NEW ISSUE-Book Entry Only **Ratings: See "RATINGS" herein**

In the opinion of Co-Bond Counsel, based upon certain assumptions and subject to conditions, qualifications and exceptions herein described, under existing laws, regulations, rulings, and judicial decisions, interest on the Series AU-1 Bonds and Series AU-2 Bonds is neither includable in gross income for federal income tax purposes nor a specific "item of tax preference" for purposes of the federal alternative minimum tax, provided, however, that interest paid to corporations is taken into account in determining adjusted current earnings for computing said alternative minimum tax. Under current Pennsylvania law, the Series AU Bonds are exempt from personal property taxes in Pennsylvania and interest on the Series AU Bonds is exempt from Pennsylvania personal income tax and Pennsylvania corporate net income tax. In the opinion of Co-Bond Counsel, interest on the Series AU-3 Bonds IS INCLUDABLE in gross income for purposes of federal income tax. For a more detailed description of Co-Bond Counsel's opinion including the aforementioned assumptions, qualifications and exceptions, see "TAX MATTERS" herein.

$128,260,000
PENNSYLVANIA HIGHER EDUCATIONAL FACILITIES AUTHORITY
(Commonwealth of Pennsylvania)
REVENUE BONDS
STATE SYSTEM OF HIGHER EDUCATION, SERIES AU
Consisting of:

$36,625,000 Series AU-1 Revenue Bonds

$76,490,000 Series AU-2 Refunding Revenue Bonds

$15,145,000 Series AU-3 Federally Taxable Refunding Revenue Bonds

Dated: Date of Delivery **Due: June 15, as shown on the inside front cover**

The Series AU Bonds are issuable only as fully registered bonds without coupons, and when issued, will be registered in the name of Cede & Co., as registered owner and nominee for The Depository Trust Company ("DTC"), New York, New York. DTC will act as securities depository for the Series AU Bonds. Purchase of the Series AU Bonds will be made in book-entry only form, in the denomination of $5,000 or any integral multiple thereof. Purchasers will not receive certificates representing their interest in the Series AU Bonds. So long as the Series AU Bonds are registered in the name of Cede & Co. as nominee of DTC, references herein to the registered owners shall mean Cede & Co., and shall not mean the Beneficial Owners of the Series AU Bonds. See "The Series AU Bonds - Book-Entry Only System" herein.

Principal of and interest on the Series AU Bonds will be paid by The Bank of New York Mellon Trust Company, N.A., Philadelphia, Pennsylvania, as trustee (the "Trustee"). So long as DTC or its nominee, Cede & Co., is the registered owner of the Series AU Bonds, such payments will be made directly to it as registered owner. Disbursement of such payments to the DTC Participants is the responsibility of DTC and disbursement of such payments to the Beneficial Owners is the responsibility of the DTC Participants and the Indirect Participants, as more fully described herein. Interest will be payable on December 15 and June 15, commencing December 15, 2017, to the registered owners of record as of the pertinent record dates herein described.

The Series AU Bonds are subject to redemption prior to maturity as described herein.

The Series AU Bonds are limited obligations of the Authority and are secured under the provisions of the Indenture and the Loan Agreement, as each is defined herein, and are payable solely from payments to be received under the Loan Agreement by the Authority from the State System of Higher Education (the "System") and from certain funds held under the Indenture.

Neither the general credit of the Authority nor the credit or taxing power of the Commonwealth of Pennsylvania or of any political subdivision thereof is pledged for the payment of the principal of or the interest on the Series AU Bonds described above, nor shall such Series AU Bonds be deemed to be general obligations of the Authority or obligations of the Commonwealth of Pennsylvania or any political subdivision thereof, nor shall the Commonwealth of Pennsylvania or any political subdivision thereof be liable for the payment of the principal of or interest on the Series AU Bonds described above. The Authority has no taxing power.

