

## **Section I**

# **Financial Statements**

**California Institute of Technology**  
**Balance Sheets**  
**At September 30, 2016 and 2015**  
**(Dollars in Thousands)**

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	<b>2016</b>	<b>2015</b>
<b>ASSETS</b>		
Cash and cash equivalents (Notes B and D)	\$ 6,374	\$ 5,257
Accounts and notes receivable, net		
United States government	231,915	215,801
Other	61,424	56,682
Contributions receivable, net	212,398	162,565
Investments	3,028,378	2,834,504
Prepaid expenses and other assets	175,629	107,991
Deferred United States government billings	371,378	349,940
Property, plant, and equipment, net	862,460	865,023
	<u>                    </u>	<u>                    </u>
<b>Total assets</b>	<b>\$ 4,949,956</b>	<b>\$ 4,597,763</b>
<b>LIABILITIES and NET ASSETS</b>		
<b>Liabilities:</b>		
Accounts payable and accrued expenses	\$ 318,916	\$ 296,169
Accrued compensation and benefits	209,465	190,936
Deferred revenue and refundable advances	32,955	48,695
Annuities, trust agreements, and agency funds	89,761	87,821
Bonds and notes payable, net	1,255,505	1,169,776
Accumulated postretirement benefit obligation	415,710	379,752
	<u>                    </u>	<u>                    </u>
<b>Total liabilities</b>	<b>2,322,312</b>	<b>2,173,149</b>
<b>Net assets:</b>		
Unrestricted	424,153	507,208
Temporarily restricted	766,388	688,071
Permanently restricted	1,437,103	1,229,335
	<u>                    </u>	<u>                    </u>
<b>Total net assets</b>	<b>2,627,644</b>	<b>2,424,614</b>
	<u>                    </u>	<u>                    </u>
<b>Total liabilities and net assets</b>	<b>\$ 4,949,956</b>	<b>\$ 4,597,763</b>
	<u>                    </u>	<u>                    </u>

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

**California Institute of Technology**  
**Statement of Activities**  
**For the Year Ended September 30, 2016**  
**(with summarized financial information for the year ended September 30, 2015)**  
**(Dollars in Thousands)**

	Unrestricted	Temporarily Restricted	Permanently Restricted	2016 Total	2015 Total
Operating revenues:					
Tuition and fees, net of student financial aid	\$ 40,814	\$ -	\$ -	\$ 40,814	\$ 38,065
Endowment spending, distributed	54,597	65,762	-	120,359	113,492
Gifts and pledges	48,235	101,022	-	149,257	50,204
Grants and contracts:					
Jet Propulsion Laboratory - direct	1,870,621	-	-	1,870,621	1,758,660
United States government, Campus - direct	166,131	-	-	166,131	179,867
Other Campus - direct	27,718	-	-	27,718	26,220
Recovery of indirect costs and allowances	121,198	-	-	121,198	116,488
Auxiliary enterprises	28,933	-	-	28,933	28,127
Other	36,621	-	-	36,621	39,039
Net assets released from restrictions	114,105	(114,105)	-	-	-
<b>Total operating revenues</b>	<b>2,508,973</b>	<b>52,679</b>	<b>-</b>	<b>2,561,652</b>	<b>2,350,162</b>
Operating expenses:					
Compensation and benefits	368,352	-	-	368,352	355,953
Supplies and services	120,033	-	-	120,033	128,262
Subcontracts	31,647	-	-	31,647	38,107
Graduate fellowships	19,037	-	-	19,037	18,104
Depreciation, accretion, and amortization	65,913	-	-	65,913	65,794
Utilities	16,992	-	-	16,992	16,233
Interest	20,742	-	-	20,742	19,095
Jet Propulsion Laboratory	1,870,621	-	-	1,870,621	1,758,660
<b>Total operating expenses</b>	<b>2,513,337</b>	<b>-</b>	<b>-</b>	<b>2,513,337</b>	<b>2,400,208</b>
<b>Results of operations</b>	<b>(4,364)</b>	<b>52,679</b>	<b>-</b>	<b>48,315</b>	<b>(50,046)</b>
Non-operating changes:					
Investment return in excess/(deficit) of endowment spending	45,513	25,092	572	71,177	(180,250)
Endowment spending, undistributed	2,737	6,974	652	10,363	7,740
Net assets released from restrictions	2,995	(2,995)	-	-	-
Gifts and pledges	1,606	5,830	136,169	143,605	175,521
Changes in fair value of interest rate swap	(15,112)	-	-	(15,112)	(14,743)
Non periodic changes in benefit obligations	(19,859)	-	-	(19,859)	(13,555)
Interest expense	(23,214)	-	-	(23,214)	(13,370)
Loss on retirement of debt and other	(12,264)	-	19	(12,245)	(4,065)
Resignations and reclassifications of net assets	(61,093)	(9,263)	70,356	-	-
<b>Total non-operating activities</b>	<b>(78,691)</b>	<b>25,638</b>	<b>207,768</b>	<b>154,715</b>	<b>(42,722)</b>
<b>Increase/(decrease) in net assets</b>	<b>(83,055)</b>	<b>78,317</b>	<b>207,768</b>	<b>203,030</b>	<b>(92,768)</b>
Net assets at beginning of year	507,208	688,071	1,229,335	2,424,614	2,517,382
Net assets at end of year	\$ 424,153	\$ 766,388	\$ 1,437,103	\$ 2,627,644	\$ 2,424,614

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

**California Institute of Technology**  
**Statement of Activities**  
**For the Year Ended September 30, 2015**  
**(Dollars in Thousands)**

	Unrestricted	Temporarily Restricted	Permanently Restricted	2015 Total
Operating revenues:				
Tuition and fees, net of student financial aid	\$ 38,065	\$ -	\$ -	\$ 38,065
Endowment spending, distributed	53,818	59,674	-	113,492
Gifts and pledges	21,171	29,033	-	50,204
Grants and contracts:				
Jet Propulsion Laboratory - direct	1,758,660	-	-	1,758,660
United States government, Campus - direct	179,867	-	-	179,867
Other Campus - direct	26,220	-	-	26,220
Recovery of indirect costs and allowances	116,488	-	-	116,488
Auxiliary enterprises	28,127	-	-	28,127
Other	39,039	-	-	39,039
Net assets released from restrictions	93,956	(93,956)	-	-
<b>Total operating revenues</b>	<b>2,355,411</b>	<b>(5,249)</b>	<b>-</b>	<b>2,350,162</b>
Operating expenses:				
Compensation and benefits	355,953	-	-	355,953
Supplies and services	128,262	-	-	128,262
Subcontracts	38,107	-	-	38,107
Graduate fellowships	18,104	-	-	18,104
Depreciation, accretion, and amortization	65,794	-	-	65,794
Utilities	16,233	-	-	16,233
Interest	19,095	-	-	19,095
Jet Propulsion Laboratory	1,758,660	-	-	1,758,660
<b>Total operating expenses</b>	<b>2,400,208</b>	<b>-</b>	<b>-</b>	<b>2,400,208</b>
<b>Results of operations</b>	<b>(44,797)</b>	<b>(5,249)</b>	<b>-</b>	<b>(50,046)</b>
Non-operating changes:				
Investment return in excess of endowment spending	(104,524)	(74,952)	(774)	(180,250)
Endowment spending, undistributed	3,357	3,740	643	7,740
Net assets released from restrictions	634	(634)	-	-
Gifts and pledges	1,366	14,351	159,804	175,521
Changes in fair value of interest rate swap	(14,743)	-	-	(14,743)
Non periodic changes in benefit obligations	(13,555)	-	-	(13,555)
Interest expense	(13,370)	-	-	(13,370)
Other	(4,087)	-	22	(4,065)
Resignations and reclassifications of net assets	(11,423)	(152)	11,575	-
<b>Total non-operating activities</b>	<b>(156,345)</b>	<b>(57,647)</b>	<b>171,270</b>	<b>(42,722)</b>
<b>Decrease in net assets</b>	<b>(201,142)</b>	<b>(62,896)</b>	<b>171,270</b>	<b>(92,768)</b>
Net assets at beginning of year	708,350	750,967	1,058,065	2,517,382
Net assets at end of year	<b>\$ 507,208</b>	<b>\$ 688,071</b>	<b>\$ 1,229,335</b>	<b>\$ 2,424,614</b>

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

**California Institute of Technology**  
**Statements of Cash Flows**  
**For the Years Ended September 30, 2016 and 2015**  
**(Dollars in Thousands)**

