promising property investments but also passed on deals that no longer fit our strategy.

Our natural resources portfolio returned 5.1% in the fiscal year, lagging its benchmark by 2.5%. However, we were pleased that this portfolio generated roughly $600 million of liquidity this past year, owing to sales of timberland properties at strong prices. Over the last ten years our natural resources portfolio has returned 12.2% per year, versus the market benchmark of 7.0%, demonstrating the continued potential of this investment area.

ORGANIZATIONAL UPDATE

HMC, like Harvard, prides itself on being a magnet for talent. We have added a number of promising new investment professionals to our team this past year, including a new Chief Risk Officer, Jake Xia. We now feel HMC is fully staffed on the investment front with highly experienced, high quality talent across the board.

We are also pleased to welcome Jameela Pedicini to the HMC team as our first Vice President of Sustainable Investing. As long-term investors we are acutely aware of the many factors that can impact the sustainability and growth of Harvard's endowment, including environmental, social and governance (ESG) considerations. As HMC's subject matter expert in this area, Jameela will work with HMC investment professionals and University officials to ensure that we are actively considering ESG issues while maintaining our singular focus on maximizing returns for the University.

LOOKING AHEAD

The outlook for the world's economies and markets continues to be full of uncertainty. Questions abound about fiscal and monetary policy here and abroad, about how much "stimulus" is still needed, about the impact of new market regulations and participants, and about the prospects for economic growth across global markets in sometimes shaky political environments. There are many issues to be pondered and debated. However, looking beyond some of the shorter-term issues, which we are fortunate to be able to do, we are confident that there is plentiful opportunity for long-term investors like Harvard.

Harvard University has an immensely long and successful history in making a positive contribution to the world through higher education and research, and in recent years our role in supporting the University has become more meaningful. Our support is likely to become even more important in the coming years given the myriad challenges facing higher education. We at HMC come to work every day with one mission front of mind – achieving strong long-term investment returns that will enable this remarkable institution to continue to achieve its goals and maintain its excellence far into the future.

Sincerely,

Jane L. Mendillo
President and Chief Executive Officer

November 8, 2013

PURPOSE OF THE POLICY PORTFOLIO BENCHMARK

The Policy Portfolio is a theoretical target portfolio comprised of a mix of asset classes that is determined to be best equipped to meet Harvard's needs over time in terms of both potential return and risk. The Policy Portfolio provides HMC with a guide as to the actual allocation of the investment portfolio and also serves as a measuring stick against which we judge the success of our active management strategies. Each year the HMC Board and management team create the Policy Portfolio and review it for continued fit with the University's risk profile and our projections for expected returns in each asset class. Recent evolution of the Policy Portfolio is summarized in the following table:

	2008	2013
Domestic equity	12%	11%
Foreign equity	12	11
Emerging markets	10	11
Private equity	11	16
TOTAL EQUITIES	**45**	**49**
ABSOLUTE RETURN	**18**	**15**
Public commodities	8	2
Natural resources	9	13
Real estate	9	10
TOTAL REAL ASSETS	**26**	**25**
Domestic bonds	5	4
Foreign bonds	3	2
Inflation-indexed bonds	7	3
TOTAL FIXED INCOME	**15**	**9**
HIGH YIELD	**1**	**2**
CASH	**-5**	**0**
TOTAL	**100%**	**100%**

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Independent Auditor's Report

To the Board of Overseers of Harvard College:

We have audited the accompanying consolidated financial statements of Harvard University (the "University"), which comprise the consolidated balance sheet as of June 30, 2013, and the related consolidated statements of changes in net assets with general operating account detail, changes in net assets of the endowment, and cash flows for the year then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated 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 consolidated financial statements are free from material misstatement.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the University at June 30, 2013, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

We have previously audited the University's 2012 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated November 2, 2012. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2012 is consistent, in all material respects, with the audited financial statements from which it has been derived.

PricewaterhouseCoopers LLP

November 8, 2013

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BALANCE SHEETS

with summarized financial information as of June 30, 2012

In thousands of dollars	June 30 2013	2012
ASSETS:		
Cash	**$ 63,399**	$ 155,088
Receivables, net (*Note 6*)	**226,150**	227,401
Prepayments and deferred charges	**158,655**	171,026
Notes receivable, net (*Note 7*)	**365,626**	363,566
Pledges receivable, net (*Note 8*)	**1,236,091**	908,558
Fixed assets, net (*Note 9*)	**5,793,371**	5,776,545
Interests in trusts held by others (*Note 4*)	**352,069**	343,798
Investment portfolio, at fair value (*Notes 3 and 4*)	**52,805,403**	43,385,126
Securities pledged to counterparties, at fair value (*Notes 3 and 4*)	**13,209,043**	6,383,535
TOTAL ASSETS	**74,209,807**	**57,714,643**
LIABILITIES:		
Accounts payable	**324,524**	284,250
Deposits and other liabilities	**705,187**	648,896
Securities lending and other liabilities associated with the investment portfolio (*Notes 3, 4 and 12*)	**26,895,350**	12,294,626
Liabilities due under split interest agreements (*Note 11*)	**717,325**	670,242
Bonds and notes payable (*Note 12*)	**5,688,007**	6,039,139
Accrued retirement obligations (*Note 13*)	**753,957**	1,056,015
Government loan advances (*Note 7*)	**68,249**	67,044
TOTAL LIABILITIES	**35,152,599**	**21,060,212**
NET ASSETS, attributable to non-controlling interests in the pooled general investment account (*Notes 3 and 4*)	**453,940**	**1,070,136**
NET ASSETS, attributable to the University	**38,603,268**	**35,584,295**
TOTAL LIABILITIES AND NET ASSETS	**$ 74,209,807**	**$ 57,714,643**

	Unrestricted	Temporarily restricted	Permanently restricted	June 30 2013	2012
NET ASSETS, attributable to the University:					
General Operating Account (*Note 10*)	$ 3,286,843	$ 1,960,942	$ 96,970	**$ 5,344,755**	$ 4,288,513
Endowment (*Note 10*)	5,609,017	21,150,238	5,930,234	**32,689,489**	30,745,534
Split interest agreements (*Note 11*)		77,418	491,606	**569,024**	550,248
TOTAL NET ASSETS, attributable to the University	**$ 8,895,860**	**$ 23,188,598**	**$ 6,518,810**	**$ 38,603,268**	**$ 35,584,295**

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

STATEMENTS OF CHANGES IN NET ASSETS WITH GENERAL OPERATING ACCOUNT DETAIL

with summarized financial information for the year ended June 30, 2012

In thousands of dollars	Unrestricted	Temporarily restricted	Permanently restricted	For the year ended June 30 2013	For the year ended June 30 2012
OPERATING REVENUE:					
Student income:					
Undergraduate program	$ 269,431			**$ 269,431**	$ 264,513
Graduate and professional degree programs	456,407			**456,407**	432,518
Board and lodging	160,649			**160,649**	155,417
Continuing education and executive programs	290,760			**290,760**	281,317
Scholarships applied to student income (*Note 14*)	(362,532)			**(362,532)**	(357,001)
Total student income	814,715	0	0	**814,715**	**776,764**
Sponsored support (*Note 15*):					
Federal government - direct costs	479,527			**479,527**	493,003
Federal government - indirect costs	173,846			**173,846**	176,560
Non-federal sponsors - direct costs	63,190	$ 102,038		**165,228**	139,618
Non-federal sponsors - indirect costs	18,164	7,992		**26,156**	23,443
Total sponsored support	734,727	110,030	0	**844,757**	**832,624**
Gifts for current use (*Note 16*)	91,829	246,706		**338,535**	289,217
Investment income:					
Endowment returns made available for operations (*Note 10*)	272,379	1,227,033		**1,499,412**	1,422,064
GOA returns made available for operations	134,170			**134,170**	141,804
Other investment income	11,014	6,768		**17,782**	17,510
Total investment income	417,563	1,233,801	0	**1,651,364**	**1,581,378**
Other income (*Note 17*)	565,293			**565,293**	538,327
Net assets released from restrictions	1,560,745	(1,560,745)		**0**	0
TOTAL OPERATING REVENUE	**4,184,872**	**29,792**	**0**	**4,214,664**	**4,018,310**
OPERATING EXPENSES:					
Salaries and wages	1,553,096			**1,553,096**	1,497,642
Employee benefits (*Note 13*)	506,570			**506,570**	476,368
Services purchased	465,522			**465,522**	424,786
Space and occupancy	331,264			**331,264**	268,623
Depreciation (*Note 9*)	293,106			**293,106**	284,160
Interest (*Note 12*)	267,634			**267,634**	287,067
Supplies and equipment	234,301			**234,301**	235,907
Scholarships and other student awards (*Note 14*)	136,360			**136,360**	128,993
Other expenses (*Note 18*)	460,518			**460,518**	422,673
TOTAL OPERATING EXPENSES	**4,248,371**	**0**	**0**	**4,248,371**	**4,026,219**
NET OPERATING SURPLUS/(DEFICIT)	**(63,499)**	**29,792**	**0**	**(33,707)**	**(7,909)**
NON-OPERATING ACTIVITIES:					
Income from GOA investments	11,762			**11,762**	10,938
Realized and unrealized appreciation/(depreciation), net (*Note 3*)	372,591			**372,591**	(162,764)
GOA returns made available for operations	(134,170)			**(134,170)**	(141,804)
Change in pledge balances (*Note 8*)		281,400		**281,400**	123,553
Change in interests in trusts held by others		1,388		**1,388**	8,140
Capital gifts for loan funds and facilities (*Note 16*)		87,766	$ 451	**88,217**	26,243
Change in retirement obligations (*Note 13*)	389,845			**389,845**	(208,814)
Gain from discontinued operations (*Note 2*)	24,891			**24,891**	3,359
Other changes	(88,616)			**(88,616)**	(17,226)
Transfers between GOA and endowment (*Note 10*)	40,859	86,738	(3,676)	**123,921**	140,142
Transfers between GOA and split interest agreements		18,695	25	**18,720**	14,235
Non-operating net assets released from restrictions	(10,145)	6,473	3,672	**0**	0
TOTAL NON-OPERATING ACTIVITIES	**607,017**	**482,460**	**472**	**1,089,949**	**(203,998)**
GENERAL OPERATING ACCOUNT NET CHANGE DURING THE YEAR	**543,518**	**512,252**	**472**	**1,056,242**	**(211,907)**
Endowment net change during the year	246,681	1,386,944	310,330	**1,943,955**	(1,267,195)
Split interest agreement net change during the year (*Note 11*)		6,713	12,063	**18,776**	32,459
NET CHANGE DURING THE YEAR, attributable to the University	**790,199**	**1,905,909**	**322,865**	**3,018,973**	**(1,446,643)**
NET CHANGE IN NET ASSETS, attributable to non-controlling interests in the pooled general investment account	(616,196)			**(616,196)**	**237,797**
NET CHANGE DURING THE YEAR	**174,003**	**1,905,909**	**322,865**	**2,402,777**	**(1,208,846)**
Net assets, beginning of year	9,175,797	21,282,689	6,195,945	**36,654,431**	37,863,277
NET ASSETS, end of year	**$ 9,349,800**	**$ 23,188,598**	**$ 6,518,810**	**$ 39,057,208**	**$ 36,654,431**

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

STATEMENTS OF CHANGES IN NET ASSETS OF THE ENDOWMENT

with summarized financial information for the year ended June 30, 2012

In thousands of dollars	Unrestricted	Temporarily restricted	Permanently restricted	For the year ended June 30 2013	2012
Investment return (*Note 3*):					
Income from general investments	$ 17,682	$ 81,192		**$ 98,874**	$ 104,109
Realized and unrealized appreciation/(depreciation), net	541,956	2,626,458		**3,168,414**	(103,709)
Total investment return	559,638	2,707,650	0	**3,267,288**	400
Endowment returns made available for operations	(272,379)	(1,227,033)		**(1,499,412)**	(1,422,064)
Net investment return	287,259	1,480,617	0	**1,767,876**	(1,421,664)
Gifts for capital (*Note 16*)	3,276	35,903	$ 183,507	**222,686**	226,494
Transfers between endowment and the GOA (*Note 10*)	(40,859)	(86,738)	3,676	**(123,921)**	(140,142)
Capitalization of split interest agreements (*Note 11*)		3,815	40,979	**44,794**	58,267
Change in pledge balances (*Note 8*)		(9,741)	54,778	**45,037**	25,510
Change in interests in trusts held by others (*Note 10*)		431	6,452	**6,883**	(15,750)
Other changes	(7,104)	(36,897)	24,601	**(19,400)**	90
Net assets released from restrictions	4,109	(446)	(3,663)	**0**	0
NET CHANGE DURING THE YEAR	**246,681**	**1,386,944**	**310,330**	**1,943,955**	**(1,267,195)**
Net assets of the endowment, beginning of year	5,362,336	19,763,294	5,619,904	**30,745,534**	32,012,729
NET ASSETS OF THE ENDOWMENT, end of year	**$ 5,609,017**	**$ 21,150,238**	**$ 5,930,234**	**$ 32,689,489**	**$ 30,745,534**