The Series AU Bonds are offered when, as and if issued by the Authority and received by the Underwriters subject to receipt of the approving legal opinion of Kutak Rock LLP and Turner Law, P.C., both of Philadelphia, Pennsylvania, Co-Bond Counsel. Certain legal matters will be passed upon for the Authority by its counsel, Barley Snyder LLP, Lancaster, Pennsylvania, and for the System by its Chief Legal Counsel. It is expected that the Series AU Bonds in definitive form will be available for delivery in New York, New York on or about September 14, 2017.

This cover page contains certain information for quick reference only. It is not a summary of the issue. Prospective purchasers of the Series AU Bonds must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

The date of this Official Statement is September 6, 2017.

$128,260,000
PENNSYLVANIA HIGHER EDUCATIONAL

FACILITIES AUTHORITY
(Commonwealth of Pennsylvania)
STATE SYSTEM OF HIGHER EDUCATION, SERIES AU

MATURITY SCHEDULES

$36,625,000 Series AU-1 Revenue Bonds

Maturity (June 15)	Amount	Interest	Yield	Price	CUSIP†
2018	$1,005,000	5.000%	0.850%	103.106	70917S G56
2019	1,135,000	5.000%	1.000%	106.931	70917S G64
2020	1,205,000	5.000%	1.170%	110.343	70917S G72
2021	1,285,000	5.000%	1.310%	113.467	70917S G80
2022	1,360,000	5.000%	1.420%	116.395	70917S G98
2023	1,450,000	5.000%	1.600%	118.612	70917S H22
2024	1,535,000	5.000%	1.800%	120.258	70917S H30
2025	1,625,000	5.000%	2.000%	121.442	70917S H48
2026	1,720,000	5.000%	2.140%	122.714	70917S H55
2027	1,825,000	5.000%	2.280%	123.661	70917S H63
2028	1,930,000	4.000%	2.450%	113.371[c]	70917S H71
2029	2,030,000	4.000%	2.550%	112.447[c]	70917S H89
2030	2,125,000	4.000%	2.630%	111.714[c]	70917S H97
2031	2,230,000	3.000%	2.900%	100.841[c]	70917S J20
2032	2,315,000	3.000%	2.960%	100.333[c]	70917S J38
2033	1,745,000	3.000%	3.020%	99.747	70917S J46
2034	1,815,000	3.000%	3.080%	98.956	70917S J53
2035	1,885,000	3.000%	3.170%	97.702	70917S J61
2036	1,965,000	3.000%	3.200%	97.193	70917S J79
2037	2,045,000	3.125%	3.230%	98.472	70917S J87
2038	450,000	3.125%	3.250%	98.120	70917S J95
2039	465,000	3.125%	3.270%	97.752	70917S K28
2040	480,000	3.125%	3.290%	97.368	70917S K36
2041	490,000	3.125%	3.320%	96.810	70917S K44
2042	510,000	3.250%	3.340%	98.488	70917S K51

[c] Priced at the stated yield to the June 15, 2027 optional redemption date.