	<b>2016</b>	<b>2015</b>
<b>Cash flows from operating activities:</b>		
Increase/(decrease) in net assets	\$ 203,030	\$ (92,768)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation, accretion, and amortization	65,913	65,794
Changes in postemployment benefit obligations	19,859	13,555
Loss on retirement of debt	10,158	-
Contributions restricted for long-term investment and capital projects	(136,682)	(175,302)
Investment return restricted for long-term investment and capital projects	(996)	(1,444)
Realized and unrealized (gains)/losses on investments and swap	(147,066)	117,228
In-kind receipts of property, plant, and equipment	(603)	(720)
In-kind receipts of investments	(3,666)	-
Changes in annuity and trust liabilities	(3,075)	4,623
Losses on disposals of property, plant, and equipment	305	1,035
Changes in assets and liabilities:		
Accounts and notes receivable, net	(12,843)	(8,544)
Contributions receivable, net	(65,578)	2,969
Prepaid expenses and other assets	(6,244)	(4,988)
Deferred United States government billings	(21,438)	(3,780)
Accounts payable and accrued expenses	10,102	14,632
Accrued compensation and benefits	18,529	6,172
Deferred revenue and refundable advances	(15,740)	4,146
Agency funds	313	57
Accumulated postretirement benefit obligation	16,099	(3,047)
<b>Net cash used in operating activities</b>	<b>(69,623)</b>	<b>(60,382)</b>
<b>Cash flows from investing activities:</b>		
Purchases of investments	(831,184)	(1,334,566)
Proceeds from sales and maturities of investments	795,977	869,786
Purchases of property, plant, and equipment	(61,622)	(69,015)
Proceeds from sale of property, plant, and equipment	1,798	3,051
<b>Net cash used in investing activities</b>	<b>(95,031)</b>	<b>(530,744)</b>
<b>Cash flows from financing activities:</b>		
Contributions restricted for long-term investment and capital projects	91,145	93,699
Investment return restricted for long-term investment and capital projects	996	1,444
Cash received under annuity and trust agreements	5,474	5,515
Cash payments made under annuity and trust agreements	(7,232)	(7,189)
Net borrowings of short-term debt	17,170	94,572
Bond issuance costs	(1,849)	(1,750)
Proceeds from issuance of long-term debt	150,000	400,000
Cash paid for retirement of long-term debt	(89,933)	-
<b>Net cash provided by financing activities</b>	<b>165,771</b>	<b>586,291</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>1,117</b>	<b>(4,835)</b>
Cash and cash equivalents at beginning of year	5,257	10,092
<b>Cash and cash equivalents at end of year</b>	<b>\$ 6,374</b>	<b>\$ 5,257</b>

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

**A. Description of California Institute of Technology**

California Institute of Technology (the “Institute”) is a private, not-for-profit institution of higher education based in Pasadena, California. Founded in 1891, the Institute provides education and training services, primarily for students at the undergraduate, graduate, and postdoctoral levels, and performs research, training, and other services under grants, contracts, and similar agreements with sponsoring organizations, primarily departments and agencies of the government of the United States of America.

**B. Summary of Significant Accounting Policies**

**Basis of Presentation**

The accompanying financial statements include the accounts of the Institute’s main campus and satellite facilities (“Campus”), as well as the Jet Propulsion Laboratory (“JPL”), a Federally Funded Research and Development Center managed by the Institute for the National Aeronautics and Space Administration (“NASA”).

The Institute manages JPL under a cost-reimbursable contract with NASA. JPL’s land, buildings, and equipment are owned by the United States government and are excluded from the Institute’s financial statements. Receivables and liabilities arising from JPL’s activities are reflected in the Institute’s balance sheets. The direct costs of JPL’s activities and the related reimbursement of those costs are reflected separately in the statements of activities. The management allowances earned under the NASA contract were \$21,000 for each of the years ended September 30, 2016 and 2015 and are included in recovery of indirect costs and allowances in the statements of activities.

The Institute’s financial statements have been prepared on the accrual basis of accounting, in accordance with accounting principles generally accepted in the United States of America.

**Net Assets**

Net assets are classified into three categories according to donor-imposed restrictions or certain provisions of law or accounting standards: permanently restricted, temporarily restricted, and unrestricted.

- Permanently restricted net assets include endowment gifts as well as certain charitable remainder trusts, pooled income funds, gift annuities, other split-interest agreements, and contributions receivable in which donors have stipulated that the original value of their contributions and, if applicable, any subsequent accumulations, be held in perpetuity.
- Temporarily restricted net assets include investment return from permanent endowments that has not been appropriated for expenditures and gifts and related contributions receivable for which donor-imposed restrictions have not been met, including funds restricted for future capital projects, certain charitable remainder trusts, pooled income funds, gift annuities, and other split-interest agreements. These restrictions are expected to be removed through the passage of time, the appropriation of endowment earnings by the Institute, and/or the Institute’s incurrence of expenditures or other payments that meet donors’ restrictions. Expirations of temporary restrictions on net assets are reported as releases from temporarily restricted to unrestricted net assets in the statements of activities. Donor-restricted gifts that

are received and either spent or deemed spent within the same fiscal year are reported as unrestricted revenues.

- Unrestricted net assets are those not subject to donor-imposed restrictions or requirements for classification imposed by law or accounting standards.

#### **Use of Estimates**

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

#### **Reclassifications**

Certain prior year amounts at September 30, 2015 have been reclassified to conform to the current year presentation.

#### **Redesignations**

Net assets related to certain contributions received in prior periods have been transferred among net asset categories due to changes in donor designations. Redesignations during the year ended September 30, 2016 also include \$69,093 transferred from unrestricted net assets to permanently restricted net assets due to endowment funding agreements with donors.

#### **Cash and Cash Equivalents**

Cash and cash equivalents include bank account balances, investments in money market funds, and direct short-term investments that have remaining maturities of three months or less when purchased. Bank account balances at September 30, 2016 and 2015 were \$6,374 and \$5,257, respectively. The Institute classifies all cash and cash equivalents held as part of the investment portfolios as short-term investments. At September 30, 2016 and 2015, short-term investments, as disclosed in Note D, included \$146,080 and \$177,206, respectively, in cash and cash equivalents. Carrying amounts of cash and cash equivalents approximate fair value due to the relatively short maturities of these instruments.

Under the Institute's cash management system, checks issued by the Institute but not yet cashed by recipients may result in overdraft balances for accounting purposes and are included in accounts payable and accrued expenses in the balance sheets if an overdraft situation exists. There were no overdrafts at September 30, 2016 and 2015.

#### **Accounts and Notes Receivable**

Accounts receivable under contracts and grants are carried at cost, less an immaterial allowance for doubtful accounts. Accounts receivable under contracts and grants totaled \$237,643 and \$222,940 at September 30, 2016 and 2015, respectively. Activity in the allowance accounts was not significant during the years ended September 30, 2016 and 2015. The carrying value of net accounts receivable approximates fair value.

**California Institute of Technology**  
**Notes to Financial Statements**  
**September 30, 2016 and 2015**  
**(Dollars in Thousands)**

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Accounts receivable from students and employees of \$2,136 and \$2,482 at September 30, 2016 and 2015, respectively, are carried at cost and approximate fair value. Doubtful accounts are charged to expense when they are deemed to become uncollectible. During the years ended September 30, 2016 and 2015, only minor amounts were written off as uncollectible.

The Institute provides loans to students from both internal funds and from funds provided by the United States government under the Federal Perkins Loan Program. Substantially all student loans that bear interest carry fixed rates, and substantially all student loans carry ten-year terms. Student loans receivable of \$6,322 and \$6,703 at September 30, 2016 and 2015, respectively, are carried at cost.

The Institute holds all loans to maturity. Loans to students are considered delinquent 10-90 days after a borrower misses a required payment. Delinquent interest-bearing loans continue to accrue interest. At September 30, 2016 and 2015, there were no significant delinquencies on outstanding loans. No allowances have been recorded, and only minor amounts of loans are expected to become uncollectible. The principal credit quality indicator for such loans is collection experience. The Institute manages its credit risk by limiting amounts loaned per term, monitoring aggregate loan levels, and maintaining an active collections process with the assistance of third-party collection agencies as necessary. Student loans generally are not dischargeable in bankruptcy. Loans are not considered uncollectible until all reasonable collection efforts have been made.

**Investments**

Investments are carried at fair value as discussed in Note K. Purchases and sales of securities are recorded on trade dates, and realized gains and losses are determined based on the average cost of securities sold. Accounts receivable included \$46,205 and \$38,192 related to outstanding sales and accounts payable included \$1,512 and \$7,024 related to outstanding purchases of investments at September 30, 2016 and 2015, respectively.

Short-term investments included \$51,811 and \$36,314 held by the counterparty to the Institute's interest rate swap as collateral, in accordance with the terms of the swap agreement at September 30, 2016 and 2015, respectively.