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

STATEMENTS OF CASH FLOWS

In thousands of dollars	For the year ended June 30 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	**$ 2,402,777**	$ (1,208,846)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Change in non-controlling interests in the pooled general investment account	**616,196**	(237,797)
Depreciation*	**293,106**	288,865
Realized and unrealized (gain)/loss on investments, net	**(3,628,851)**	154,235
Change in fair value of interest rate exchange agreements	**(30,574)**	115,907
Payments to terminate swaps	**(345,280)**	(134,582)
Change in interests in trusts held by others	**(8,271)**	7,610
Change in liabilities due under split interest agreements	**47,083**	(101,326)
Gifts of securities	**(108,058)**	(83,471)
Gifts restricted for capital purposes	**(262,814)**	(212,776)
Loss on redemption of debt	**75,088**	17,185
Loss on disposal of assets	**36,181**	1,348
Write-off of assets and liabilities related to discontinued operations	**(7,340)**	
Net gain on sale of property related to discontinued operations	**(22,923)**	
Change in accrued retirement obligations	**(302,058)**	238,130
Changes in operating assets and liabilities:		
Receivables, net	**1,251**	(28,170)
Prepayments and deferred charges	**12,371**	(7,140)
Pledges receivable, net	**(327,533)**	(150,117)
Accounts payable	**10,751**	(14,666)
Deposits and other liabilities	**56,291**	(30,430)
NET CASH USED IN OPERATING ACTIVITIES	**(1,492,607)**	**(1,386,041)**
CASH FLOWS FROM INVESTING ACTIVITIES:		
Loans made to students, faculty, and staff	**(47,669)**	(48,024)
Payments received on student, faculty, and staff loans	**43,950**	46,383
Change in other notes receivable	**1,659**	1,431
Proceeds from the sales of gifts of securities	**108,058**	83,471
Proceeds from the sales and maturities of investments	**81,179,764**	46,924,811
Purchases of investments	**(81,065,595)**	(47,415,716)
Additions to fixed assets	**(463,715)**	(437,673)
Proceeds from sale of property related to discontinued operations	**167,732**	
NET CASH USED IN INVESTING ACTIVITIES	**(75,816)**	**(845,317)**
CASH FLOWS FROM FINANCING ACTIVITIES:		
Change in overdrafts included in accounts payable	**9,656**	(24,003)
Proceeds from the issuance of debt	**402,904**	136,280
Debt repayments	**(829,124)**	(450,035)
Gifts restricted for capital purposes	**262,814**	212,776
Non-controlling interests in the pooled general investment account contributions and distributions, net	**45,888**	78,083
Change associated with securities lending agreements	**1,583,391**	2,290,785
Change in government loan advances	**1,205**	57
NET CASH PROVIDED BY FINANCING ACTIVITIES	**1,476,734**	**2,243,943**
NET CHANGE IN CASH	**(91,689)**	**12,585**
Cash, beginning of year	**155,088**	**142,503**
CASH, end of year	**$ 63,399**	**$ 155,088**

* *Included in depreciation for FY12 is $4,705 that has been reclassed to non-operating activities for discontinued operations.*

Supplemental disclosure of cash flow information:		
Accounts payable related to fixed asset additions	$ 63,924	$ 44,057
Cash paid for interest	$ 280,423	$ 302,149

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

1. UNIVERSITY ORGANIZATION

Harvard University (the "University") is a private, not-for-profit institution of higher education with approximately 7,260 undergraduate and 14,000 graduate students. Established in 1636, the University includes the Faculty of Arts and Sciences, the School of Engineering and Applied Sciences, the Division of Continuing Education, ten graduate and professional Schools, the Radcliffe Institute for Advanced Study, a variety of research museums and institutes, and an extensive library system to support the teaching and research activities of the Harvard community. The President and Fellows of Harvard College (the "Corporation"), a governing board of the University, has oversight responsibility for all of the University's financial affairs. The Corporation delegates substantial authority to the Schools and departments for the management of their resources and operations.

The University includes Harvard Management Company (HMC), a wholly owned subsidiary founded in 1974 to manage the University's investment assets. HMC is governed by a Board of Directors that is appointed by the Corporation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

The consolidated financial statements present the activities of Harvard University as a whole, including significant affiliated organizations controlled by the University.

Funds transferred to the University on behalf of specific beneficiaries (agency funds) are recorded as assets and liabilities in the *Balance Sheets* and are not included in the *Statement of Changes in Net Assets with General Operating Account Detail*.

The financial statements include certain prior year summarized comparative information in total, not by net asset classification. This information is not presented in sufficient detail to conform with generally accepted accounting principles (GAAP). Accordingly, such information should be read in conjunction with the University's financial statements for the year ended June 30, 2012, from which the summarized information is derived.

Certain prior year amounts have been reclassified to conform to current year presentation. The reclassifications include moving a portion of 2012 operating results to "Gain from discontinued operations" in the non-operating section of the accompanying *Statement of Changes in Net Assets with General Operating Account Detail*. This reclassification increased the prior year operating deficit by $3.4 million. Additionally, investing activities and financing activities within the *Statements of Cash Flows* have been increased by $78.1 million to correctly present the cash flows from non-controlling interests in the pooled general investment account, which the University has concluded is immaterial.

Discontinued operations

In May 2013, the University sold the property known as Arsenal on the Charles (the "Arsenal") for $167.7 million which resulted in a gain of $22.9 million. The gain from operations is $2.0 million. Both are classified as "Gain from discontinued operations" in the non-operating section of the accompanying *Statement of Changes in Net Assets with General Operating Account Detail*.

Net asset classifications

For the purposes of financial reporting, the University classifies resources into three net asset categories pursuant to any donor-imposed restrictions and applicable law. Accordingly, the net assets of the University are classified in the accompanying financial statements in the categories that follow:

UNRESTRICTED net assets are not subject to donor-imposed restrictions. Funds invested in fixed assets and unrestricted endowment funds comprise 89% of the University's unrestricted net assets as of June 30, 2013. In addition, this category includes unrestricted gifts and endowment income balances, University-designated loan funds, and other unrestricted current funds.

TEMPORARILY RESTRICTED net assets are subject to legal or donor-imposed stipulations that will be satisfied either by actions of the University, the passage of time, or both. These net assets include gifts donated for a particular purpose, amounts subject to time restrictions such as funds pledged for future payment, or amounts subject to legal restrictions such as portions of otherwise unrestricted capital appreciation and income, which must be reported as temporarily restricted net assets until appropriated for spending in accordance with Massachusetts law.

PERMANENTLY RESTRICTED net assets are subject to donor-imposed stipulations that they be invested to provide a perpetual source of income to the University. Generally, donors of these assets require the University to maintain and invest the original contribution in perpetuity, but permit the use of some or all investment returns for general or specific purposes.

Revenues from sources other than contributions are generally reported as increases in unrestricted net assets. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets, unless their use is restricted by donor stipulations or by law. Investment returns earned by restricted donor funds are initially classified as temporarily restricted net assets and then reclassified to unrestricted net assets when expenses are incurred for their intended purpose. Expirations of temporary restrictions on net assets are reported as reclassifications from temporarily restricted to unrestricted net assets and appear as "Net assets released from restrictions" and "Non-operating net assets released from restrictions" in the *Statements of Changes in Net Assets*.

Unconditional pledges are reported as increases in the appropriate categories of net assets in accordance with donor restrictions.

Net operating surplus/(deficit)

Revenues earned, expenses incurred, and returns made available for operations for the purpose of teaching, conducting research, and the other programs and activities of the University are the components of "Net operating surplus/(deficit)" in the *Statements of Changes in Net Assets with General Operating Account Detail*.

Collections

The University's vast array of museums and libraries house priceless works of art, historical treasures, literary works, and artifacts. These collections are protected and preserved for public exhibition, education, research, and the furtherance of public service. They are neither disposed of for financial gain nor encumbered in any manner. Accordingly, such collections are not recorded for financial statement purposes.

Insurance programs

The University, together with the Harvard-affiliated teaching hospitals, participates in a group captive insurance company, Controlled Risk Insurance Company (CRICO), to secure limited professional liability, general liability, and medical malpractice insurance for its member shareholders. The University self-insures a portion of its professional liability, including those related to Harvard Medical School activities occurring away from the affiliated teaching hospitals, and general liability programs for which it maintains a reserve for incurred claims. The CRICO provided malpractice coverage applies with no deductible for medical professionals practicing within Harvard's University Health Services department, the School of Dental Medicine, and the School of Public Health. The University also maintains reserves for the self-insured portion of claims related to automobile liability, property damage, and workers' compensation; these programs are supplemented with commercial excess insurance above the University's self-insured retention. In addition, the University is self-insured for unemployment, the primary retiree health plan, and all health and dental plans for active employees. The University's claims liabilities are recognized as incurred, including claims that have been incurred but not reported, and are included in operating expenses.

Tax-exempt status

The University is a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code.

Use of estimates

The preparation of financial statements in accordance with GAAP in the United States of America requires management to make estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates.

New accounting pronouncements

Effective July 1, 2012, the University adopted ASU 2011-4, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S.* GAAP and IFRS. ASU 2011-4 aids entities in measuring fair value, as well as provides guidelines for additional quantitative and qualitative disclosures for instruments categorized within Level 3 of the FASB's fair value hierarchy. The effects of adopting this amendment are addressed in *Note 4*.

The FASB issued ASU 2012-05, *Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows*. ASU 2012-05 defines the appropriate financial reporting for the receipt of donated securities in the Statements of Cash Flows. Donated securities with no donor-imposed restrictions are to be included in the Operating section of the statement, while donated securities with donor-imposed long-term restrictions should be included in the financing section. The University is currently evaluating the impact the adoption of ASU 2012-05 will have on the financial statements.

The FASB issued ASU 2013-01, *Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*. ASU 2013-01 clarifies the scope of previously issued FASB guidance, and its applicability to derivatives, repurchase and reverse repurchase agreements, and securities borrowing and lending transactions that are either offset in accordance with US GAAP or that are subject to master netting agreements. The University is currently evaluating the impact the adoption of ASU 2013-01 will have on the financial statements.

3. INVESTMENTS

The significant accounting policies of the University related to investments are as follows:

A) Investments are presented at fair value in accordance with GAAP. The University's investment valuation policies and procedures are discussed in detail in *Note 4*.

B) Cash and short-term investments are recorded at cost, which approximates fair value, and include cash in bank accounts, institutional money market funds, and other temporary investments held for working capital purposes with maturities of three months or less. Cash and short-term investments do not include cash balances held as collateral by the University.

C) Dividend income is recognized net of applicable withholding taxes on the ex-dividend date. Non-cash dividends are recorded at the fair value of the securities received. Interest income and expenses are recorded net of applicable withholding taxes on the accrual basis of accounting. The University amortizes bond premiums and accretes bond discounts using the effective yield method and when cash collection is expected.

D) The University utilizes a number of wholly owned subsidiary entities to support its investment activities. The consolidated financial statements include all assets, liabilities, income, and expenses associated with these entities. All intercompany accounts and transactions have been eliminated during consolidation.

E) The *Balance Sheets* display both the assets and corresponding liabilities generated by repurchase, reverse repurchase, securities borrowed, and securities lending transactions. The University requires the fair value of the collateral exchanged under these agreements to be equal to or in excess of the total amount of the agreement, including interest where applicable. Collateral is exchanged as required by fluctuations in the fair value of these instruments, and in the event of a counterparty default, the University generally has the right to use the collateral to satisfy the terms of the respective agreement.

F) The University separately reports the fair value of assets for which counterparties have the right to pledge or exchange the collateral they have received; investment portfolio assets that are unencumbered are included in "Investment portfolio, at fair value" in the *Balance Sheets*.

The majority of the University's investments are managed by HMC in the General Investment Account (GIA), a pooled fund that consists primarily of endowment assets. Certain other investments are managed separately from the GIA. These other investments consist primarily of cash, short-term investments, and fixed income securities (principally US government securities) held for the University's working capital and liquidity needs; interest rate contracts on the University's debt portfolio; publicly traded securities associated with split interest agreements; and alternative investments donated to the University. All investments are measured at fair value using valuation techniques consistent with ASC 820 and the accounting policies presented herein.

The University's investment holdings as of June 30, 2013 and 2012 are summarized in the following table (in thousands of dollars):

	2013	2012
Investment portfolio, at fair value:		
Pooled general investment account assets*	**$ 63,746,348**	$ 47,788,308
Other investments**	**2,268,098**	1,980,353
Investment assets***	**66,014,446**	49,768,661
Pooled general investment account liabilities	**26,889,311**	11,912,733
Interest rate exchange agreements	**6,039**	381,893
Investment liabilities	**26,895,350**	12,294,626
TOTAL INVESTMENTS	**39,119,096**	**37,474,035**
Non-controlling interests attributable to the pooled general investment account	**453,940**	1,070,136
TOTAL INVESTMENTS, NET	**$ 38,665,156**	**$ 36,403,899**

* *Includes securities pledged to counterparties of $13,209,043 and $6,383,535 at June 30, 2013 and 2012, respectively.*

** *Consists primarily of repurchase agreements and US government securities of $1,365,059 and $1,150,003 at June 30, 2013 and 2012, respectively.*

*** *Investment holdings include cash and cash equivalents that consist principally of deposits that have maturities of 90 days or less. Cash and cash equivalents classified as investments were $932,136 and $926,896 at June 30, 2013 and 2012, respectively.*

A summary of the University's total return on investments for fiscal 2013 and 2012 is presented below (in thousands of dollars):

	2013	2012
Return on pooled general investment account:		
Realized and change in unrealized gains and losses, net	**$ 3,577,635**	$ (141,861)
Net investment income	**112,974**	117,569
Total return on pooled general investment account*	**3,690,609**	(24,292)
Return on other investments:		
Realized and change in unrealized gains and losses, net	**51,216**	(12,374)
Net investment income	**30,131**	28,979
Total return on other investments	**81,347**	16,605
Realized and change in unrealized gains and losses on interest rate exchange agreements, net	**9,067**	(140,219)
TOTAL RETURN ON INVESTMENTS	**$ 3,781,023**	**$ (147,906)**

* *Net of all internal and external management fees and expenses.*

The University's investment strategy incorporates a diversified asset allocation approach and maintains, within defined limits, exposure to the movements of the global equity, fixed income, real estate, commodities, and private equity markets. The pooled GIA assets and liabilities below have been disaggregated based on the exposure of the investment to these markets. Exposure to each asset class is achieved through investments in individual securities, direct investments in special purpose vehicles, and/or through vehicles advised by external managers.

The pooled GIA assets and liabilities as of June 30, 2013 and 2012 are summarized as follows (in thousands of dollars):

	2013	2012
POOLED GENERAL INVESTMENT ACCOUNT ASSETS:		
Investment assets:		
Domestic common and convertible equity	**$ 5,051,705**	$ 3,510,380
Foreign common and convertible equity	**1,985,000**	1,771,081
Domestic fixed income	**5,694,840**	5,232,751
Foreign fixed income	**7,770,908**	1,774,283
Emerging market equity and debt	**2,658,377**	2,959,047
High yield	**1,477,559**	1,557,938
Absolute return	**5,114,051**	4,751,754
Private equities	**7,271,038**	7,095,625
Natural resources	**3,978,822**	5,349,620
Real estate	**5,948,080**	4,806,388
Inflation-indexed bonds	**749,993**	919,081
Due from brokers	**315,504**	299,518
Total investment assets	**48,015,877**	40,027,466
Repurchase and securities borrowing agreements*	**13,031,450**	6,002,202
Cash and short-term investments	**791,238**	750,733
Other assets**	**1,907,783**	1,007,907
POOLED GENERAL INVESTMENT ACCOUNT ASSETS	**63,746,348**	**47,788,308**
POOLED GENERAL INVESTMENT ACCOUNT LIABILITIES:		
Investment liabilities:		
Equity and convertible securities sold, not yet purchased	**260,056**	38,854
Fixed income securities sold, not yet purchased	**9,059,758**	3,343,931
Due to brokers	**135,116**	63,512
Total investment liabilities	**9,454,930**	3,446,297
Reverse repurchase and securities lending agreements***	**15,037,679**	6,725,670
Other liabilities****	**2,396,702**	1,740,766
POOLED GENERAL INVESTMENT ACCOUNT LIABILITIES	**26,889,311**	**11,912,733**
Non-controlling interests attributable to the pooled general investment account	**453,940**	1,070,136
POOLED GENERAL INVESTMENT ACCOUNT NET ASSETS***	**$ 36,403,097**	**$ 34,805,439**

* *Includes pending repurchase agreements that settled subsequent to the balance sheet date of $3,067,037 and $2,468,475 as of June 30, 2013 and 2012, respectively.*

** *As of June 30, 2013, other assets consisted primarily of receivables for the sale of securities of $306,036, assets consolidated under ASC 810 of $493,293, and pending settlements for reverse repurchase agreements that settled subsequent to the balance sheet date of $999,945. As of June 30, 2012, other assets consisted primarily of receivables for the sale of securities of $179,148, assets consolidated under ASC 810 of $426,018, and pending settlements for reverse repurchase agreements that settled subsequent to the balance sheet date of $255,763.*

*** *Includes pending reverse repurchase agreements that settled subsequent to the balance sheet date of $5,123,004 and $1,477,687 as of June 30, 2013 and 2012, respectively.*

**** *As of June 30, 2013, other liabilities consisted primarily of payables for the purchase of securities of $142,037, and liabilities consolidated under ASC 810 of $1,752,956. As of June 30, 2012, other liabilities consisted primarily of payables for the purchase of securities of $143,644, and liabilities consolidated under ASC 810 of $1,203,333.*

***** *The cost of the total pooled GIA net assets, net of proceeds received from short positions, was $33,979,408 and $33,203,550 as of June 30, 2013 and 2012, respectively.*

As of June 30, 2013 and 2012, the GIA was comprised of the following components (in thousands of dollars):

	2013	2012
POOLED GENERAL INVESTMENT ACCOUNT		
Endowment*	**$ 31,778,186**	$ 29,907,024
General Operating Account	**3,445,655**	3,792,118
Split interest agreements	**769,566**	761,333
Other internally designated funds	**409,690**	344,964
TOTAL POOLED GENERAL INVESTMENT ACCOUNT NET ASSETS	**$ 36,403,097**	**$ 34,805,439**

* *Includes only the portion of the endowment invested in the GIA and excludes pledges, interests in trusts held by others, other non-GIA investments, and GIA income.*

The asset allocation of the University's investment portfolio involves exposure to a diverse set of markets. The investments within these markets involve various risks such as price, interest rate, market, sovereign, currency, liquidity, and credit risks. Additionally, the GIA's investments in natural resources and direct real estate expose the University to a unique set of risks such as operational, environmental, and political risks. Furthermore, a component of the investment portfolio's asset allocation includes two diversified funds managed by external advisors, which represent 15% of the GIA net asset value ("NAV"), in the aggregate. The University anticipates that the value and composition of its investments may, from time to time, fluctuate substantially in response to any or all of the risks described herein.

The University has various sources of liquidity at its disposal within its investment pools, including approximately $3.3 billion in cash and cash equivalents (including repurchase agreements of $2.7 billion) at June 30, 2013 in the GIA and the General Operating Account (GOA). In addition, the University estimates that as of June 30, 2013, it could liquidate additional unencumbered US government securities of $2.2 billion within one business day (typical settlement terms) to meet any immediate short-term needs of the University.

The University has consolidated certain non-controlling interests relating to its investments in natural resources and real estate assets under ASC 810. These non-controlling interests represent the minority interest portion of these assets controlled by the University that are required to be presented on the University's balance sheet under GAAP. The net decrease in non-controlling interests of $616.2 million is primarily driven by a deconsolidation event relating to the sale of an interest in a natural resource investment during the fiscal year. Immediately prior to the sale, the consolidated market value of this investment was $2,030.3 million. As a result of the transaction, for which the University received proceeds of $638.6 million, the University no longer has a controlling interest in the investment. However, the University continues to retain an equity interest in a portion of this investment as of the balance sheet date.

As noted above, the sale of a natural resource investment in fiscal year 2013 triggered a deconsolidation event for accounting purposes, which resulted in a reduction of $805.1 million in non-controlling interest. This reduction was offset by $45.9 million of contributions made by the minority partners during the fiscal year, and appreciation on existing non-controlling interests of $143.0 million for the year ended June 30, 2013.

Other liabilities on page 21 include debt outstanding on consolidated portfolio investments of $1,404.0 million and $979.4 million as of June 30, 2013 and 2012, respectively. This debt would typically be categorized as Level 3 in the ASC 820 fair value hierarchy. Based on the structure, duration, and nature of the debt being consolidated, the University believes the amounts approximate the fair value of the debt as of each reporting period. This debt is utilized for purposes specific to natural resources and real estate assets held by the investment portfolio, and is non-recourse to any other assets held by the University.

4. FAIR VALUE OF INVESTMENT ASSETS AND LIABILITIES

The University endeavors to utilize all relevant and available information in measuring fair value. Investments are valued in accordance with ASC 820, and under the guidelines prescribed by the HMC investment valuation policy, which is reviewed and approved by the HMC Board of Directors on an annual basis.

Instruments listed or traded on a securities exchange are valued at the last quoted price on the primary exchange where the security is traded. Where no sale has occurred on the valuation date, long positions are valued at the bid price and short positions are valued at the ask price. Restrictions that are attached to a security are factored into the valuation of that security, reflective of the estimated impact of those restrictions. Investments in non-exchange traded debt and equity instruments are primarily valued using inputs provided by independent pricing services or by broker/dealers who actively make markets in these securities.

Over the counter derivative products classified as due to/from brokers include option, swap, credit default, interest rate, and forward contracts. These types of instruments are primarily valued using industry standard models with market inputs, or by independent broker quotes. Inputs such as prices, spreads, curves, and/or broker quotes are evaluated for source reliability and consistency with industry standards. Counterparty marks obtained and utilized to determine daily collateral requirements are also used to corroborate input reasonability. The University considers current market conditions including interest rate and credit risks in its evaluation of inputs, pricing methodologies, and models utilized to determine fair values.

Investments managed by external advisors include investments in private equity, real estate, natural resources, and hedge funds. The majority of these investments are not readily marketable and are reported at fair value utilizing the most current information provided by the external advisor, subject to assessments that the information is representative of fair value and in consideration of any additional factors deemed pertinent to the fair value measurement. The University evaluates its external advisors through a manager due-diligence program executed by HMC, which includes an analysis of an advisor's use of and adherence to fair value principles. In situations where the information provided by the external advisor is deemed to not be representative of fair value as of the measurement date, the University will evaluate specific features of the investment and utilize supplemental information provided by the external advisor along with any relevant market data to measure the investment's fair value as of that date.

Fair value measurements of direct investments in natural resources and real estate are based on a combination of information obtained from independent appraisals and/or one or more industry standard valuation techniques (e.g., income approach, market approach, or cost approach). The income approach is primarily based on the investment's anticipated future income using one of two principal methods: the discounted cash flow method or the capitalization method. Inputs and estimates developed and utilized in the income approach may be subjective and require judgment regarding significant matters such as estimating the amount and timing of future cash flows and the selection of discount and capitalization rates that appropriately reflect market and credit risks. The market approach derives investment value through comparison to recent and relevant market transactions with similar investment characteristics. The cost approach is utilized when the cost of the investment is determined to be the best representation of fair value. This method is typically used for newly purchased or undeveloped assets. These valuations are determined by HMC management and subject to review by the HMC Board of Directors.

The University's investments have been categorized based upon the fair value hierarchy in accordance with ASC 820, which prioritizes the inputs to valuation techniques used to measure fair value of investment assets and liabilities into three levels:

LEVEL 1 Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

LEVEL 2 Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly;

LEVEL 3 Prices or valuations that require inputs that are significant to the fair value measurement, unobservable and/or require the University to develop its own assumptions.

The level of an asset or liability within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Transfers between levels are recognized at the beginning of the year.

The following is a summary of the levels within the fair value hierarchy for those investment assets and liabilities subject to fair value measurement as of June 30, 2013 and 2012 (in thousands of dollars):

	2013				2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
INVESTMENT ASSETS:								
Cash and short-term investments	$ 932,136			**$ 932,136**	$ 926,896			**$ 926,896**
Domestic common and convertible equity	630,759	$ 2,339,215	$ 2,303,357	**5,273,331**	190,117	$1,693,625	$ 1,807,661	**3,691,403**
Foreign common and convertible equity	114,636	1,052,088	912,456	**2,079,180**	82,331	1,056,359	713,439	**1,852,129**
Domestic fixed income	6,085,594	10,256		**6,095,850**	5,212,122	100,678	319	**5,313,119**
Foreign fixed income	7,129,303	670,004		**7,799,307**	1,742,134	58,383		**1,800,517**
Emerging market equity and debt	2,240,427	354,475	63,474	**2,658,376**	2,360,648	393,687	204,712	**2,959,047**
High yield	68,670	1,189,459	235,262	**1,493,391**	12,936	962,175	595,763	**1,570,874**
Absolute return		2,546,039	2,568,013	**5,114,052**		2,734,708	2,017,046	**4,751,754**
Private equities			7,387,994	**7,387,994**		1,952	7,193,196	**7,195,148**
Natural resources	9,824		3,972,573	**3,982,397**	2,886	71,316	5,278,303	**5,352,505**
Real estate	54,052		5,903,979	**5,958,031**	60,544		4,758,542	**4,819,086**
Inflation-indexed bonds	764,575			**764,575**	936,662			**936,662**
Due from brokers	67,387	228,802	19,315	**315,504**	30,743	242,474	26,302	**299,519**
Other investments	21,489	1,712	21,338	**44,539**	19,279	1,321	7,862	**28,462**
TOTAL INVESTMENT PORTFOLIO ASSETS*	**18,118,852**	**8,392,050**	**23,387,761**	**49,898,663**	**11,577,298**	**7,316,678**	**22,603,145**	**41,497,121**
Interests in trusts held by others			352,069	**352,069**			343,798	**343,798**
TOTAL INVESTMENT ASSETS	**$ 18,118,852**	**$ 8,392,050**	**$ 23,739,830**	**$ 50,250,732**	**$11,577,298**	**$7,316,678**	**$22,946,943**	**$ 41,840,919**
INVESTMENT LIABILITIES:								
Equity and convertible securities sold, not yet purchased	$ 260,056			**$ 260,056**	$ 36,792	$ 2,062		**$ 38,854**
Fixed income securities sold, not yet purchased	8,568,564	$ 491,194		**9,059,758**	3,233,121	110,810		**3,343,931**
Due to brokers	52,358	88,137	$ 660	**141,155**	6,416	437,719	$ 1,270	**445,405**
TOTAL INVESTMENT LIABILITIES**	**8,880,978**	**579,331**	**660**	**9,460,969**	**3,276,329**	**550,591**	**1,270**	**3,828,190**
Liabilities due under split interest agreements		717,325		**717,325**		670,242		**670,242**
TOTAL LIABILITIES	**$ 8,880,978**	**$ 1,296,656**	**$ 660**	**$ 10,178,294**	**$ 3,276,329**	**$1,220,833**	**$ 1,270**	**$ 4,498,432**