**Derivatives**

The Institute uses an interest rate swap to manage the interest rate exposure of a portion of its variable rate debt. The swap is recorded at fair value, which is the estimated amount that the Institute would receive or pay to terminate the agreement, taking into account current interest rates and the current credit-worthiness of the swap counterparty. Costs of regular settlements with the counterparty of \$5,399 and \$5,658 during the years ended September 30, 2016 and 2015, respectively, are included in interest expense in the statements of activities. Changes in the swap's fair value during the years ended September 30, 2016 and 2015, resulted in unrealized losses of \$15,112 and \$14,743, respectively, which are included in non-operating changes in net assets in the statements of activities. The fair value of the swap was a liability of \$70,521 and \$55,409 at September 30, 2016 and 2015, respectively, and is included in accounts payable and accrued expenses in the balance sheets.

The Institute also directly transacts in options to manage equity risks of certain investments. The fair value of options is included in investments in the balance sheets and is classified as derivatives in disclosures of investments. Changes in the fair value of options are reported in investment return



(loss). The Institute does not designate any derivative instruments as hedging instruments under Generally Accepted Accounting Principles. Further disclosure of the fair value of derivatives is reported in Note K.

### **Property, Plant, and Equipment**

Property, plant, and equipment is recorded at the cost of construction, acquisition, or the fair value of contributed assets at the date of gift. Interest costs related to debt used for construction of assets are capitalized and included in the cost of construction. Depreciation on all assets subject to depreciation is calculated over the estimated useful lives as defined for each class of depreciable asset, which range from three to fifty years, using the straight-line method. Depreciation on buildings and building improvements is calculated based on the useful lives of each major building component. The Institute provides for the renewal and replacement of assets from various sources set aside for this purpose.

The Institute routinely acquires or constructs equipment under federally and non-federally funded research awards. The costs of such assets for which title does not ultimately transfer to the Institute are charged to expense.

The Institute's conditional asset retirement obligations are primarily related to future asbestos removal and disposal. Asset retirement cost, net of accumulated depreciation, at September 30, 2016 and 2015 was \$349 and \$1,015, respectively, and is included in property, plant, and equipment in the balance sheets. Conditional asset retirement obligations at September 30, 2016 and 2015 were \$13,683 and \$13,918, respectively, and are included in accounts payable and accrued expenses in the balance sheets.

### **Annuity and Trust Agreements**

The Institute's split-interest agreements with donors consist primarily of charitable gift annuities and charitable remainder trusts for which the Institute serves as trustee. For irrevocable agreements, assets contributed are included in investments at fair value. Contribution revenue is recognized at the date each trust is established after recording liabilities for the actuarially-determined present value of the estimated future payments to be made to beneficiaries. Actuarial liabilities are discounted at an appropriate credit risk-adjusted rate determined at the inception of each agreement. Discount rates on split-interest agreements range from 1.20% to 11.20% per annum. The liabilities are adjusted during the terms of the agreements for changes in the fair value of the assets, accretion of discounts, and other changes in the estimates of future benefits. The 2012 Individual Annuity Reserving (IAR) table was used for the years ended September 30, 2016 and 2015. Split-interest agreement liabilities totaled \$68,537 and \$67,478 at September 30, 2016 and 2015, respectively, and are included in liabilities for annuities, trust agreements and agency funds in the balance sheets and classified in Level 3 of the valuation hierarchy described in Note K.

The Institute is also the trustee for certain revocable agreements. Assets contributed are included in Institute investments at fair value, and amounts equal to the value of assets are included in liabilities for annuities, trust agreements, and agency funds in the balance sheets. Total assets and liabilities for revocable agreements were \$8,045 and \$7,562 at September 30, 2016 and 2015, respectively.

### **Beneficial Interests**

The Institute is the beneficiary of both charitable remainder and perpetual trusts held and administered by others and interests in certain estates bequeathed by donors. The fair value of the Institute's interests in charitable and perpetual trusts is estimated by multiplying the Institute's percentage interest by the fair value of trust assets at the time that receipt of such interests is both probable and reasonably estimable. The value of the Institute's interests in such trusts is adjusted for changes in the fair values of the underlying assets. Distributions from perpetual trusts are recorded as revenue when contributed by the trustee. Interests in estates are recognized based on estimates of cash flows from estate settlements at the time such cash flows are probable and reasonably estimable. Beneficial interests totaled \$73,341 and \$22,379 at September 30, 2016 and 2015, respectively, and are included in prepaid expenses and other assets in the balance sheets.

### **Retirement Plans**

The Institute provides a defined contribution retirement program for eligible academic and administrative employees. Contributions to Internal Revenue Code "IRC" Section 403(b) defined contribution plans for the years ended September 30, 2016 and 2015 were \$24,614 and \$24,151, respectively, for the Campus and \$75,918 and \$73,934, respectively, for JPL. The Institute has no assets or liabilities related to these plans.

At September 30, 2016 and 2015, respectively, prepaid expenses and other assets included \$77,462 and \$69,731 in assets held pursuant to IRC section 457 defined contribution retirement plans. These assets are invested with external investment managers and are included in investments in the balance sheets at fair value. The Institute's liabilities related to these funds were \$77,277 and \$69,562 at September 30, 2016 and 2015, respectively, and are included in accrued compensation and benefits in the balance sheets.

### **Funds Held for Others**

The Institute held assets totaling \$13,179 and \$12,781 in agency funds at September 30, 2016 and 2015, respectively. The assets held are primarily included in investments in the balance sheets. The corresponding liability, which is equal to assets held, is included in annuities, trust agreements, and agency funds in the balance sheets.

### **Compensated Absences**

Institute employees are entitled to paid vacation based upon length of service and other factors. Certain employees also accrue benefits related to sick leave. The Institute records a liability for these benefits that employees have earned but not yet taken. At September 30, 2016 and 2015, accrued compensated absences of \$83,219 and \$79,240, respectively, are included in accrued compensation and benefits in the balance sheets. Other compensated absences do not accumulate and are treated as current period costs.

### **Workers' Compensation Insurance**

The Institute provides workers' compensation insurance to its employees. Liabilities for the Institute's retained risk related to such coverage are determined by an actuary and are included in accrued compensation and benefits in the balance sheets. At September 30, 2016 and 2015, the liabilities for workers' compensation were \$9,657 and \$9,845, respectively.

### **Revenue Recognition**

The Institute's revenue recognition policies are as follows:

- *Tuition and fees* - Student tuition and fees are recorded as revenues during the year the related academic services are rendered and are displayed net of financial aid on the statements of activities. Tuition and fees totaled \$98,835 and \$93,319 for the years ended September 30, 2016 and 2015, respectively. Student financial aid totaled \$58,021 and \$55,254 for the years ended September 30, 2016 and 2015, respectively. Student tuition and fees received in advance of services to be rendered, net of applicable financial aid, are recorded as deferred revenue.
- *Investment return (loss)* - Investment transactions are recorded on the trade date. Investment income and realized and unrealized gains and losses, net of investment management fees, are reported as increases or decreases to the appropriate net asset category.
- *Gifts* - Unconditional promises to give are recorded as revenues in the year received. Non-cash gifts are recorded at fair value using quoted market prices, market prices for similar assets, independent appraisals, or as estimated by Institute management. Gift revenue from contributions to be collected in the form of securities or other investments is adjusted at each year end to reflect the year-end value of securities and/or investments to be contributed.

Donor-restricted gifts, which are received and either spent, or deemed spent, within the same year are reported as unrestricted revenue. Gifts of long-lived assets with no donor-imposed time restrictions are reported as unrestricted revenue in the year received. Gifts restricted to the acquisition or construction of long-lived assets are reported as temporarily restricted revenue and released to unrestricted net assets when such assets are placed in service. Gifts that are subject to time or other purpose restrictions are reported as temporarily restricted revenue and released to unrestricted net assets when such restrictions are met. Gifts received for endowment investment are held in perpetuity and recorded as permanently restricted revenue.

Conditional promises to give are not recorded until donor-imposed conditions have been substantially met. Conditional promises to give totaled \$69,214 and \$113,922 at September 30, 2016 and 2015, respectively. Payments received related to conditional promises totaled \$2,538 and \$19,602 at September 30, 2016 and 2015, respectively, and are included in deferred revenue and refundable advances in the balance sheets.

- *Grants and contracts* - Revenues from grants and contracts generally are recognized in unrestricted net assets as allowable expenditures are incurred under such agreements. Substantially all United States government grants and contracts awarded to the Campus provide for the reimbursement of indirect facilities and administrative costs based on rates negotiated with the Office of Naval Research, the Campus' federal cognizant agency for the negotiation and approval of facilities and administrative and other indirect cost rates. Costs related to the performance of activities under the JPL contract are reimbursable by NASA. Amounts received in excess of expenditures are recorded as deferred revenue. At September 30, 2016 and 2015, deferred revenue related to grants and contracts was \$10,098 and \$10,119, respectively.

**California Institute of Technology**  
**Notes to Financial Statements**  
**September 30, 2016 and 2015**  
**(Dollars in Thousands)**

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- *Auxiliary enterprises* - Revenues from supporting services, such as dining facilities, faculty and student housing, and retail stores are recorded at the time of delivery of products or services. Amounts received in advance of deliveries of products or services are recorded as deferred revenue.

**Expenses**

Expenses are generally reported as decreases in unrestricted net assets. Campus expenses are reported in the statements of activities by natural classification. Campus expenses by functional classification were as follows for the years ended September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Instruction and academic support	\$ 289,421	\$ 274,934
Organized research	237,005	252,677
Institutional	82,168	81,225
Auxiliary enterprises	34,122	32,712
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<b>Total Campus functional expenses</b>	<b>\$ 642,716</b>	<b>\$ 641,548</b>
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Building and improvements depreciation and plant operation expenses are allocated to functional classifications based on square footage occupancy of Institute facilities. Equipment depreciation is allocated to functional classifications based on average equipment purchases attributed to each classification. Interest expense on external debt, net of amounts capitalized, is allocated to the functional categories that have benefited from the proceeds of such debt.

**Operating and Non-operating Activities**

The statements of activities report the changes in net assets from the Institute's operating and non-operating activities. Operating activities exclude investment returns/losses in excess/deficit of endowment spending, endowment spending available but not distributed to operations, revenues and releases from restrictions related to gifts for construction, endowments, and annuity and trust agreements, changes in postemployment benefit obligations that are not otherwise recognized in net periodic benefit cost, changes in fair value of interest rate swaps, interest expense related to any bonds issued for which the proceeds have not yet been used for capital projects or to refund other bonds, gains or losses on disposal of plant, property and equipment, net gains or losses on nonrecurring transactions, actuarial adjustments related to annuity and trust agreements, losses on retirement of indebtedness, and donor redesignations or other reclassifications of net assets.

**Tax Status**

The Institute is generally exempt from federal taxes on income related to its charitable purpose under the provisions of IRC Section 501(c)(3) and from California and other state income taxes under corresponding state laws. The Institute is subject to both federal and state income taxes on income from certain activities not substantially related to its exempt purpose. At September 30, 2016 and 2015, the Institute maintained a full valuation allowance on its deferred tax assets, which are primarily due to tax losses from certain investment activities. Due to uncertainties surrounding both the timing and amounts of potential future net taxable income, the Institute has concluded that it is

more likely than not that the Institute will not realize the deferred tax assets. The Institute has not provided for any uncertain tax positions at September 30, 2016 and 2015.

#### **Related Party Transactions**

Members of the Institute's Board of Trustees and senior management may, from time to time, be associated, either directly or indirectly, with entities doing business with the Institute. These transactions are conducted in the normal course of business at an arm's length, and in accordance with the Institute's policies and procedures governing potential conflicts of interest.

#### **Accounting Pronouncements Adopted**

In April 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-03 to simplify the presentation of debt issuance costs. The financial statements for the years ended September 30, 2016 and 2015 reflect the implementation of the ASU. Adoption of the ASU resulted in a reclassification of \$7,166 from prepaid expenses and other assets to bonds and notes payable, net at September 30, 2015.

In May 2015, FASB issued ASU 2015-07. The ASU excludes financial instruments measured at net asset value as a practical expedient from the fair value hierarchy. The Institute adopted the provisions of ASU 2015-7 during the year ended September 30, 2016. The effects of adopting this new standard are reflected in Note K and the prior-year presentation has been adjusted to conform to the current year presentation.

In June 2015, FASB issued ASU 2015-10. The ASU amends the definition of readily-determinable fair value (RDFV). The change in the definition of RDFV under this new standard was considered in connection with the Institute's election to early-adopt ASU 2015-7 during the fiscal year ended September 30, 2016.

In January 2016, FASB issued ASU 2016-01 regarding certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. ASU 2016-01 is effective for the Institute's fiscal year ending September 30, 2020. The Institute early-adopted the provisions of ASU 2016-01 permitting the elimination of fair value disclosures for financial instruments measured at cost or amortized cost for fiscal 2016.

#### **New Accounting Pronouncements**

In May 2014, FASB issued ASU 2014-09 regarding the recognition of revenue from contracts with customers. ASU 2014-09 is effective for the Institute's fiscal year ending September 30, 2019. The Institute is evaluating the impact this standard may have on its financial statements and disclosures.

In February 2016, FASB issued ASU 2016-02 regarding accounting for leases. ASU 2016-12 is effective for the Institute's fiscal year ending September 30, 2020. The Institute is evaluating the impact this standard may have on its financial statements and disclosures.

In August 2016, FASB issued ASU 2016-14 regarding presentation of financial statements of not-for-profit organizations. ASU 2016-14 is effective for the Institute's fiscal year ending September 30, 2019. The Institute is evaluating the impact this standard may have on its financial statements and disclosures.

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**C. Contributions Receivable, net**

Contributions receivable consist of unconditional promises to give to the Institute in the future. Contributions receivable are initially recorded at fair value, including a discount to the present value of the future cash flows at an appropriate credit risk-adjusted rate, and are classified in Level 3 of the valuation hierarchy described in Note K. Discount rates on outstanding contributions at September 30, 2016 and 2015 range from 0.74% to 4.56%.

Contributions receivable are expected to be collected as follows at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Within one year	\$ 50,730	\$ 58,247
Between one year and five years	125,726	89,597
More than five years	<u>46,540</u>	<u>21,045</u>
Gross contributions receivable	222,996	168,889
Less:		
Unamortized discounts	10,314	6,133
Allowance for uncollectible contributions	<u>284</u>	<u>191</u>
Net contributions receivable	<u>\$ 212,398</u>	<u>\$ 162,565</u>

Net contributions receivable carried the following restrictions at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Endowment	\$ 128,806	\$ 135,405
Building construction	-	388
Other purpose and/or time restrictions	<u>83,592</u>	<u>26,772</u>
Net contributions receivable	<u>\$ 212,398</u>	<u>\$ 162,565</u>

At September 30, 2016 and 2015, net contributions receivable of \$183,631 and \$139,034, respectively, were due from board members, their estates, and charitable entities founded by board members.

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**D. Investments**

Investments consisted of the following at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Short-term investments	\$ 178,866	\$ 210,636
Fixed-income securities	223,353	192,666
Equity securities	1,146,711	1,027,796
Alternative investments:		
Alternative securities	798,994	776,106
Private equity	282,099	224,986
Real assets	400,649	397,447
Derivatives, net	(2,294)	4,867
	<hr/>	<hr/>
<b>Total investments</b>	<b>\$ 3,028,378</b>	<b>\$ 2,834,504</b>
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The Institute engages a number of outside investment managers to manage portions of its investment portfolios, which include an investment pool and other separately managed portfolios.

Below is a description of the holdings included within each investment classification:

- *Short-term investments* consist primarily of cash and cash equivalents invested in U.S. government and government agency money-market funds, as well as deposits with financial institutions.
- *Fixed-income securities* consist primarily of debt instruments issued by corporate or sovereign entities in both U.S. and foreign markets and investments in funds that hold such instruments.
- *Equity securities* consist primarily of investments in publicly traded corporate equities in globally diversified public markets including domestic, developed international, emerging markets and investments in funds that hold such investments. Investment managers invest according to each manager's particular investment strategy.
- *Alternative securities* consist primarily of investments in funds in which redemption options and/or distributions are determined by the respective investment managers. Alternative securities managers pursue returns through a variety of strategies such as high yield and distressed credit, long/short equity, event-driven, and relative value. Managers invest and trade in various securities and financial instruments, including publicly traded and privately issued common and preferred shares of domestic and foreign companies, corporate debt, bonds, swaps, options, futures contracts and commodities.
- *Private equity* consists of investments in limited partnership interests that invest primarily in the securities of privately held companies. Investment managers utilize leveraged buyout and

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venture capital strategies in a wide variety of industries and company sizes. Distributions from these investments are made either in-kind as distributions of publicly tradeable equity securities after initial public offerings, or in cash after liquidation of the underlying securities by the investment manager.

- *Real assets* consist primarily of investments in limited partnerships that invest in foreign and/or domestic real estate and/or energy sectors and/or domestic timber industries. Real estate consists primarily of illiquid investments in residential and commercial real estate assets, projects or land, and notes receivable secured by real estate. Such holdings are either held directly or in partnership funds. Energy holdings consist primarily of illiquid investments in oil and gas exploration and production or materials mining businesses, as well as related oil and gas services businesses, held in limited partnerships. Timber holdings consist primarily of illiquid investments in timber land and harvesting businesses held in limited partnerships.
- *Derivatives, net* consist of options in which the Institute directly transacts to manage equity risks of certain investments and interest and currency futures of minor value.

Investments were held as follows at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Investment pool	\$ 2,193,480	\$ 2,053,675
Separately invested endowments	34,928	35,643
Trusts, annuities, and other	799,970	745,186
	<u>                    </u>	<u>                    </u>
<b>Total investments</b>	<b>\$ 3,028,378</b>	<b>\$ 2,834,504</b>

At September 30, 2016 and 2015, endowment investments were \$2,217,372 and \$2,078,954, respectively. At September 30, 2016, and 2015, other investments included \$48,259 and \$32,476, respectively, held in separately invested accounts as required by donors and/or sponsors.