* *Excludes repurchase and securities borrowing agreements of $14,086,336 and $7,152,205 as of June 30, 2013 and 2012, respectively, which would typically be categorized as Level 2 in the ASC 820 fair value hierarchy. Also excludes other assets of $2,029,447 and $1,119,335 as of June 30, 2013 and 2012, respectively, which are not subject to fair value.*

** *Includes fair value of interest rate exchange agreements on the University's debt portfolio of $6,039 and $381,893 as of June 30, 2013 and 2012, respectively. Excludes reverse repurchase and securities lending agreements of $15,037,679 and $6,725,670 as of June 30, 2013 and 2012, respectively, which would typically be categorized as Level 2 in the ASC 820 fair value hierarchy. Also excludes other liabilities of $2,396,702 and $1,740,766 as of June 30, 2013 and 2012, respectively, which are not subject to fair value.*

The following is a rollforward of Level 3 investments for the year ended June 30, 2013 (in thousands of dollars):

	Beginning balance as of July 1, 2012	Net realized gains/ (losses)	Net change in unrealized gains/(losses)*	Purchases/ contributions	Sales/ distributions	Transfers into Level 3**	Transfers out of Level 3**	Ending balance as of June 30, 2013
INVESTMENT ASSETS:								
Domestic common and convertible equity	$ 1,807,661	$ 245,989	$ 896,942	$ 276,213	$ (579,599)	$ 306,724	$ (650,573)	**$ 2,303,357**
Foreign common and convertible equity	713,439	(1,761)	99,739	1,260,207	(1,149,738)	147	(9,577)	**912,456**
Domestic fixed income	319						(319)	
Emerging market equity and debt	204,712	(13,792)	(10,855)	202,352	(261,429)		(57,514)	**63,474**
High yield	595,763	12,784	64,578	32,882	(305,634)	211,292	(376,403)	**235,262**
Absolute return	2,017,046	167,631	453,344	1,063,131	(1,609,635)	783,220	(306,724)	**2,568,013**
Private equities	7,193,196	627,978	83,993	843,826	(1,392,339)	32,073	(733)	**7,387,994**
Natural resources	5,278,303	390,492	(967,722)	604,150	(1,163,304)	71,316	(240,662)	**3,972,573**
Real estate	4,758,542	164,280	835,263	1,123,947	(978,053)			**5,903,979**
Due from brokers	26,302	25,296	(25,333)	20,499	(25,296)		(2,153)	**19,315**
Other investments	7,862	197	13,279					**21,338**
TOTAL INVESTMENT PORTFOLIO ASSETS	**22,603,145**	**1,619,094**	**1,443,228**	**5,427,207**	**(7,465,027)**	**1,404,772**	**(1,644,658)**	**23,387,761**
Interests in trusts held by others	343,798		8,271					**352,069**
TOTAL INVESTMENT ASSETS	**$ 22,946,943**	**$ 1,619,094**	**$ 1,451,499**	**$ 5,427,207**	**$ (7,465,027)**	**$1,404,772**	**$ (1,644,658)**	**$ 23,739,830**
INVESTMENT LIABILITIES:								
Due to brokers	$ 1,270	$ 294	$ 675	$ (3,146)	$ 1,912		$ (345)	**$ 660**
TOTAL INVESTMENT LIABILITIES	**$ 1,270**	**$ 294**	**$ 675**	**$ (3,146)**	**$ 1,912**		**$ (345)**	**$ 660**

* *Total change in unrealized gains/(losses) relating to Level 3 investment assets and investment liabilities still held by the University at June 30, 2013 is $2,228,549 and is reflected in "Realized and unrealized appreciation/(depreciation), net" in the* Statements of Changes in Net Assets.

** *During the fiscal year, the University changed the asset class designation for certain Level 3 investments to better align with the investment exposure; these reclassifications are included in Transfers into Level 3 and Transfers out of Level 3. Additionally, certain investments in public markets and absolute return fund vehicles with liquidity provisions available within one year of the measurement date have been reclassified out of Level 3 into Level 2. There were no other transfers between levels for the year.*

The following is a rollforward of Level 3 investments for the year ended June 30, 2012 (in thousands of dollars):

	Beginning balance as of July 1, 2011	Net realized gains/ (losses)	Net change in unrealized gains/(losses)*	Purchases/ contributions	Sales/ distributions	Transfers into Level 3**	Transfers out of Level 3**	Ending balance as of June 30, 2012
INVESTMENT ASSETS:								
Domestic common and convertible equity	$ 1,948,111	$ 134,362	$ 109,828	$ 212,045	$ (653,700)	$ 57,015		**$ 1,807,661**
Foreign common and convertible equity	886,485	38,737	(152,352)	138,770	(238,737)	40,536		**713,439**
Domestic fixed income	12,405	1,680	111	14,133	(23,498)		$ (4,512)	**319**
Emerging market equity and debt	288,984	(50,485)	(93,460)	51,476	(168,518)	176,715		**204,712**
High yield	858,459	38,501	30,168	86,320	(229,986)	30,738	(218,437)	**595,763**
Absolute return	2,299,749	255,439	(241,720)	474,511	(986,508)	216,618	(1,043)	**2,017,046**
Private equities	7,312,137	596,506	(453,981)	991,832	(1,294,758)	41,460		**7,193,196**
Natural resources	5,239,931	74,733	(109,722)	555,371	(488,583)	6,573		**5,278,303**
Real estate	3,440,667	(2,365)	772,291	1,105,512	(557,563)			**4,758,542**
Due from brokers	63,507	(101)	(19,009)		(18,095)			**26,302**
Other investments	3,677	6	4,179					**7,862**
TOTAL INVESTMENT PORTFOLIO ASSETS	**22,354,112**	**1,087,013**	**(153,667)**	**3,629,970**	**(4,659,946)**	**569,655**	**(223,992)**	**22,603,145**
Interests in trusts held by others	351,408		(7,610)					**343,798**
TOTAL INVESTMENT ASSETS	**$ 22,705,520**	**$ 1,087,013**	**$ (161,277)**	**$ 3,629,970**	**$ (4,659,946)**	**$ 569,655**	**$ (223,992)**	**$ 22,946,943**
INVESTMENT LIABILITIES:								
Due to brokers	$ 9,183	$ (527)	$ (7,913)	$ 527				**$ 1,270**
TOTAL INVESTMENT LIABILITIES	**$ 9,183**	**$ (527)**	**$ (7,913)**	**$ 527**				**$ 1,270**

* *Total change in unrealized gains/(losses) relating to Level 3 investment assets and investment liabilities still held by the University at June 30, 2012 is $(573,061) and is reflected in "Realized and unrealized appreciation/(depreciation), net" in the* Statements of Changes in Net Assets.

** *During the fiscal year, the University changed the asset class designation for certain Level 3 investments to better align with the investment exposure; these reclassifications are included in Transfers into Level 3 and Transfers out of Level 3. Additionally, certain investments in public markets and absolute return fund vehicles with liquidity provisions available within one year of the measurement date have been reclassified out of Level 3 into Level 2. There were no other transfers between levels for the year.*

Investments that trade in inactive markets, but are valued based on quoted market prices, broker/dealer quotations, or independent pricing services supported by observable inputs are primarily classified within Level 2. These may include non-exchange traded equity and fixed income securities, securities subject to restriction, and certain over the counter derivatives. Other investments, including over the counter derivatives valued using independent broker quotes or other industry standard models, where unobservable inputs may have been obtained from third parties, have been classified as Level 3 in accordance with the fair value hierarchy under ASC 820.

The University is a limited partner in private equity and real estate partnerships, and other external investment managers, which include commitments to make periodic contributions in future periods. The amounts of these expected disbursements as of June 30, 2013 and 2012 are disclosed below (in thousands of dollars):

	As of June 30, 2013			As of June 30, 2012		
	Fair value*	Remaining unfunded commitments	Estimated remaining life (unaudited)**	Fair value*	Remaining unfunded commitments	Estimated remaining life (unaudited)**
Private equities	$ 5,839,037	$ 2,293,811	4 – 10	$ 6,494,120	$ 2,382,070	4 – 10
Real estate	2,694,348	1,376,584	4 – 10	2,908,048	1,568,704	4 – 10
Other externally managed funds***	819,202	567,246	2 – 8	1,156,885	624,765	2 – 8
TOTAL	**$ 9,352,587**	**$ 4,237,641**		**$ 10,559,053**	**$ 4,575,539**	

* *Represents the fair value of the funded portion of investments with remaining unfunded commitments.*

** *The estimated remaining lives of these funds, expressed in years, are forward-looking projections based on the University's estimates and could vary significantly depending on the investment decisions of external managers, changes in the University's investment portfolio, and other circumstances.*

*** *Investments in other externally managed funds primarily include exposures to absolute return, natural resources, domestic, foreign, and emerging equities, and high yield asset classes.*

The nature of these partnership interests is that distributions are received through the liquidation of the underlying assets of the partnership over its remaining life. The fair value of the investments in these asset classes has generally been estimated using the University's capital account balance with each partnership, unless the University has deemed the NAV to be an inappropriate representation of fair value. In evaluating the level at which the University's externally managed investments have been classified within this hierarchy, the University has assessed factors including, but not limited to, the external advisor's adherence to fair value principles in calculating the capital account balance, the University's ability to redeem these investments at NAV at the measurement date, and the existence or absence of certain restrictions at the measurement date. Investments in externally managed funds generally have limited redemption options for investors and, subsequent to final closing, may or may not permit subscriptions by new or existing investors. These entities may also have the ability to impose gates, lockups, and other restrictions on an investor's ability to readily redeem out of their investment interest in the fund. While the University generally classifies its interest in these types of entities as Level 3, certain interests in public markets and absolute return fund vehicles with liquidity provisions available within one year of the measurement date have been classified as Level 2 within the aforementioned fair value hierarchy.

The University also invests directly in natural resources assets, specifically timberland and agriculture, as well as real estate properties, that are primarily valued using a combination of independent appraisals and other industry standard methodologies, as applicable. The University strives to corroborate information from third-party sources for relevance and accuracy; these valuations are subject to review and consideration by HMC management and the HMC Board of Directors. The valuation process encompasses a wide range of procedures that in the aggregate allow the University to assert as to the adequacy of the fair values reported as of the measurement date. The HMC Board of Directors discusses the valuation process and results with HMC management, and, as necessary, makes determinations on issues regarding valuation matters that may arise.

The valuation procedures performed on these assets are based on industry standard processes for each respective asset class. The inputs utilized in any valuation model may be significant and unobservable, and require a certain degree of judgment. The University examines market data and collaborates closely with industry experts to attempt to arrive at the best estimation of fair value for each respective asset. While the inputs described below represent the range of inputs utilized as of the measurement date, these inputs may change over time, which may have a material effect on the valuation of these types of investments in the future. Additionally, there may be interrelationships between the unobservable inputs utilized in any valuation model, and significant changes in any of those inputs, in isolation or in the aggregate, may trigger changes in other inputs or in the estimated fair value for each respective investment asset. The University has not assessed the sensitivity to unforeseeable changes in significant unobservable inputs; rather, the range of inputs described below illustrate those inputs utilized by the University in arriving at fair value for these direct investments as of the measurement date.

As of June 30, 2013	
Significant unobservable input by asset class*	Range of inputs utilized in valuation model**
Natural resources:	
Income approach discount rate	4.0% – 13.0%
Price per planted hectare	$1,625 – $88,451
Real estate:	
Income approach discount rate	7.0% – 20.0%
Capitalization rate	5.0% – 9.5%
Net operating income growth rate	2.0% – 5.0%

* *The fair value of investments may be determined using multiple valuation techniques.*

** *The range of inputs encompasses a variety of investment types within each asset class.*

5. DERIVATIVES

The University uses a variety of financial instruments with off-balance sheet risk involving contractual or optional commitments for future settlement, which are exchange traded or executed over the counter. These instruments are used to increase or decrease exposure to a given asset class, with the goal of enhancing the returns of said asset classes. The market risk of a strategy is influenced by the relationship between the financial instruments with off-balance sheet risk and the offsetting positions recorded in the *Balance Sheets*. The University manages exposure to market risk through the use of industry standard analytical tools that measure the market exposure of each position within a strategy. The strategies are monitored daily, and positions are frequently adjusted in response to changes in the financial markets.