Investment return consisted of the following for the years ended September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Interest and dividend income	\$ 34,322	\$ 37,809
Net realized gains	107,437	86,041
Net unrealized appreciation/(depreciation)	60,140	(182,868)
	<u>                    </u>	<u>                    </u>
<b>Total investment return/(loss)</b>	<b>\$ 201,899</b>	<b>\$ (59,018)</b>



**E. Deferred United States Government Billings**

The Institute's contract with NASA provides for the reimbursement of certain employee benefit costs incurred but not yet billed to the JPL contract. Therefore, the Institute has recorded deferred United States government billings related to the unfunded postretirement benefit obligation, accrued vacation, and workers' compensation liabilities attributable to JPL, as the Institute is able to recover these amounts through future charges to JPL contracts. Although these deferred billing amounts may not be currently funded, and therefore may need to be funded as part of future NASA budgets, the Institute has the contractual right to require that such funding be made available at the time these employee benefit liabilities become payable by the Institute.

Deferred United States government billings related to deferred reimbursements of the following liabilities at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Unfunded postretirement benefit obligation	\$ 300,376	\$ 282,313
Accrued vacation	67,046	63,138
Accrued worker's compensation expense	3,956	4,489
	<hr/>	<hr/>
<b>Total deferred United States government billings</b>	<b>\$ 371,378</b>	<b>\$ 349,940</b>
	<hr/>	<hr/>

**F. Property, Plant, and Equipment, net**

Property, plant, and equipment consisted of the following at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Land and land improvements	\$ 67,799	\$ 67,703
Buildings and building improvements	1,064,918	1,031,295
Equipment	577,899	564,443
Construction in progress	70,462	65,845
Less: accumulated depreciation	(918,618)	(864,263)
	<hr/>	<hr/>
<b>Total property, plant, and equipment, net</b>	<b>\$ 862,460</b>	<b>\$ 865,023</b>
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Depreciation expense for the years ended September 30, 2016 and 2015 was \$65,048 and \$64,998, respectively.

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**G. Bonds and Notes Payable**

Bonds and notes payable are uncollateralized, general obligations of the Institute and consisted of the following at September 30, 2016 and 2015:

	Maturity	Interest rate		Outstanding	
		2016/2015	2016	2015	
Bonds payable:					
Taxable bonds:					
Series 2016	2116	4.28%	\$ 150,000	\$ -	
Series 2015	2045	4.32%	400,000	400,000	
Series 2011	2111	4.70%	350,000	350,000	
California Educational Facilities Authority (CEFA) tax-exempt revenue bonds:					
2009 Series	2039	- / 5.00%	-	80,000	
2006 Series A, with variable rates	2036	0.89% / 0.01%	82,500	82,500	
2006 Series B, with variable rates	2036	0.85% / 0.01%	82,500	82,500	
Series 1994, with variable rates	2024	0.84% / 0.01%	30,000	30,000	
Total bonds payable, gross			1,095,000	1,025,000	
Unamortized original issue premiums/discounts and issuance costs, net			(11,128)	(9,688)	
Total bonds payable, net			1,083,872	1,015,312	
Notes payable:		<b>Maximum</b>			
Variable rate facilities:					
General working capital and capital projects:					
Bank of America revolving bank credit facility	\$ 100,000	2017	0.80% / 0.57%	70,000	31,790
Bank of America revolving bank credit facility	50,000	2017	- / 0.40%	-	25,000
Bank of New York Mellon money market loan program	50,000	None	-	-	-
JPMorgan Chase revolving bank credit facility	50,000	2017	0.68% / -	1,633	-
U.S. Bank revolving bank credit facility	50,000	2017	0.84% / 0.37%	50,000	47,674
Wells Fargo revolving bank credit facility	50,000	2018	0.87% / 0.54%	50,000	50,000
Supplemental liquidity for variable rate debt:					
Northern Trust revolving bank credit facility	100,000	2018	-	-	-
Wells Fargo revolving bank credit facility	50,000	2018	-	-	-
Total notes payable			171,633	154,464	
<b>Total bonds and notes payable, net</b>			<b>\$1,255,505</b>	<b>\$1,169,776</b>	

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As of September 30, 2016, the Institute had eight unsecured revolving lines of credit available (collectively, the “Lines of Credit”), consisting of seven unsecured revolving bank credit facilities and one unsecured revolving money market loan program. The Institute currently has internally- mandated aggregate borrowing limits under the Lines of Credit as follows: \$100,000 for borrowings to finance working capital, \$50,000 for borrowings to finance acquisitions of real estate and temporary funding for capital projects, and \$200,000 for borrowings secured to preserve liquidity.

The lines of credit from Bank of New York Mellon and JPMorgan Chase, and the Bank of America line of credit with a permitted maximum of \$50,000, are all uncommitted. Maturity dates for individual advances made under these lines of credit are determined at the time advances are made.

The Institute is required to comply with financial covenants in certain line of credit agreements, including maintaining minimum ratios of unrestricted cash and investments to total adjusted debt outstanding. As of September 30, 2016, the Institute was in compliance with all of its required financial covenants.

Under certain circumstances, the CEFA Series 1994, 2006 Series A, and 2006 Series B variable rate revenue bonds, which have contractual maturities commencing in 2024, could fail to be remarketed, requiring the Institute to repurchase the outstanding bonds totaling approximately \$195,000. Therefore, those bonds have been classified as repayable in the year ending September 30, 2017 in the following table.

Future principal repayments on bonds and notes payable were as follows at September 30, 2016:

<b>Year Ending September 30</b>	<b>Amount</b>
2017	\$ 366,633
2018	-
2019	-
2020	-
2021	-
Thereafter	900,000
<b>Total</b>	<u>\$ 1,266,633</u>

As disclosed in Note B, the Institute uses an interest rate swap to manage the interest rate exposure of the 2006 Series A and B variable rate revenue bonds. Under the terms of the agreement, which expires October 1, 2036, the Institute pays the counterparty a fixed interest rate of 3.549% and receives a variable rate, indexed at 67% of one-month LIBOR (0.36% at September 30, 2016), on a \$165,000 underlying notional principal amount.

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In September 2016, the Institute issued \$150,000 in Series 2016 taxable bonds. At the issuance date, the Institute deposited \$91,600 of the proceeds in an escrow fund to purchase noncallable notes, bills, and bonds issued by the U.S. Department of the Treasury to be held in trust to provide for interest and principal payments to the holders of the Institute's \$80,000 in CEFA 2009 Series tax-exempt revenue bonds ("2009 Bonds") until the 2009 Bonds' planned redemption in 2019. This advance refunding legally defeased the 2009 Bonds and resulted in a loss on retirement of debt of \$10,158, which is reflected in non-operating changes in unrestricted net assets in the statement of activities.

During the year ended September 30, 2015, the Institute issued \$400,000 in Series 2015 taxable bonds.

**H. Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets were available for the following purposes at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Educational and research funds	\$ 137,843	\$ 127,903
Contributions receivable	83,592	27,402
Capital projects	962	577
Life income and annuity funds	30,364	30,803
Endowments	513,627	501,386
<b>Total temporarily restricted net assets</b>	<u>\$ 766,388</u>	<u>\$ 688,071</u>

Permanently restricted net assets were available for the following purposes at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Student loan funds	\$ 18,317	\$ 17,820
Contributions receivable	128,806	135,163
Life income and annuity funds	87,249	34,595
Endowments	1,202,731	1,041,757
<b>Total permanently restricted net assets</b>	<u>\$ 1,437,103</u>	<u>\$ 1,229,335</u>

## **I. Endowment**

Endowment net assets are comprised of donor-restricted and board-designated funds held for long-term investment that support educational, research, and general operating activities of the Institute. All endowment assets are held in the investment pool unless special considerations or donor stipulations require that they be invested separately. Gift annuities, beneficial interests, contributions receivable, and unexpended endowment distributions that are subject to remaining purpose restrictions are not considered endowment net assets.

Pursuant to its interpretation of the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”) as enacted in California, the Institute classifies the following as permanently restricted net assets: the original value of initial gifts to permanent endowments, the original value of subsequent gifts to permanent endowments, and the value of accumulations to permanent endowments made in accordance with the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portions of donor-restricted endowment funds that are not classified as permanently restricted net assets are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Institute in a manner consistent with the standard of prudence prescribed by UPMIFA and Institute policies and expended accordingly.

The Institute’s endowment spending policy includes a Board of Trustees-approved endowment spending formula which takes into consideration the prior year’s spending, inflation factors, and endowment growth. In addition, in accordance with UPMIFA, when determining the annual amount to be made available for distribution to the operating budget each year, the Board of Trustees also considers the following factors:

- The purpose of each donor-restricted endowment fund
- The duration and preservation of each fund
- General economic conditions
- The possible effects of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Institute
- The investment policies of the Institute

Any excess of endowment spending over current-year investment income and gains (losses) is funded by prior years’ accumulated investment return. The Institute appropriates endowment funds for expenditure based on current spending rates and, if applicable, the incurrence of specific expenditures in accordance with donors’ purpose restrictions.

The Institute invests endowment assets targeted to earn an average annual total return that exceeds inflation by at least the amount required to support the endowment spending. Total return includes both capital appreciation/depreciation (realized and unrealized gains/losses) and investment income (including interest, dividends, and royalties). The Institute targets a diversified asset allocation, including investments in both public markets and in alternative investments, within risk constraints deemed to be prudent.

The portion of endowment available for spending that is transferred to operating accounts each year is shown as endowment spending distributed in the statements of activities. Any endowment spending

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available for expenditure but not distributed remains invested in the Institute's endowment and is included in non-operating changes to net assets in the statements of activities.

Endowment net assets consisted of the following at September 30, 2016 and 2015:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>
<b>September 30, 2016</b>		
Donor-restricted endowment funds	\$ (41,121)	\$ 507,063
Board-designated endowment funds	576,183	6,564
<b>Total endowment net assets</b>	<u>\$ 535,062</u>	<u>\$ 513,627</u>
<b>September 30, 2015</b>		
Donor-restricted endowment funds	\$ (51,061)	\$ 495,392
Board-designated endowment funds	622,527	5,994
<b>Total endowment net assets</b>	<u>\$ 571,466</u>	<u>\$ 501,386</u>

Changes in endowment net assets for the years ended September 30, 2016 and 2015 were as follows:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
<b>October 1, 2014</b>	\$ 612,315	\$ 564,603	\$ 938,812	\$ 2,115,730
Investment return:				
Investment income	16,941	16,034	157	33,132
Net depreciation in market value	(36,836)	(34,864)	(341)	(72,041)
Total investment return	(19,895)	(18,830)	(184)	(38,909)
Contributions and pledge payments	-	10,825	91,272	102,097
Additions to board-designated endowments	47,095	5,991	-	53,086
Available for expenditure	(57,174)	(63,415)	(643)	(121,232)
Redesignations, reclassifications and other	(10,875)	2,212	12,500	3,837
<b>September 30, 2015</b>	<u>571,466</u>	<u>501,386</u>	<u>1,041,757</u>	<u>2,114,609</u>
Investment return:				
Investment income	9,544	12,925	110	22,579
Net appreciation in market value	58,380	79,179	673	138,232
Total investment return	67,924	92,104	783	160,811
Contributions and pledge payments	-	734	91,372	92,106
Additions to board-designated endowments	24,985	-	-	24,985
Available for expenditure	(57,334)	(72,736)	(652)	(130,722)
Redesignations, reclassifications and other	(71,979)	(7,861)	69,471	(10,369)
<b>September 30, 2016</b>	<u>\$ 535,062</u>	<u>\$ 513,627</u>	<u>\$ 1,202,731</u>	<u>\$ 2,251,420</u>

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Under Accounting Standards Codification 958, for accounting purposes the Institute must maintain the historical values of donor-restricted endowment funds as permanently restricted net assets even in cases where the fair values of those funds are less than historical values. Such deficits are recorded as reductions of unrestricted net assets. The aggregate deficits for such funds were \$34,336 and \$42,362 at September 30, 2016 and 2015, respectively, and are recorded in unrestricted net assets. Such deficits reverse with market value appreciation. Reversals of these deficits increase unrestricted net assets.

**J. Postretirement and Postemployment Benefits**

The Institute provides postretirement health and life insurance benefit plans to eligible retirees and their dependents. The Institute's obligation related to these benefits is actuarially determined based on a September 30 measurement date. The Institute also provides defined contribution retirement plans, which are described in Note B.

Components of the funded status of postretirement benefits reported in the Institute's balance sheet and changes therein were as follows for the years ended September 30, 2016 and 2015. Additional detail regarding the JPL and Campus-related portions of the funded status of postretirement benefits is provided at the end of this note.

	<b>2016</b>	<b>2015</b>
Change in the accumulated postretirement benefit obligation:		
Benefit obligation at beginning of year	\$ 400,995	\$ 369,244
Service cost	10,375	9,982
Interest cost	18,019	15,843
Participant contributions	-	1,654
Benefits paid	(14,275)	(17,486)
Actuarial loss	45,225	21,758
Benefit obligation at end of year	<u>460,339</u>	<u>400,995</u>
Changes in plan assets:		
Fair value of plan assets at beginning of year	21,243	-
Return on plan assets	3,080	(933)
Employer contributions	34,581	38,008
Participant contributions	-	1,654
Benefits paid	(14,275)	(17,486)
Fair value of plan assets at end of year	<u>44,629</u>	<u>21,243</u>
<b>Funded status</b>	<u>\$ (415,710)</u>	<u>\$ (379,752)</u>

Pursuant to a modification of the JPL contract, NASA changed its method of funding postretirement benefits for JPL retirees and their dependents from the pay-as-you-go basis to an accrual-accounting approach based on the Federal Acquisition Regulation during the year ended September 30, 2015. Benefits for campus retirees and their dependents continue to be funded on a pay-as-you-go basis.

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JPL-related contributions in excess of benefits paid are held in a trust for the benefit of JPL retirees and are invested according to the related plan's investment policies. At September 30, 2016 and 2015, trust investments consisted of short-term investments and non-publicly traded collective trust funds and mutual funds. Short-term investments are classified in level 1 of the valuation hierarchy described in Note K, and the collective trust funds and mutual funds, which have readily-determinable fair values, are classified within level 2 of that hierarchy.

Trust investments were held as follows at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Short-term investments	\$ 223	\$ 442
Collective trust funds	13,395	6,224
Mutual funds	31,011	14,577
<b>Total</b>	<u>\$ 44,629</u>	<u>\$ 21,243</u>

Net periodic postretirement benefit cost was as follows for the years ended September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Components of net periodic postretirement benefit cost:		
Service cost	\$ 10,375	\$ 9,982
Interest cost	18,019	15,843
Expected return on plan assets	(1,683)	(470)
Amortization of prior year service credit	(28,188)	(29,642)
Amortization of loss	4,544	3,348
<b>Net periodic benefit cost</b>	<u>\$ 3,067</u>	<u>\$ (939)</u>

The statements of activities include the effects of changes in funded status that are not otherwise recognized in net periodic postretirement benefit cost. The effect related to JPL for the years ended September 30, 2016 and 2015 was an increase of \$47,613 and \$35,900, respectively, in both JPL direct expense and revenue and in deferred U.S. government billings, as any cost associated with this adjustment related to JPL is contractually recoverable from NASA. The effect of those changes for the Campus was a decrease of \$19,859 and \$13,555 in unrestricted net assets for the years ended September 30, 2016 and 2015, respectively, and is recorded in non-operating changes in unrestricted net assets in the statements of activities.



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At September 30, 2016 and 2015, the differences recognized in unrestricted net assets between cumulative net periodic postretirement benefit cost, less cumulative contributions, and funded status were as follows:

	<b>2016</b>	<b>2015</b>
Amounts recognized in unrestricted net assets:		
Prior service credit	\$ (44,384)	\$ (51,259)
Net loss	29,655	16,671
<b>Cumulative amounts recognized in unrestricted net assets</b>	<b>\$ (14,729)</b>	<b>\$ (34,588)</b>

Any actuarial deferrals resulting from changes in the accumulated postretirement benefit obligation are amortized over the average future working lifetime of Institute employees. An estimated prior service credit of \$26,305 and actuarial loss of \$6,958 will be amortized into net periodic benefit cost during the year ending September 30, 2017.

The following weighted-average assumptions were used to determine the Institute's net periodic benefit cost under the plan for the years ended September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Discount rate	4.60%	4.40%
Discount rate for service cost	4.80%	4.40%
Expected return on plan assets	5.75%	5.75%
Health care cost trend rate	7.50%	7.50%

To develop the expected long-term rate of return on assets, the Institute considers the historical returns and future expectations for each asset class, as well as the asset allocation of the retirement plan's investment portfolio. Estimated future return was based on expected returns for various asset categories. The evaluation of the historical and future returns resulted in the selection of 5.75% for the expected return on plan assets.

The following weighted-average assumptions were used to determine the Institute's obligation under the plan at September 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Discount rate	3.80%	4.60%
Discount rate for service cost	4.10%	4.80%
Health care cost trend rate	7.50%	7.50%

The Institute's postretirement medical benefit plans provide a substantial portion of the Institute's retirees and their eligible dependents awards of defined-dollar credits that are available to be used by retirees for medical premiums and other eligible medical expenses. The defined-dollar credits may be

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changed in future years at the Institute's discretion. Certain grandfathered retirees and eligible dependents remain eligible for future medical benefits at no cost through an Institute-sponsored plan. The cost of these benefits is expected to increase in the future according to health care cost trend rates. The assumed health care cost trend rate is 7.50% in 2017, and annual rates are assumed to decrease approximately 0.25% per year until 2029, after which healthcare cost is assumed to increase 4.25% in all future years.