The following table presents the gross fair values and the net profit/(loss) from derivatives by primary risk exposure for the years ended June 30, 2013 and 2012 (in thousands of dollars):

	As of June 30, 2013		For the year ended June 30, 2013	As of June 30, 2012		For the year ended June 30, 2012
Primary risk exposure	Gross derivative assets	Gross derivative liabilities	Net profit/ (loss)****	Gross derivative assets	Gross derivative liabilities	Net profit/ (loss)****
Equity instruments:						
Equity futures	$ 8,429	$ 430	$ 27,216		$ 3,615	$ 58,307
Equity options	54,700	38,917	(28,859)	$ 58,236	31,730	7,871
Equity exchange agreements	50,132	145,663	347,357	83,168	55,589	(488,127)
TOTAL EQUITY INSTRUMENTS	**113,261**	**185,010**	**345,714**	**141,404**	**90,934**	**(421,949)**
Fixed income instruments:						
Fixed income futures	16,950	16,746	9,222	10,069	5,075	(113,800)
Fixed income options	4,156	4,105	29	5,409	4,194	796
Interest rate exchange agreements*	1,101,492	934,331	86,911	776,602	1,070,542	(205,686)
Interest rate caps and floors	262,803	229,478	35,059	169,899	172,167	303
TOTAL FIXED INCOME INSTRUMENTS	**1,385,401**	**1,184,660**	**131,221**	**961,979**	**1,251,978**	**(318,387)**
Commodity instruments:						
Commodity futures	6,434	19,117	14,731	26,619	30,052	19,898
Commodity options	4,998	1	(2,845)	53,846	41,019	2,706
Commodity exchange agreements	14,286	12,501	4,169	42,660	18,109	(62,253)
TOTAL COMMODITY INSTRUMENTS	**25,718**	**31,619**	**16,055**	**123,125**	**89,180**	**(39,649)**
Currency instruments:						
Currency forwards	2,004,240	1,994,898	37,563	1,780,893	1,777,928	71,673
Currency options	71,386	53,268	(14,843)	42,498	11,581	(2,087)
Currency exchange agreements	11,819	9,713	(6,814)	34,649	21,013	4,558
TOTAL CURRENCY INSTRUMENTS	**2,087,445**	**2,057,879**	**15,906**	**1,858,040**	**1,810,522**	**74,144**
CREDIT INSTRUMENTS	**44,992**	**23,300**	**(20,428)**	**47,071**	**34,878**	**(6,099)**
SUBTOTAL	**3,656,817**	**3,482,468**	**$ 488,468**	**3,131,619**	**3,277,492**	**$ (711,940)**
Counterparty netting**	(3,341,313)	(3,341,313)		(2,820,570)	(2,820,556)	
TOTAL* **	**$ 315,504**	**$ 141,155**		**$ 311,049**	**$ 456,936**	

* *For the year ended June 30, 2013, includes gross derivative liabilities of $6,039 and a net profit of $9,067, related to interest rate exchange agreements on the University's debt portfolio. For the year ended June 30, 2012, includes $11,531 and $393,424 of gross derivative assets and liabilities, respectively, and a net profit/(loss) of $(140,219), related to interest rate exchange agreements on the University's debt portfolio. These positions are further discussed in* Note 12.

** *GAAP permits the netting of derivative assets and liabilities and the related cash collateral received and paid when a legally enforceable master netting agreement exists between the University and a derivative counterparty.*

*** *Included within the "Investment portfolio, at fair value" and "Securities lending and other liabilities associated with the investment portfolio" line items of the* Balance Sheets.

**** *Included within the "Realized and unrealized appreciation/(depreciation), net" line items of the* Statements of Changes in Net Assets.

The following section details the accounting for each type of derivative contract, as well as the University's intended purpose for entering into each type of derivative instrument.

Options

The University purchases and sells put and call options to take advantage of expected volatility in the price of underlying instruments. When purchasing an option, the University pays a premium, which is recorded as an asset and subsequently marked-to-market to reflect the current value of the option. When the University sells (writes) an option, the premium received is recorded as a liability and subsequently marked-to-market to reflect the current fair value of the option written. Premiums paid or received from options that expire unexercised are treated as realized losses and gains, respectively. When an option is closed before expiration or exercise, the University records a realized gain or loss equal to the difference between the proceeds paid/received upon closing and the original premium paid/received.

During fiscal years 2013 and 2012, the University transacted approximately 400 and 500 equity and fixed income option trades with an average transaction size of approximately 8,500 and 2,500 contracts, respectively. Additionally, during the same period the University transacted approximately 500 and 400 currency option contracts with average USD equivalent notional amounts of approximately $18.0 million and $23.0 million per contract, respectively.

Swap contracts

The University enters into swap contracts, which are contracts between two parties to exchange future cash flows at periodic intervals based on a notional principal amount, to increase or decrease its exposure to changes in the level of interest rates, underlying asset values and/or credit risk. Payments are exchanged at specified intervals, accrued daily commencing with the effective date of the contract and recorded as realized gains or losses. Gains or losses are realized in the event of an early termination of a swap contract. Risks of loss may include unfavorable changes in the returns of the underlying instruments or indexes, adverse fluctuations of interest rates, failure of the counterparty to perform under the terms of the agreement, and lack of liquidity in the market.

Collateral in the form of securities or cash may be posted to or received from the swap counterparty in accordance with the terms of the swap contract. Realized gains or losses are recorded relating to periodic payments received or made on swap contracts and with respect to swaps that are closed prior to termination date. When the University enters into a swap transaction, it may make or receive a payment equal to the value of the swap on the entry date and amortizes such payments to realized gain or loss over the outstanding term of the swap. The terms of the swap contracts can vary, and they are reported at fair value based on a valuation model or a counterparty provided price.

In the normal course of its trading activities, the University enters into credit default, interest rate, and total return swap contracts.

Credit default contracts

The University enters into credit derivatives to simulate long and short bond exposure that is either unavailable or considered to be less attractively priced in the bond market, or to hedge exposure obtained in the bond market. The University also uses these derivatives to reduce risk where it has exposure to the issuer, or to take an active long or short position with respect to the likelihood of an event of default. The underlying debt security on which the derivative is structured can be based on a single issuer, a "basket" of issuers, or an index. During fiscal years 2013 and 2012, the University transacted approximately 600 and 700 credit default contracts with average notional amounts of approximately $8.0 million and $22.0 million, respectively.

In instances where the University has purchased credit protection on an underlying debt security, the University is obligated to pay the seller of the credit protection a periodic stream of payments over the term of the contract in return for a contingent payment upon the occurrence of a credit event with respect to the issuer of the debt security. The contingent payment may be a cash settlement or a physical delivery of the debt security in return for payment of the face amount of the obligation. The amount paid for purchased protection is typically a nominal percentage of the notional amount. In instances where the University has sold credit protection on an underlying debt security, the University receives a fixed rate of income throughout the term of the contract, which typically is between one month and five years, and in some instances up to ten years. In the case where the University sold credit protection, if a credit event occurs, the University may cash settle the contract or pay the purchaser of credit protection the full notional value of the contract in exchange for the debt security.

As of June 30, 2013, the University's purchased and written credit derivatives had gross notional amounts of $1,400.9 million and $444.0 million, respectively, for total net purchased protection of $956.9 million in notional value.

As of June 30, 2012, the University's purchased and written credit derivatives had gross notional amounts of $1,784.4 million and $261.0 million, respectively, for total net purchased protection of $1,523.4 million in notional value.

The table below summarizes certain information regarding credit protection purchased and written as of June 30, 2013 and 2012 (in thousands of dollars):

As of June 30, 2013								
	Purchased protection		Written protection					
			Years to maturity					
Credit rating on underlying	Purchased notional*	Purchased fair value	< 5 years	5-10 years	Total written notional	Offsetting purchased notional**	Net written notional	Net written fair value
A- to AAA	$ 698,486	$ 967		$ 65,000	$ 65,000	$ 17,000	$ 48,000	$ (2,008)
BBB- to BBB+	402,249	(92)	$ 64,249		64,249	15,250	48,999	(206)
Non-investment grade	225,686	22,146	313,039	1,724	314,763	42,250	272,513	888
TOTAL	**$ 1,326,421**	**$ 23,021**	**$ 377,288**	**$ 66,724**	**$ 444,012**	**$ 74,500**	**$ 369,512**	**$ (1,326)**

As of June 30, 2012								
	Purchased protection		Written protection					
			Years to maturity					
Credit rating on underlying	Purchased notional*	Purchased fair value	< 5 years	5-10 years	Total written notional	Offsetting purchased notional**	Net written notional	Net written fair value
A- to AAA	$ 654,143	$ 2,777	$ 75,000	$ 23,000	$ 98,000	$ 12,000	$ 86,000	$ (3,269)
BBB- to BBB+	854,000	769	50,000		50,000		50,000	3,601
Non-investment grade	252,208	31,922	113,042		113,042	12,000	101,042	(23,606)
TOTAL	**$ 1,760,351**	**$ 35,468**	**$ 238,042**	**$ 23,000**	**$ 261,042**	**$ 24,000**	**$ 237,042**	**$ (23,274)**

* *Amounts shown are net of purchased credit protection that directly offsets written credit protection, as discussed in the note (**) below.*

** *Offsetting purchased credit derivatives represent the notional amount of purchased credit derivatives to the extent they hedge written credit derivatives with identical underlying debt securities.*

Credit ratings on the underlying debt security, together with the period of expiration, are indicators of payment/performance risk. For example, the seller of credit protection is least likely to pay or otherwise be required to perform where the credit ratings are AAA and the period of expiration is "< 5 years". The likelihood of payment or performance is generally greater as the credit ratings fall and period of expiration increases.

Interest rate contracts

The University enters into interest rate swaps to hedge certain investment positions against interest rate fluctuations; to benefit from interest rate fluctuations; to obtain better interest rate terms than it would have been able to get without the swap; or to manage the interest, cost, and risk associated with its outstanding and/or future debt. Interest rate swaps involve the exchange by the University with another party of its respective commitments to pay or receive interest at specified intervals based on a notional amount of principal. During fiscal years 2013 and 2012, the University transacted approximately 3,400 and 3,500 interest rate swap and cap/floor contracts with average notional amounts of approximately $225.0 million and $200.0 million, respectively.

Total return swaps

The University enters into total return swaps to manage its exposure to market fluctuations in various asset classes. Total return swaps involve commitments to pay interest in exchange for a market linked return, both based on notional amounts. To the extent the total return of the security or index underlying the transaction exceeds or falls short of the offsetting interest rate obligation, the University will receive a payment from or make a payment to the counterparty, respectively. During fiscal years 2013 and 2012, the University transacted approximately 500 and 400 commodity swap contracts with average notional amounts of approximately $6.0 million and $12.0 million; 1,400 and 700 equity swap contracts with average notional amounts of approximately $1.5 million and $10.0 million; and 200 and 200 currency swap contracts with average notional amounts of approximately $25.0 million and $8.0 million, respectively.

Forward currency contracts

The University enters into forward currency contracts in connection with settling planned purchases or sales of securities, or to hedge the currency exposure associated with some or all of the University's portfolio securities. A forward currency contract is an agreement between two parties to buy and sell a currency at a set price on a future date. The value of a forward currency contract fluctuates with changes in forward currency exchange rates. Forward currency contracts are marked-to-market daily and the change in fair value is recorded by the University as an unrealized gain or loss. During fiscal years 2013 and 2012, the University transacted approximately 7,000 and 5,700 forward currency contracts with average USD equivalent notional amounts of approximately $3.0 million and $3.0 million, respectively.

Futures contracts

The University uses futures contracts to manage its exposure to financial markets, including hedging such exposures. Buying futures tends to increase the University's exposure to the underlying instrument, while selling futures tends to decrease exposure to the underlying instrument. Upon entering into a futures contract, the University is required to deposit with its prime broker an amount of cash or securities in accordance with the initial margin requirements of the broker or exchange. Futures contracts are marked-to-market daily based on settlement prices established by the board of trade or exchange on which they are traded, and an appropriate payable or receivable for the change in fair value is recorded by the University. Gains and losses are realized when the contracts expire or are closed. During fiscal years 2013 and 2012, the University transacted approximately 31,800 and 10,000 futures trades with an average transaction size of approximately 50 and 100 contracts, respectively.

Counterparty credit exposure

Financial instruments with off-balance sheet risk involve counterparty credit exposure. The policy of the University is to require collateral to the maximum extent possible under normal trading practices. Collateral, generally in the form of debt obligations issued by the US Treasury, is exchanged on a daily basis as required by fluctuations in the market. In the event of counterparty default, the University has the right to use the collateral held to offset any losses ensuing from the default event. Specific credit limits are established for counterparties based on their individual credit ratings. Credit limits are monitored daily by the University and are adjusted according to policy, as necessary. Some of the financial instruments entered into by the University contain credit-risk-related contingency features that allow the parties to the agreement to demand immediate payment for outstanding contracts and/or collateral. If material credit-risk-related contingency features were triggered on June 30, 2013 and 2012, the additional collateral due to counterparties for derivative contracts would have been $10.4 million and $6.4 million, respectively.

6. RECEIVABLES

The major components of receivables, net of reserves for doubtful accounts of $13.2 million and $12.0 million as of June 30, 2013 and 2012, respectively, were as follows (in thousands of dollars):

	2013	2012
Federal sponsored support	**$ 72,095**	$ 66,902
Publications	**39,758**	37,114
Executive education	**24,351**	23,286
Non-federal sponsored support	**16,822**	13,450
Gift receipts	**14,529**	27,167
Tuition and fees	**12,738**	12,807
Other	**45,857**	46,675
TOTAL RECEIVABLES, NET	**$ 226,150**	**$ 227,401**

7. NOTES RECEIVABLE

Notes receivable are recorded initially at face value plus accrued interest, which approximates fair value. Notes receivable, and the related allowance for doubtful accounts, were as follows (in thousands of dollars):

	2013			2012		
	Receivable	Allowance	Net	Receivable	Allowance	Net
Student loans:						
Government revolving	$ 78,666	$ 2,685	**$ 75,981**	$ 80,039	$ 2,619	**$ 77,420**
Institutional	86,490	2,970	**83,520**	83,931	2,955	**80,976**
Federally insured	722		**722**	985		**985**
Total student loans	165,878	5,655	**160,223**	164,955	5,574	**159,381**
Faculty and staff loans	189,958	422	**189,536**	187,081	422	**186,659**
Other loans	20,358	4,491	**15,867**	22,393	4,867	**17,526**
TOTAL	**$ 376,194**	**$ 10,568**	**$ 365,626**	**$ 374,429**	**$ 10,863**	**$ 363,566**

Government revolving loans are funded principally with federal advances to the University under the Perkins Loan Program and certain other programs. These advances totaled $68.2 million and $67.0 million as of June 30, 2013 and 2012, respectively, and are classified as liabilities in the *Balance Sheets*. Interest earned on the revolving and institutional loan programs is reinvested to support additional loans. The repayment and interest rate terms of the institutional loans vary considerably.