A one-percentage point change in assumed health care cost trend rates would have the following effects:

	<b>1%</b> <b>Increase</b>	<b>1%</b> <b>Decrease</b>
Effect on the total of service and interest cost components	\$ 68	\$ (59)
Effect on accumulated postretirement benefit obligation	\$ 1,343	\$ (1,177)

A substantial majority of the above effects would be related to JPL and therefore would result in corresponding changes in amounts expected to be recoverable from NASA.

At September 30, 2016, the estimated future benefit payments are as follows:

<b>Year Ending September 30</b>	<b>Campus</b>	<b>JPL</b>	<b>Total</b>
2017	\$ 4,249	\$ 13,964	\$ 18,213
2018	4,303	13,881	18,184
2019	4,356	13,746	18,102
2020	4,521	14,121	18,642
2021	4,717	14,693	19,410
2022-2026	27,267	81,827	109,094

Additional detail regarding the JPL and campus-related portions of the funded status of postretirement benefits and changes therein for the years ended September 30, 2016 and 2015, is as follows:

	<b>Campus</b>	<b>JPL</b>	<b>Total</b>
<b>September 30, 2016</b>			
Benefit obligation at end of year	\$ 115,334	\$ 345,005	\$ 460,339
Fair value of plan assets at end of year	-	44,629	44,629
<b>Funded status</b>	<u>\$ (115,334)</u>	<u>\$ (300,376)</u>	<u>\$ (415,710)</u>
<b>September 30, 2015</b>			
Benefit obligation at end of year	\$ 97,439	\$ 303,556	\$ 400,995
Fair value of plan assets at end of year	-	21,243	21,243
<b>Funded status</b>	<u>\$ (97,439)</u>	<u>\$ (282,313)</u>	<u>\$ (379,752)</u>

## **K. Fair Value**

Fair value is defined as the price that the Institute would receive upon selling an asset or would pay to settle a liability in an orderly transaction between market participants. The Institute evaluates the fair value of financial instruments using an established hierarchy that ranks the inputs to valuation techniques used to measure fair value. Inputs refer broadly to the assumptions that market participants would use in such fair value determinations, including assumptions regarding various risks.

A financial instrument's level within the fair value hierarchy is based on the least-transparent level of any input that is significant to the fair value measurement. The classification of financial instruments within the hierarchy is based upon the transparency of the inputs to valuation techniques used to measure fair value and does not necessarily correspond to the Institute's perceived risk of those instruments. The three levels of the fair value hierarchy are described below.

Level 1 fair value measurements are based upon unadjusted quoted prices for identical assets or liabilities in active, accessible markets. Market price data is generally obtained from exchange dealer markets.

Level 2 fair value measurements are generally based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the instruments. Inputs to Level 2 measurements include, but are not limited to, interest rates, credit risk adjustments, and prices for similar instruments, and are obtained from various sources, including market participants, dealers, and brokers.

Level 3 fair value measurements are those that use significant inputs that are unobservable. Assets and liabilities included in Level 3 primarily consist of investments in real assets that are valued by investment managers or the Institute using industry-standard methodologies, independent appraisals, and Institute models. The Institute regularly monitors the adequacy of these fair value measurements. Fair value measurements derived using specific unobservable quantitative inputs developed by the Institute were not significant for the years ended September 30, 2016 and 2015.

The Institute generally uses net asset value ("NAV") as a practical expedient to determine the fair value of investments in funds that do not have readily determinable fair values and either have certain specific attributes of investment companies or prepare their financial statements consistent with the measurement principles of investment companies. For these funds, net asset values are determined by each fund's general partner or investment manager and are based on appraisals or other estimates that include considerations such as the cost of the fund's securities, prices of recent significant placements of securities of the same issuer, and subsequent developments concerning the companies to which the securities relate. The fair value of investments valued at NAV as a practical expedient are excluded from the fair value hierarchy.

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The following is a summary of the fair value of the Institute's financial instruments according to fair value level or NAV at September 30, 2016 and 2015:

	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>NAV</b>	<b>2016 Total</b>
<b>September 30, 2016</b>					
<b>Investments:</b>					
Short-term investments	\$ 178,866	\$ -	\$ -	\$ -	\$ 178,866
Fixed-income securities	30,749	192,604	-	-	223,353
Equity securities	602,132	163,759	6,246	374,574	1,146,711
Alternative investments:					
Alternative securities	-	-	-	798,994	798,994
Private equity	-	-	5,537	276,562	282,099
Real assets	-	18,792	131,597	250,260	400,649
Derivative assets	2,242	-	-	-	2,242
Derivative liabilities	(4,536)	-	-	-	(4,536)
<b>Total investments</b>	<b>\$ 809,453</b>	<b>\$ 375,155</b>	<b>\$ 143,380</b>	<b>\$1,700,390</b>	<b>\$ 3,028,378</b>
<b>Other assets and liabilities:</b>					
Cash and cash equivalents	\$ 6,374	\$ -	\$ -	\$ -	\$ 6,374
Beneficial interests	-	-	73,341	-	73,341
Defined contribution plan assets	26,916	24,147	26,399	-	77,462
Defined contribution plan liabilities	(26,827)	(24,062)	(26,388)	-	(77,277)
Interest rate swap	-	(70,521)	-	-	(70,521)
<b>September 30, 2015</b>					
<b>Investments:</b>					
Short-term investments	\$ 210,636	\$ -	\$ -	\$ -	\$ 210,636
Fixed-income securities	31,496	150,542	-	10,628	192,666
Equity securities	565,146	160,143	6,245	296,262	1,027,796
Alternative investments:					
Alternative securities	-	-	-	776,106	776,106
Private equity	-	-	-	224,986	224,986
Real assets	-	19,152	143,102	235,193	397,447
Derivative assets	8,866	-	-	-	8,866
Derivative liabilities	(3,999)	-	-	-	(3,999)
<b>Total investments</b>	<b>\$ 812,145</b>	<b>\$ 329,837</b>	<b>\$ 149,347</b>	<b>\$1,543,175</b>	<b>\$2,834,504</b>
<b>Other assets and liabilities:</b>					
Cash and cash equivalents	\$ 5,257	\$ -	\$ -	\$ -	\$ 5,257
Beneficial interests	-	-	22,379	-	22,379
Defined contribution plan assets	22,501	23,740	23,490	-	69,731
Defined contribution plan liabilities	(22,422)	(23,661)	(23,479)	-	(69,562)
Interest rate swap	-	(55,409)	-	-	(55,409)

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The fair value of assets held in trust for postretirement benefit plans, as disclosed in Note J, is excluded from the tables above.

At September 30, 2016 and 2015, additional detail regarding the Institute's investments valued using NAV by major investment category was as follows:

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period in days	Lives in years
<b>September 30, 2016</b>					
Equity securities					
Quarterly or less	\$ 120,086	\$ -	Quarterly or less	7 to 180	-
Greater than quarterly	253,972	-	Annually to triennially	60 to 120	-
Not actionable	516	-	Not actionable	-	-
Alternative investments:					
Alternative securities					
Quarterly or less	186,065	-	Quarterly or less	60 to 90	-
Greater than quarterly	414,023	750	Semi-annually to triennially	30 to 90	-
Not actionable	198,906	112,195	Not actionable	-	upto 17
Private equity	276,562	164,629	Not actionable	-	upto 10
Real assets	250,260	77,559	Not actionable	-	upto 10
<b>Total investments</b>	<b>\$ 1,700,390</b>	<b>\$ 355,133</b>			

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period in days	Lives in years
<b>September 30, 2015</b>					
Equity securities					
Quarterly or less	\$ 109,168	\$ -	Quarterly or less	7 to 180	-
Greater than quarterly	171,459	-	Annually to triennially	60 to 120	-
Not actionable	15,635	-	Not actionable	-	-
Fixed-income securities	10,628	-	Quarterly	90	-
Alternative investments:					
Alternative securities					
Quarterly or less	261,285	-	Quarterly or less	60 to 90	-
Greater than quarterly	383,091	750	Annually to triennially	30 to 180	-
Not actionable	131,730	123,445	Not actionable	-	upto 10
Private equity	224,986	145,135	Not actionable	-	upto 10
Real assets	235,193	77,883	Not actionable	-	upto 10
<b>Total investments</b>	<b>\$ 1,543,175</b>	<b>\$ 347,213</b>			

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In addition to the unfunded commitments noted above, at September 30, 2016 and 2015, the Institute was committed to invest an additional \$54,789 and \$42,702, respectively, in investments classified within the fair value hierarchy over approximately the next ten years. Alternative investments may not be readily marketable or redeemable, and may specify penalties for early withdrawal from the related funds.