Faculty and staff notes receivable primarily consists of mortgage and educational loans. Mortgages include shared appreciation loans and loans that bear interest at the applicable federal rate. In addition, certain mortgages bear interest at the current market rate, which may be subsidized for an initial period. The educational loans are primarily zero-interest loans.

The University assesses the adequacy of the allowance for doubtful accounts by evaluating the loan portfolio, including such factors as the differing economic risks associated with each loan category, the financial condition of specific borrowers, the economic environment in which the borrowers operate, the level of delinquent loans, the value of any collateral, and, where applicable, the existence of any guarantees or indemnifications. In addition to these factors, the University reviews the aging of the loans receivable and the default rate in comparison to prior years. The allowance is adjusted based on these reviews. The University considers the allowance at June 30, 2013 and 2012 to be reasonable and adequate to absorb potential credit losses inherent in the loan portfolio.

8. PLEDGES RECEIVABLE

Unconditional promises to donate to the University in the future are initially recorded at fair value (pledge net of discount) and subsequently amortized over the expected payment period, net of an allowance for uncollectible pledges. Discounts of $43.8 million and $34.4 million for the years ended June 30, 2013 and 2012, respectively, were calculated using discount factors based on the University taxable unsecured borrowing rate.

Pledges receivable included in the financial statements as of June 30, 2013 and 2012 are expected to be realized as follows (in thousands of dollars):

	2013	2012
Within one year	**$ 214,608**	$ 157,294
Between one and five years	**858,429**	629,175
More than five years	**300,568**	210,582
Less: discount and allowance for uncollectible pledges	**(137,514)**	(88,493)
TOTAL PLEDGES RECEIVABLE, NET	**$1,236,091**	**$ 908,558**

Pledges receivable as of June 30, 2013 and 2012 have been designated for the following purposes (in thousands of dollars):

	2013	2012
General Operating Account balances:		
Gifts for current use	**$ 615,878**	$ 429,859
Non-federal sponsored grants	**102,318**	106,149
Gifts for facilities	**162,699**	62,391
Total General Operating Account balances	**880,895**	598,399
Endowment	**355,196**	310,159
TOTAL PLEDGES RECEIVABLE, NET	**$ 1,236,091**	**$ 908,558**

Because of uncertainties with regard to realizability and valuation, bequest intentions and other conditional promises are only recognized as assets if and when the specified conditions are met. Non-bequest conditional pledges totaled $95.3 million and $63.8 million as of June 30, 2013 and 2012, respectively.

9. FIXED ASSETS

Fixed assets are reported at cost or, if a gift, at fair value as of the date of the gift, net of accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

The major categories of fixed assets as of June 30, 2013 and 2012 are summarized as follows (in thousands of dollars):

	2013	2012	Estimated useful life (in years)
Research facilities	**$ 2,139,280**	$ 2,091,652	*
Classroom and office facilities	**1,667,974**	1,572,065	35
Housing facilities	**1,200,518**	1,173,626	35
Other facilities	**357,273**	526,102	35
Service facilities	**597,034**	568,626	35
Libraries	**440,394**	434,622	35
Museums and assembly facilities	**323,131**	312,214	35
Athletic facilities	**172,089**	167,427	35
Land	**672,222**	698,673	N/A
Construction in progress	**849,654**	719,589	N/A
Equipment	**1,043,040**	950,602	**
SUBTOTAL AT COST	**9,462,609**	9,215,198	
Less: accumulated depreciation	**(3,669,238)**	(3,438,653)	
FIXED ASSETS, NET	**$ 5,793,371**	**$ 5,776,545**	

* *Estimated useful lives of components range from 10 to 45 years.*
** *Estimated useful lives of equipment range from 3 to 8 years.*

Certain University facilities are subject to restrictions as to use, structural modifications, and ownership transfer. Included in the fixed asset balances are restricted facilities with a net book value of $223.6 million and $226.4 million as of June 30, 2013 and 2012, respectively.

The costs of research facilities are separated into the shell, roof, finishes, fixed equipment, and services. These components are separately depreciated.

Equipment includes general and scientific equipment, computers, software, furniture, and vehicles.

The University has asset retirement obligations of $81.6 million and $61.3 million, which are included in the "Deposits and other liabilities" in the *Balance Sheets* as of June 30, 2013 and 2012, respectively.

10. ENDOWMENT AND GENERAL OPERATING ACCOUNT NET ASSETS

The University's endowment consists of approximately 12,370 separate funds established over many years for a wide variety of purposes. Endowment fund balances, including funds functioning as endowment, are classified and reported as unrestricted, temporarily restricted, or permanently restricted net assets in accordance with donor specifications and state law. Net unrealized losses on permanently restricted endowment funds are classified as a reduction to unrestricted net assets until such time as the fair value equals or exceeds historic dollar value. Unrestricted net assets, on a cumulative basis, were reduced by $20.2 million and $23.4 million for such losses in fiscal 2013 and 2012, respectively. Although funds functioning as endowment are not subject to donor restrictions, decisions to spend their principal require the approval of the Corporation. All but a small fraction of the endowment is invested in the GIA (*Note 3*).

The University is also the beneficiary of certain irrevocable trusts held and administered by others. The estimated fair values of trust assets, which include the present values of expected future cash flows from outside trusts and the fair value of the underlying assets of perpetual trusts, are recognized as assets and increases in net assets when the required trust documentation is provided to the University. The fair values of these trusts are provided by the external trustees and are adjusted annually by the University. These are included as Level 3 investments in the fair value hierarchy table in *Note 4*.

The endowment consisted of the following as of June 30, 2013 and 2012 (in thousands of dollars):

	2013				2012
	Unrestricted	Temporarily restricted	Permanently restricted	Total	Total
Endowment funds	$ (20,194)	$ 18,439,223	$ 5,313,666	**$ 23,732,695**	$ 22,245,420
Funds functioning as endowment	5,629,211	2,672,827		**8,302,038**	7,897,278
Pledge balances		24,811	330,385	**355,196**	310,159
Interests in trusts held by others		13,377	286,183	**299,560**	292,677
TOTAL ENDOWMENT	**$ 5,609,017**	**$ 21,150,238**	**$ 5,930,234**	**$ 32,689,489**	**$ 30,745,534**

The University's endowment distribution policies are designed to preserve the value of the endowment in real terms (after inflation) and generate a predictable stream of available income. Each fall, the Corporation approves the endowment distribution for the following fiscal year. The endowment distribution is based on presumptive guidance from a formula that is intended to provide budgetary stability by smoothing the impact of annual investment gains and losses. The formula's inputs reflect expectations about long-term returns and inflation rates. For fiscal 2013, the endowment distribution approved by the Corporation (prior to decapitalizations) was equal to 5.1% of the fair value of the endowment invested in the GIA as of the beginning of the fiscal year. The total endowment distribution made available for operations was $1.5 billion and $1.4 billion in fiscal 2013 and 2012, respectively.

Each year the Corporation also approves certain decapitalizations from the endowment to support strategic, mission-critical activities or objectives that are typically one-time or time-limited. These decapitalizations totaled $157.4 million and $308.5 million in fiscal 2013 and 2012, respectively. These additional decapitalizations, in combination with the endowment distribution, resulted in an aggregate payout rate of 5.5% in fiscal 2013 and 2012.

The GOA consists of the general or current funds of the University as well as the assets and liabilities related to student and faculty loans and facilities. The GOA accepts, manages, and pays interest on deposits made by University departments; invests surplus working capital; makes loans; and arranges external financing for major capital projects. It is used to manage, control, and execute all University financial transactions, except for those related to investment activities conducted by HMC.

The GOA consisted of the following as of June 30, 2013 and 2012 (in thousands of dollars):

	2013				2012
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
General Operating Account	$ 3,286,843	$ 1,960,942	$ 96,970	**$ 5,344,755**	**$ 4,288,513**

The temporarily restricted net assets of the GOA consist primarily of unexpended income, gifts, and pledges. The permanently restricted net assets of the GOA are loan funds.

11. SPLIT INTEREST AGREEMENTS

Under split interest agreements, donors enter into trust arrangements with the University in which the University receives benefits that are shared with other beneficiaries and institutions. Split interest agreement (SIA) investment assets are invested primarily in the GIA and publicly traded securities, a small segment is managed by an external advisor, and all are recorded at fair value as discussed in *Notes 3* and *4*. The publicly traded securities are included as Level 1 and externally managed investments are included as Level 3 investments in the fair value hierarchy table in *Note 4*. Associated liabilities are recorded at the present value of estimated future payments due to beneficiaries and other institutions. These liabilities were calculated using discount factors based on the appropriate US Treasury Note rates for gifts received prior to the adoption of ASC 820, and using the University's current taxable unsecured borrowing rate for gifts received beginning in fiscal 2009.

The changes in split interest agreement net assets for fiscal 2013 and 2012 were as follows (in thousands of dollars):

	2013			2012
	Temporarily restricted	Permanently restricted	Total	Total
Investment return:				
Investment income	$ 3,623	$ 11,045	**$ 14,668**	$ 13,963
Realized and unrealized appreciation/(depreciation), net	23,798	72,555	**96,353**	(27,809)
Total investment return	27,421	83,600	**111,021**	(13,846)
Gifts for capital (*Note 16*)*	16,836	14,981	**31,817**	20,168
Payments to annuitants	(14,430)	(43,994)	**(58,424)**	(58,257)
Transfers to endowment	(3,815)	(40,979)	**(44,794)**	(58,267)
Transfers between SIA and the GOA	(18,695)	(25)	**(18,720)**	(14,235)
Change in liabilities and other adjustments	(604)	(1,520)	**(2,124)**	156,896
NET CHANGE DURING THE YEAR	**6,713**	**12,063**	**18,776**	**32,459**
Total split interest agreement net assets, beginning of year	**70,705**	**479,543**	**550,248**	517,789
TOTAL SPLIT INTEREST AGREEMENT NET ASSETS, end of year	**$ 77,418**	**$ 491,606**	**$ 569,024**	**$ 550,248**

* *Shown at net present value. The undiscounted value of these gifts was $60,481 and $51,045 for the years ended June 30, 2013 and 2012, respectively.*

Split interest agreement net assets as of June 30, 2013 and 2012 consisted of the following (in thousands of dollars):

	2013	2012
Split interest agreement investments (*Note 3*):		
Charitable remainder trusts	**$ 834,042**	$ 786,258
Charitable lead trusts	**133,551**	115,618
Charitable gift annuities	**207,215**	213,847
Pooled income funds	**111,541**	104,767
Total split interest agreement investments	**1,286,349**	1,220,490
Liabilities due under split interest agreements:		
Amounts due to beneficiaries	**(599,093)**	(560,474)
Amounts due to other institutions	**(118,232)**	(109,768)
Total liabilities due under split interest agreements	**(717,325)**	(670,242)
TOTAL SPLIT INTEREST AGREEMENT NET ASSETS, end of year	**$ 569,024**	**$ 550,248**

12. BONDS AND NOTES PAYABLE

Bonds and notes payable as of June 30, 2013 and 2012 were as follows (in thousands of dollars):

	Fiscal year of issue	Years to final maturity*	One-year yield**	Outstanding principal 2013***	2012****
Tax-exempt bonds and notes payable:					
Variable-rate bonds and notes payable:					
Series R - daily	2000-2006	19	0.1%	**$ 131,200**	$ 131,200
Series Y - weekly	2000	22	0.2	**117,905**	117,905
Commercial paper	2012	<1	0.2	**289,299**	288,735
Total variable-rate bonds and notes payable			0.2	**538,404**	537,840
Fixed-rate bonds:					
Series N	1992	7	6.3	**79,311**	79,210
Series Z	2001	0	5.7		10,143
Series FF	2003	24	5.1		185,154
Series 2005A	2005	23	4.8	**92,886**	93,049
Series 2005B	2006	19	4.8	**104,135**	104,324
Series 2005C	2006	22	4.9	**129,315**	129,469
Series 2008B	2008	25	4.8	**215,565**	215,829
Series 2009A	2009	23	5.5	**983,304**	984,205
Series 2010A	2010	21	4.5	**520,172**	523,579
Series 2010B	2011	27	4.7	**654,163**	657,918
Total fixed-rate bonds			5.0	**2,778,851**	2,982,880
Total tax-exempt bonds and notes payable			**4.2**	**3,317,255**	**3,520,720**
Taxable bonds and notes payable:					
Series 2006A	2006	24	6.3		401,459
Series 2008A	2008	25	5.0	**242,844**	387,805
Series 2008C	2008	5	5.3	**125,205**	125,205
Series 2008D	2009	26	6.3	**997,119**	996,820
Series 2010C	2011	27	4.9	**298,172**	298,105
Series 2013A	2013	24	3.4	**402,000**	
Commercial paper	2012	<1	0.2	**158,347**	158,007
Total taxable bonds and notes payable			**5.4**	**2,223,687**	**2,367,401**
Other notes payable	Various	Various	Various	**147,065**	151,018
TOTAL BONDS AND NOTES PAYABLE			**4.7%**	**$ 5,688,007**	**$ 6,039,139**

* *The weighted average maturity of the portfolio on June 30, 2013 was 17.1 years.*

** *Exclusive of interest rate exchange agreements. Inclusive of these agreements, the overall portfolio rate was 4.9%.*

*** *Series N, 2008A, 2008D, 2009A and 2010C principal are net of $0.7 million, $0.2 million, $2.9 million, $16.7 million and $1.8 million of discounts, respectively. Series 2005A, 2005B, 2005C, 2008B, 2010A and 2010B principal include premiums of $3.8 million, $3.6 million, $3.4 million, $6.7 million, $40.2 million and $53.1 million, respectively.*

**** *Series N, FF, 2006A, 2008A, 2008D, 2009A and 2010C principal are net of $0.8 million, $1.3 million, $0.5 million, $0.2 million, $3.2 million, $15.8 million and $1.9 million of discounts, respectively. Series 2005A, 2005B, 2005C, 2008B, 2010A and 2010B principal include premiums of $3.9 million, $3.8 million, $3.6 million, $7.0 million, $43.6 million and $56.9 million, respectively.*

Interest expense related to bonds and notes payable was $265.1 million and $285.8 million for fiscal 2013 and 2012, respectively. The interest expense in the *Statements of Changes in Net Assets with General Operating Account Detail* includes additional components related to capital leases. Excluding maturity of commercial paper and unamortized discounts and premiums, scheduled principal payments are (in thousands of dollars):

Fiscal year	Principal payments
2014	$ 65,935
2015	38,603
2016	38,601
2017	29,724
2018	34,716
Thereafter	4,944,296
TOTAL PRINCIPAL PAYMENTS	**$ 5,151,875**

In fiscal 2013, the University defeased the Series 2006A bonds of $402 million by exercising the bonds' call option. The redemption cost of these bonds was funded primarily with proceeds from the sale of the Series 2013A bonds, also completed during fiscal 2013. A $69.8 million loss representing the defeasance cost of the Series 2006A bonds is reflected in the "Other changes" line of the *Statements of Changes in Net Assets with General Operating Account Detail* and in "Debt repayments" on the *Statements of Cash Flows*.

In fiscal 2013, the University redeemed the full outstanding amount of $161.5 million of the Series FF bonds using cash on hand, while $25.0 million of the bonds matured as scheduled. As a result, none of the Series FF bonds were outstanding at June 30, 2013.

In fiscal 2013, the University entered into a $1.0 billion unsecured, revolving credit facility with a syndicate of banks, which expires in January 2014. An additional $1.0 billion unsecured, revolving credit facility with the same syndicate of banks (originally entered into in fiscal 2012) remains in place and expires in January 2017. There was no outstanding balance on either of these credit facilities at June 30, 2013 or June 30, 2012.

In fiscal 2013, the University's AAA/Aaa credit ratings were affirmed by Standard & Poor's Ratings Services and Moody's Investors Service, respectively.

As of June 30, 2013, the University had $249.1 million of variable-rate demand bonds outstanding (excluding commercial paper) with either a daily or weekly interest rate reset, as noted in the bonds and notes payable table on page 35. In the event that the University receives notice of any optional tender on its variable-rate demand bonds, or if the bonds become subject to mandatory tender, the purchase price of the bonds will be paid from the remarketing of such bonds. However, if the remarketing proceeds are insufficient, the University will have a general obligation to purchase the bonds tendered with cash on hand.

In fiscal 2012, the University redeemed Series DD and Series GG2 bonds in full ($135.9 million and $16.6 million, respectively) by exercising the bonds' call options, and $200.0 million of the Series 2008D bonds, scheduled to mature in 2014, by exercising the bonds' make-whole call option. The redemption price of these bonds was funded with cash on hand.

The estimated fair value of the University's outstanding bonds and notes payable, including accrued interest, was $6,404.5 million and $7,213.9 million as of June 30, 2013 and June 30, 2012, respectively.

Interest rate exchange agreements

The University has entered into various interest rate exchange agreements in order to manage the interest cost and risk associated with its outstanding debt and to hedge issuance of future debt. The interest rate exchange agreements were not entered into for trading or speculative purposes. Each of these agreements is collateralized, as described in *Note 5*, and thereby carries liquidity risk to the extent the relevant agreements have negative fair values (pursuant to methodologies described below).

In fiscal 2013, the University terminated interest rate exchange agreements with a notional amount of $942.0 million, for which it realized a loss of $345.3 million.

In fiscal 2012, the University terminated interest rate exchange agreements with a notional amount of $756.0 million, for which it realized a loss of $134.6 million. In addition, interest rate exchange agreements with $207.8 million notional value matured during fiscal 2012.

The fair value of the interest rate exchange agreements is the estimated amount that the University would have received or (paid), including accrued interest, to terminate the agreements on the dates of the *Balance Sheets*. The notional amount and fair value of the interest rate exchange agreements were $125.4 million and $(6.0) million, respectively, as of June 30, 2013 and $1,075.6 million and $(381.9) million, respectively, as of June 30, 2012. The fair value of these agreements is included in the "Securities lending and other liabilities associated with the investment portfolio" line in the *Balance Sheets*.

The expense realized related to the interest rate exchange agreements was $14.6 million and $23.0 million for fiscal 2013 and 2012, respectively. All unrealized and realized gains and losses from interest rate exchange agreements are included in the "Realized and unrealized appreciation/(depreciation), net" line in the *Statements of Changes in Net Assets with General Operating Account Detail*.

NOTIONAL AMOUNT OF INTEREST RATE EXCHANGE AGREEMENTS
In thousands of dollars

Beginning balance, July 1, 2012	$ 1,075,555
Interest rate exchange agreements terminated/matured	(942,000)
Interest rate exchange agreement notional amortization	(8,165)
ENDING BALANCE, JUNE 30, 2013	**$ 125,390**

The University determines the fair value of its existing fixed rate debt obligations based on trade data, broker/dealer quotes, and other observable market data. The carrying amounts of its variable rate debt obligations approximate fair value because the obligations are currently callable at a price equal to the carrying amounts. The University considers this to be a Level 2 measurement.

13. EMPLOYEE BENEFITS

The University offers current employees a choice of health plans, a dental plan, short-term and long-term disability plans, life insurance, tuition assistance, and a variety of other benefits such as subsidized passes for public transportation and for Harvard athletic facilities. In addition, the University has retirement plans covering substantially all employees.

The University uses a measurement date of June 30 for its pension and postretirement health plans.

Pension benefits

All eligible faculty members and staff are covered by retirement programs that include a defined benefit component, a defined contribution component, or a combination of the two.

In accordance with the Employee Retirement Income Security Act (ERISA) requirements, the University has established a trust to hold plan assets for its defined benefit pension plans. The fair value of the trust's assets was $758.9 million and $755.4 million as of June 30, 2013 and 2012, respectively. During fiscal year 2012, the University used $36.9 million of internally designated funds for a discretionary defined benefit pension plan contribution. The University recorded expenses for its defined contribution plans of $116.4 million and $110.3 million for fiscal 2013 and 2012, respectively. Gross benefits paid for pensions were $42.2 million and $41.0 million for the years ended June 30, 2013 and 2012, respectively.

Postretirement health benefits

The University provides postretirement health coverage and life insurance to substantially all of its employees. As of June 30, 2013, the University had internally designated and invested $403.1 million to fund the postretirement health benefit accrued liability of $674.0 million. As of June 30, 2012, the University had internally designated and invested $339.0 million to fund an accrued liability of $901.5 million.

The following table sets forth the pension and postretirement plans' funded status that is reported in the *Balance Sheets* as of June 30, 2013 and 2012 (in thousands of dollars):

	Pension benefits		Postretirement health benefits	
	2013	2012	2013	2012
Change in projected benefit obligation:				
Projected benefit obligation, beginning of year	**$ 909,909**	$ 782,567	**$ 901,470**	$ 782,219
Service cost	**15,336**	13,514	**43,646**	32,748
Interest cost	**39,906**	43,200	**42,521**	46,628
Plan participants' contributions			**3,425**	3,089
Plan change*	**2,900**			(41,605)
Gross benefits paid	**(42,230)**	(41,013)	**(18,050)**	(26,660)
Expected federal subsidy on benefits paid				790
Actuarial (gain)/loss	**(86,928)**	107,811	**(299,046)**	104,261
Special termination benefits		3,830		
PROJECTED BENEFIT OBLIGATION, end of year	**838,893**	**909,909**	**673,966**	**901,470**
Change in plan assets:				
Fair value of plan assets, beginning of year	**755,364**	746,901		
Actual return on plan assets	**45,700**	8,768		
Employer contributions	**68**	40,708		
Gross benefits paid	**(42,230)**	(41,013)		
FAIR VALUE OF PLAN ASSETS, end of year	**758,902**	**755,364**	**0**	**0**
UNFUNDED STATUS	**$ (79,991)**	**$ (154,545)**	**$ (673,966)**	**$ (901,470)**

* *The 2013 pension current year service cost relates to a change in the calculation for certain participants hired before 1973. The 2012 postretirement current year prior service credit was primarily due to the introduction of a medical deductible and co-insurance and a new cost sharing program for pharmacy.*

The accumulated benefit obligation associated with pension benefits was $733.9 million and $791.5 million at June 30, 2013 and 2012, respectively. The funded status disclosed above has been prepared in accordance with pension accounting rules. When measured on an IRS funding basis, which informs the University's required cash contribution amount, the plan was overfunded at January 1, 2013.

Net periodic benefit (income)/cost

Components of net periodic benefit (income)/cost recognized in operating activity and other amounts recognized in non-operating activity in unrestricted net assets in the *Statements of Changes in Net Assets with General Operating Account Detail* are summarized as follows for the years ended June 30 (in thousands of dollars):

	Pension benefits		Postretirement health benefits	
	2013	2012	2013	2012
Components of net periodic benefit (income)/cost:				
Service cost	**$ 15,336**	$ 13,514	**$ 43,646**	$ 32,748
Interest cost	**39,906**	43,200	**42,521**	46,628
Expected return on plan assets	**(47,484)**	(48,694)		
Amortization of:				
Actuarial loss/(gain)	**11,867**	264		(4,227)
Prior service (credit)/cost	**(132)**	(1,247)	**(3,179)**	727
Transition obligation				6,062
Cost of special termination benefits		3,830		
Total net periodic benefit cost recognized in operating activity	**19,493**	**10,867**	**82,988**	**81,938**
Other amounts recognized in non-operating activity in unrestricted net assets:				
Current year actuarial (gain)/loss	**(85,143)**	147,737	**(299,046)**	104,261
Amortization of:				
Current year prior service cost/(credit)	**2,900**			(41,605)
Transition obligation				(6,062)
Prior service credit/(cost)	**132**	1,247	**3,179**	(727)
Actuarial (loss)/gain	**(11,867)**	(264)		4,227
Total other amounts recognized in non-operating activity*	**(93,978)**	**148,720**	**(295,867)**	**60,094**
Total recognized in *Statements of Changes in Net Assets with General Operating Account Detail*	**$ (74,485)**	**$ 159,587**	**$ (212,879)**	**$ 142,032**

Cumulative amounts recognized as non-operating changes in unrestricted net assets are summarized as follows for the years ended June 30 (in thousands of dollars):

	2013	2012	2013	2012
Net actuarial loss/(gain)	**$ 44,150**	$ 141,160	**$ (209,483)**	$ 89,563
Prior service cost/(credit)	**3,150**	118	**(32,350)**	(35,529)
Cumulative amounts recognized in unrestricted net assets*	**$ 47,300**	**$ 141,278**	**$ (241,833)**	**$ 54,034**

* *These amounts totaling ($389.8) million in fiscal 2013 and $208.8 million in fiscal 2012 include gains and losses and other changes in the actuarially determined benefit obligations arising in the current period but that have not yet been reflected within net periodic benefit (income)/cost and are included in the "Change in Retirement Obligations" line in the Statements of Changes in Net Assets with General Operating Account Detail.*

The estimated net actuarial loss and prior service cost for the defined benefit plan that will be amortized from unrestricted net assets into net periodic benefit (income)/cost in fiscal 2014 are $2.1 million and $0.5 million, respectively. The estimated net actuarial gain and estimated prior service credit for the postretirement health benefit that will be amortized from unrestricted net assets into net periodic benefit (income)/cost in fiscal 2014 are ($9.8) million and ($3.2) million, respectively.