The methods described above may produce fair value calculations that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Institute believes its valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies or assumptions to determine fair values of certain financial instruments could result in different estimates of fair value.

The following table is a summary of changes in the fair values of the Institute's Level 3 assets for the years ended September 30, 2016 and 2015:

	<b>Beginning Balance</b>	<b>Gifts and Purchases</b>	<b>Sales and Maturities</b>	<b>Realized Gain/Loss</b>	<b>Unrealized Gain/Loss</b>	<b>Ending Balance</b>
<b>September 30, 2016</b>						
Investments:						
Equity securities	\$ 6,245	\$ -	\$ (41)	\$ -	\$ 42	\$ 6,246
Alternative investments:						
Private equity	-	4,000	-	-	1,537	5,537
Real assets	143,102	13,366	(11,819)	1,650	(14,702)	131,597
<b>Total investments</b>	<b>\$ 149,347</b>	<b>\$ 17,366</b>	<b>\$ (11,860)</b>	<b>\$ 1,650</b>	<b>\$ (13,123)</b>	<b>\$ 143,380</b>
Other assets:						
Beneficial interests	\$ 22,379	\$ 72,453	\$ (22,059)	\$ -	\$ 568	\$ 73,341
Defined contribution plans	23,490	4,099	(2,001)	-	811	26,399
	<b>Beginning Balance</b>	<b>Gifts and Purchases</b>	<b>Sales and Maturities</b>	<b>Realized Gain/Loss</b>	<b>Unrealized Gain/Loss</b>	<b>Ending Balance</b>
<b>September 30, 2015</b>						
Investments:						
Equity securities	\$ 6,386	\$ -	\$ -	\$ -	\$ (141)	\$ 6,245
Alternative investments:						
Real assets	143,940	38,201	(13,492)	546	(26,093)	143,102
<b>Total investments</b>	<b>\$ 150,326</b>	<b>\$ 38,201</b>	<b>\$ (13,492)</b>	<b>\$ 546</b>	<b>\$ (26,234)</b>	<b>\$ 149,347</b>
Other assets:						
Beneficial interests	\$ 26,517	\$ 2,849	\$ (6,060)	\$ -	\$ (927)	\$ 22,379
Defined contribution plans	22,765	2,961	(3,021)	-	785	23,490

The Institute classifies defined contribution plan liabilities in the fair value hierarchy based upon the investments of the related plan assets. Accordingly, liabilities classified within Level 3 approximate

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the value of plan investments that also are classified within Level 3, and increase or decrease in value according to contributions, withdrawals, vesting, and investment performance.

The Institute records transfers between levels in the current fiscal year when there is a change in circumstances that affects the liquidity of the assets and/or the ability to observe and measure the fair value. The Institute records such transfers based on the market value at the beginning of the reporting period. There were no transfers among levels during the years ended September 30, 2016 and 2015. During the years ended September 30, 2016 and 2015, unrealized losses related to Level 3 assets of (\$418) and (\$702) respectively, were recorded in non-operating gifts and pledges in the statements of activities. All other realized and unrealized gains related to Level 3 investments were recorded in non-operating investment return in excess of payout in the statement of activities. Unrealized losses included in the statements of activities related to those Level 3 assets held at September 30, 2016 and 2015 were (\$12,813) and (\$25,713), respectively.

The Institute uses an interest rate swap to manage the interest rate exposure of a portion of its variable rate debt. The interest rate swap has inputs that can generally be corroborated by market data and is therefore classified as Level 2. The interest rate swap is valued using observable inputs, such as quotations received from counterparties, dealers, or brokers, whenever available and considered reliable. In instances in which models are used, the value of the interest rate swap depends upon the contractual terms of, and specific risks inherent in, the instrument, as well as the availability and reliability of observable inputs. Such inputs include market prices for reference securities, credit curves, assumptions for nonperformance risk, and correlations of such inputs.

The Institute uses exchange-traded equity derivatives, including put and call options, to manage its market exposure related to certain equity exchange-traded funds. Balances and activities related to equity derivatives for the years ended September 30, 2016 and 2015 were as follows:

	<b>2016</b>	<b>2015</b>
<b>Investments:</b>		
Gross derivative assets	\$ 2,242	\$ 8,866
Gross derivative liabilities	(4,536)	(3,999)
Net amount	<u>\$ (2,294)</u>	<u>\$ 4,867</u>
Notional value: assets	\$ 95,947	\$ 99,373
Notional value: liabilities	(195,957)	204,468
Investments pledged	111,423	99,139
<b>Investment returns/(losses):</b>		
Realized gains	\$ 1,451	\$ 1,411
Unrealized (loss)/gain	(5,926)	2,870
Net amount	<u>\$ (4,475)</u>	<u>\$ 4,281</u>

## **L. Commitments and Contingencies**

### **Contingencies**

The Institute receives funding or reimbursement from agencies of the United States government for various activities that are subject to audit, and is a defendant in various legal actions incident to the conduct of its activities. Except as specifically discussed below, management does not expect that liabilities, if any, related to these audits or legal actions will have a material impact on the Institute's financial position. However, the settlement of audits or legal actions is subject to inherent uncertainties, and it is possible that such liabilities, if any, will differ materially from management's current expectations.

In 1997, the Institute was named as a potentially responsible party ("PRP") by NASA under the Comprehensive Environmental Response, Compensation, and Liability Act, as amended. As a PRP, the Institute may be jointly liable for contribution towards clean-up costs, estimated to be in excess of \$100,000, of the NASA/JPL Superfund site.

Officials of the Institute presently are not able to predict the impact, if any, that final resolution of this matter will have on the Institute's financial position or changes in its net assets. However, the Institute believes that it will have recourse to the United States government for any liabilities it may incur in connection with being named a PRP for that site.

### **Commitments**

The Institute was committed under certain construction and services contracts in the amounts of approximately \$81,074 and \$49,148 at September 30, 2016 and 2015, respectively.

The Institute is a member of an international consortium that was organized to construct and operate an advanced telescope. At September 30, 2016 and 2015, the Institute was committed to provide a combination of cash and in-kind assets totaling approximately \$92,000 and \$102,000, respectively, to the consortium over approximately the next ten years. Payments and other transfers related to this commitment are subject to certain contingencies. Subsequent to September 30, 2016, the Institute and the consortium amended the Institute's commitment to exclude further contributions of in-kind assets, without changing the amount of the total commitment.

The Institute's workers' compensation insurance carrier requires that the Institute maintain an unsecured letter of credit for claims that do not exceed certain deductible amounts. At September 30, 2016 and 2015, the amounts of the letter of credit facility were \$9,400 and \$9,300, respectively. The letter of credit was not used during the years ended September 30, 2016 and 2015, and therefore no liability has been recorded in the balance sheets.

The Institute is currently providing funding for the operation of certain local water treatment facilities, subject to reimbursement from NASA. Annual costs are not expected to exceed \$9,000.

The Institute leases equipment and buildings, primarily for JPL, under operating leases expiring at various dates through 2018. Rent expense incurred under operating lease obligations was \$6,684 and \$5,971 for the years ended September 30, 2016 and 2015, respectively.



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At September 30, 2016, future minimum payments under operating leases of greater than one year in duration were as follows:

<b>Year Ending September 30</b>	<b>Amount</b>
2017	\$ 1,401
2018	1,002
<b>Total</b>	<u>\$ 2,403</u>

Approximately \$1,956 of the future minimum lease payments listed above is expected to be recoverable from JPL under the Institute's cost-reimbursable contract with NASA. The Institute rents housing, equipment, and building space to students, faculty, and other organizations under operating leases expiring at various dates through 2021. Rental income under operating leases was \$9,421 and \$9,484 at September 30, 2016 and 2015, respectively.

At September 30, 2016, minimum future rentals from operating leases of greater than one year in duration were as follows:

<b>Year Ending September 30</b>	<b>Amount</b>
2017	\$ 8,974
2018	6,859
2019	3,646
2020	2,831
2021	2,832
<b>Total</b>	<u>\$ 25,142</u>

**M. Supplemental Cash Flow Information**

The following are additional supplemental disclosures related to the statements of cash flows:

	<b>2016</b>	<b>2015</b>
Cash paid during the year for interest, net of amounts capitalized	\$ 45,541	\$ 29,590
Income taxes paid	-	1,450
Non-cash investing and financing activities:		
Securities received to satisfy pledge payments	41,698	186
In-kind receipt of securities, property, plant, and equipment	19,980	30,726
Accrued purchases of property, plant, and equipment	5,717	3,353
Net amounts receivable for pending investments transactions	44,693	31,168

**N. Subsequent Events**

Subsequent events were evaluated through January 25, 2017, which is the date the financial statements were available to be issued.