Assumptions and health care cost trend rates used in determining the year end obligation as well as the net periodic benefit (income)/cost of the pension and postretirement health plans are summarized as follows for fiscal 2013 and 2012:

	Pension benefits		Postretirement health benefits	
	2013	2012	2013	2012
Weighted-average assumptions used to determine benefit obligation as of June 30:				
Discount rate	**4.95%**	4.45%	**5.15%**	4.55%
Compensation increase trend:				
– Initial rate	**3.00%**	4.00%	**3.00%**	4.00%
– Ultimate rate	**4.00%**	4.00%	**4.00%**	4.00%
– Years to ultimate rate	**3**	0	**3**	0
Health care cost trend rate:				
– Initial rate	**N/A**	N/A	**7.00%**	7.00%
– Ultimate rate	**N/A**	N/A	**4.75%**	5.00%
– Years to ultimate rate	**N/A**	N/A	**10**	6
Weighted-average assumptions used to determine net periodic benefit (income)/cost:				
Discount rate	**4.45%**	5.60%	**4.55%**	5.80%
Expected long-term rate of return on plan assets	**7.25%**	7.25%	**N/A**	N/A
Compensation increase trend:				
– Initial rate	**4.00%**	4.00%	**4.00%**	4.00%
– Ultimate rate	**4.00%**	4.00%	**4.00%**	4.00%
– Years to ultimate rate	**0**	0	**0**	0
Health care cost trend rate:				
– Initial rate	**N/A**	N/A	**7.00%**	8.50%
– Ultimate rate	**N/A**	N/A	**5.00%**	5.00%
– Years to ultimate rate	**N/A**	N/A	**6**	7

As an indicator of sensitivity, a one percentage point change in assumed health care cost trend rate would affect 2013 as shown in the following table (in thousands of dollars):

	1% point increase	1% point decrease
Effect on 2013 postretirement health benefits service and interest cost	$ 22,729	$ (16,906)
Effect on postretirement health benefits obligation as of June 30, 2013	129,114	(100,747)

The expected return on pension plan assets is determined by utilizing HMC's capital markets model, which takes into account the expected real return, before inflation, for each of the pension portfolio's asset classes, as well as the correlation of any one asset class to every other asset class. This model calculates the real returns and correlations and derives an expected real return for the entire portfolio, given the percentage weighting allocated to each asset class. After calculating the expected real return, an assessment is made to accommodate the expected inflation rate for the forthcoming period. The final expected return on assets is the aggregate of the expected real return plus the expected inflation rate.

Plan assets

The actual asset allocation of the investment portfolio for the pension plan at June 30, 2013 and 2012, along with target allocations for June 30, 2014, is as follows:

	2014 target	June 30, 2013	June 30, 2012
Asset allocation by category for pension plan:			
Equity securities	30 – 50%	37.5%	42.0%
Fixed income securities	30 – 50	31.8	28.6
Real estate	0 – 10	4.4	6.0
Absolute return	10 – 30	17.2	20.0
Cash	0 – 10	9.1	3.4
TOTAL OF ASSET ALLOCATION CATEGORIES		**100.0%**	**100.0%**

The University's investment strategy for the pension portfolio is to manage the assets across a broad and diversified range of investment categories, both domestic and international. The objective is to achieve a risk-adjusted return that is in line with the long-term obligations that the University has to the pension plan beneficiaries. During fiscal year 2013, the University has continued to increase its allocation to fixed income securities to better manage the interest rate volatility associated with its pension obligations. The University expects to continue this strategy in future years. The investment program is also managed to comply with all ERISA regulations.

The following is a summary of the levels within the fair value hierarchy for the pension plan assets subject to fair value measurement as of June 30, 2013 and 2012 (in thousands of dollars):

	2013				2012			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
INVESTMENT ASSETS:								
Absolute return		$ 123,501	$ 5,340	**$ 128,841**		$ 123,891	$ 24,681	**$ 148,572**
Cash and short-term investments	$ 64,396			**64,396**	$ 34,591			**34,591**
Domestic common and convertible equity	8,517	107,820		**116,337**	6,777	97,881		**104,658**
Domestic fixed income	54,543	140,577		**195,120**	208,820			**208,820**
Due (to)/from broker	(240)	(1,393)		**(1,633)**	235			**235**
Emerging market equity and debt	51,209			**51,209**	51,900			**51,900**
Foreign common and convertible equity	50,849			**50,849**	42,538	46,136		**88,674**
High yield		4,881	1	**4,882**		4,636	4	**4,640**
Private equities			63,145	**63,145**			68,261	**68,261**
Real estate			33,014	**33,014**			42,918	**42,918**
TOTAL INVESTMENT ASSETS*	**$ 229,274**	**$ 375,386**	**$ 101,500**	**$ 706,160**	**$ 344,861**	**$ 272,544**	**$ 135,864**	**$ 753,269**

* *Excludes investment assets not subject to fair value of $52,742 and $2,095 as of June 30, 2013 and 2012, respectively.*

The following is a rollforward of Level 3 investments for the year ended June 30, 2013 (in thousands of dollars):

	Beginning balance as of July 1, 2012	Net realized gains/(losses)	Net change in unrealized gains/(losses)	Purchases/contributions	Sales/distributions	Transfers into Level 3	Transfers out of Level 3	Ending balance as of June 30, 2013
INVESTMENT ASSETS:								
Absolute return	$ 24,681	$ 1,062	$ (369)	$ 19	$ (10,550)	$ 10,571	$ (20,074)	**$ 5,340**
High yield	4	(128)	129		(4)			**1**
Private equities	68,261	9,501	(705)	1,761	(15,673)			**63,145**
Real estate	42,918	1,188	(908)	345	(10,529)			**33,014**
TOTAL INVESTMENT ASSETS	**$ 135,864**	**$ 11,623**	**$ (1,853)**	**$ 2,125**	**$ (36,756)**	**$ 10,571**	**$ (20,074)**	**$ 101,500**

The following is a rollforward of Level 3 investments for the year ended June 30, 2012 (in thousands of dollars):

	Beginning balance as of July 1, 2011	Net realized gains/(losses)	Net change in unrealized gains/(losses)	Purchases/contributions	Sales/distributions	Transfers into Level 3	Transfers out of Level 3	Ending balance as of June 30, 2012
INVESTMENT ASSETS:								
Absolute return	$ 87,999	$ 54	$ (2,496)	$ 21	$ (1,258)	$ 0	$ (59,639)	**$ 24,681**
Foreign common and convertible equity		(4)			4			
High yield			4					**4**
Private equities	72,717	9,179	(1,937)	4,508	(16,206)			**68,261**
Real estate	43,456	780	2,626	1,445	(5,389)			**42,918**
TOTAL INVESTMENT ASSETS	**$ 204,172**	**$ 10,009**	**$ (1,803)**	**$ 5,974**	**$ (22,849)**	**$ 0**	**$ (59,639)**	**$ 135,864**

Expected future benefit payments

Employer contributions of $6 million are expected for fiscal 2014 to fund the pension plans. The following table summarizes expected benefit payments and subsidies for pension and other postretirement benefits for the University (in thousands of dollars):

	Expected benefit payments	
Fiscal year	Pension	Postretirement health
2014	$ 58,646	$ 20,270
2015	53,785	21,965
2016	55,571	23,484
2017	58,317	24,943
2018	58,990	26,553
Thereafter	287,557	164,002

14. STUDENT FINANCIAL AID

Financial aid granted to students in fiscal 2013 and 2012 is summarized as follows (in thousands of dollars):

	2013	2012
Scholarships and other student awards:		
Scholarships applied to student income	**$ 362,532**	$ 357,001
Scholarships and other student awards paid directly to students	**136,360**	128,993
Total scholarships and other student awards	**498,892**	**485,994**
Student employment	**65,964**	64,088
Student loans	**23,200**	22,015
Agency financial aid*	**8,187**	9,158
TOTAL STUDENT FINANCIAL AID	**$ 596,243**	**$ 581,255**

* *Represents aid from sponsors for which the University acts as an agent for the recipient.*

15. SPONSORED SUPPORT

Total expenditures funded by US government sponsors or by institutions that subcontract federally sponsored projects to the University were $653.4 million and $669.6 million in fiscal 2013 and 2012, respectively. The University's principal source of federal sponsored funds is the Department of Health and Human Services. The University also has many non-federal sources of sponsored awards and grants, including corporations, foundations, state and local governments, foreign governments, and research institutes.

Sponsored grants and contracts normally provide for the recovery of direct and indirect costs. The University recognizes revenue associated with direct costs as the related costs are incurred. Recovery of related indirect costs is generally recorded at fixed or predetermined rates negotiated with the federal government and other sponsors. Predetermined federal indirect cost rates have been established for the University Area and the Medical School (including the School of Dental Medicine) through fiscal year 2015. The School of Public Health has predetermined indirect cost rates through fiscal 2013. Funds received for federally sponsored activity are subject to audit.

16. GIFTS

Gifts that are available for current purposes are classified as either "Gifts for current use" or "Non-federal sponsored grants," as appropriate. Gifts that have been restricted by the donor or designated by the Corporation for facilities, loan funds, endowment, or similar purposes are classified as "Gifts for capital." Gifts for current use, non-federal sponsored grants, and gifts for capital are classified as unrestricted, temporarily restricted, or permanently restricted net assets in accordance with donor specifications.

Gifts received for the years ended June 30, 2013 and 2012 are summarized as follows (in thousands of dollars):

	2013	2012
Gifts for current use	**$ 338,535**	$ 289,217
Non-federal sponsored grants	**111,068**	88,262
Gifts for capital:		
Endowment funds	**222,686**	226,494
Split interest agreements*	**31,817**	20,168
Loan funds and facilities	**88,217**	26,243
Total gifts for capital	**342,720**	272,905
TOTAL GIFTS	**$ 792,323**	**$ 650,384**

* *Shown at net present value. The gross value of these gifts was $60,481 and $51,045 for the years ended June 30, 2013 and 2012, respectively.*

17. OTHER INCOME

The major components of other income for the years ended June 30, 2013 and 2012 were as follows (in thousands of dollars):

	2013	2012
Rental and parking	**$ 130,605**	$ 128,610
Royalties from patents, copyrights, and trademarks	**123,086**	112,814
Publications	**79,879**	78,086
Services income	**72,793**	68,060
Health and clinic fees	**55,968**	51,689
Sales income	**45,961**	45,605
Interest income	**9,527**	11,258
Other student income	**5,995**	5,934
Other	**41,479**	36,271
TOTAL OTHER INCOME	**$ 565,293**	**$ 538,327**

18. OTHER EXPENSES

The major components of other expenses for the years ended June 30, 2013 and 2012 were as follows (in thousands of dollars):

	2013	2012
Subcontract expenses under sponsored projects	**$ 160,048**	$ 160,961
Travel	**83,616**	79,446
Publishing	**48,409**	49,579
Taxes and fees	**26,371**	29,054
Postage	**22,648**	21,181
Advertising	**21,474**	19,728
Insurance	**16,047**	12,939
Telephone	**13,300**	12,851
Other	**68,605**	36,934
TOTAL OTHER EXPENSES	**$ 460,518**	**$ 422,673**

19. FUNCTIONAL CLASSIFICATION OF OPERATING EXPENSES

Operating expenses are allocated functionally on a direct basis. Interest, depreciation, and operations and maintenance expenses are allocated based on square footage.

Operating expenses by functional classification for the years ended June 30, 2013 and 2012 were as follows (in thousands of dollars):

	2013	2012
Instruction	**$ 1,105,090**	$ 1,063,971
Research	**796,606**	769,077
Institutional support	**734,290**	657,082
Academic support	**579,739**	539,516
Auxiliary services	**486,292**	462,887
Libraries	**229,748**	237,082
Student services	**180,246**	167,611
Scholarships and other student awards	**136,360**	128,993
TOTAL EXPENSES	**$ 4,248,371**	**$ 4,026,219**

20. COMMITMENTS AND CONTINGENCIES

Lease commitments

The University is the lessee of equipment and space under operating (rental) and capital leases. Rent expense related to leases was $55.6 million and $53.2 million for the years ended June 30, 2013 and 2012, respectively.

Future minimum payments under these operating and capital leases are as follows (in thousands of dollars):

	Operating	Capital
2014	$ 49,415	$ 6,727
2015	45,217	6,998
2016	35,725	7,301
2017	31,094	7,489
2018	33,336	7,494
Thereafter	61,483	170,224
TOTAL FUTURE MINIMUM PAYMENTS	**$ 256,270**	**$ 206,233**

Fixed asset-related commitments

The University has various commitments for capital projects involving construction and renovation of certain facilities, real estate acquisitions, and equipment purchases, for which the outstanding commitments as of June 30, 2013 totaled approximately $263.8 million.

Environmental remediation

The University is subject to laws and regulations concerning environmental remediation and has established reserves for potential obligations that management considers to be probable and for which reasonable estimates can be made. These estimates may change substantially depending on new information regarding the nature and extent of contamination, appropriate remediation technologies, and regulatory approvals. Costs of future environmental remediation have been discounted to their net present value. Management is not aware of any existing conditions that it believes are likely to have a material adverse effect on the University's financial position, changes in net assets, or cash flows.

Utilities purchase commitments

The University has entered into Power Purchase Agreements (PPAs) with a series of utilities providers to purchase natural gas and electricity for various quantities and time periods. As of June 30, 2013, future obligations under the PPAs are as follows (in thousands of dollars):

2014	$ 19,826
2015	14,561
2016	5,629
2017	3,174
2018	3,131
Thereafter	23,574
TOTAL UTILITY FUTURE PURCHASE OBLIGATIONS	**$ 69,895**

General

The University is a defendant in various legal actions arising from the normal course of its operations. While it is not possible to predict accurately or determine the eventual outcome of such actions, management believes that the outcome of these proceedings will not have a material adverse effect on the University's financial position, changes in net assets, or cash flows.

The University has evaluated subsequent events through November 8, 2013, the date the financial statements were available for issuance.