MATURITY SCHEDULES

$76,490,000 Series AU-2 Refunding Revenue Bonds

Maturity (June 15)	Amount	Interest	Yield	Price	CUSIP†
2018	$1,095,000	5.000%	0.950%	103.029	70917S D83
2019	2,695,000	5.000%	1.050%	106.840	70917S D91
2020	3,575,000	5.000%	1.170%	110.343	70917S E25
2021	4,830,000	5.000%	1.310%	113.467	70917S E33
2022	5,920,000	5.000%	1.420%	116.395	70917S E41
2023	6,225,000	5.000%	1.600%	118.612	70917S E58
2024	4,220,000	5.000%	1.800%	120.258	70917S E66
2025	4,510,000	5.000%	2.000%	121.442	70917S E74
2026	5,475,000	5.000%	2.140%	122.714	70917S E82
2027	5,750,000	5.000%	2.280%	123.661	70917S E90
2028	6,035,000	5.000%	2.400%	122.484c	70917S F24
2029	3,740,000	4.000%	2.600%	111.988c	70917S F32
2030	3,895,000	4.000%	2.700%	111.078c	70917S F40
2031	4,045,000	3.000%	2.950%	100.418c	70917S F57
2032	4,170,000	3.000%	3.050%	99.406	70917S F65
2033	4,295,000	3.000%	3.121%	98.500	70917S F73
2034	1,130,000	3.000%	3.180%	97.673	70917S F81
2035	1,165,000	3.125%	3.237%	98.500	70917S F99
2036	1,200,000	3.125%	3.268%	98.000	70917S G23
2037	1,240,000	3.250%	3.284%	99.500	70917S G31
2038	1,280,000	3.250%	3.317%	99.000	70917S G49

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c Priced to the stated yield to the June 15, 2027 optional redemption date.

MATURITY SCHEDULES

$15,145,000 Series AU-3 Federally Taxable Refunding Revenue Bonds

Maturity (June 15)	Amount	Interest	Yield	Price	CUSIP†
2018	$ 255,000	1.250%	1.480%	99.827	70917S K69
2019	1,370,000	1.500%	1.600%	99.827	70917S K77
2020	1,385,000	1.500%	1.800%	99.196	70917S K85
2021	1,410,000	1.750%	2.010%	99.063	70917S K93
2022	1,435,000	2.000%	2.160%	99.279	70917S L27
2023	1,460,000	2.000%	2.350%	98.125	70917S L35
2024	1,490,000	2.250%	2.500%	98.453	70917S L43
2025	1,525,000	2.500%	2.620%	99.160	70917S L50
2026	1,565,000	2.500%	2.770%	97.912	70917SL68
2027	1,600,000	2.750%	2.870%	98.983	70917SL76
2028	1,650,000	2.750%	2.920%	98.438	70917S L84

PENNSYLVANIA HIGHER EDUCATIONAL FACILITIES AUTHORITY
(Commonwealth of Pennsylvania)
1035 Mumma Road
Wormleysburg, Pennsylvania 17043

BOARD MEMBERS OF THE AUTHORITY

Honorable Thomas W. Wolf
Governor of the Commonwealth of Pennsylvania .... President

Honorable John H. Eichelberger, Jr.
Designated by the President Pro Tempore of the Senate .... Vice President

Honorable Andrew E. Dinniman
Designated by the Minority Leader of the Senate .... Vice President

Honorable Stanley E. Saylor
Designated by the Speaker of the House of Representatives .... Vice President

Honorable Joseph M. Torsella
State Treasurer .... Treasurer

Honorable Curtis M. Topper
Secretary of General Services .... Secretary

Honorable Anthony M. DeLuca
Designated by the Minority Leader of the House of Representatives .... Board Member

Honorable Eugene A. DePasquale
Auditor General .... Board Member

Honorable Pedro A. Rivera
Secretary of Education .... Board Member

EXECUTIVE DIRECTOR
Robert Baccon

AUTHORITY COUNSEL
(Appointed by the Office of General Counsel)
Barley Snyder LLP
Lancaster, Pennsylvania

TRUSTEE
The Bank of New York Mellon Trust Company, N.A.
Philadelphia, Pennsylvania

CO-BOND COUNSEL
(Appointed by the Office of General Counsel)

Kutak Rock LLP
Philadelphia, Pennsylvania

Turner Law, P.C.
Philadelphia, Pennsylvania

FINANCIAL ADVISOR
to the State System of Higher Education
RBC Capital Markets, LLC
Philadelphia, Pennsylvania

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVER-ALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SERIES AU BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

No dealer, broker, salesman, or other person has been authorized by the Pennsylvania Higher Educational Facilities Authority, the State System of Higher Education or the Underwriter to give any information or to make any representations, other than those contained in this Official Statement, and if given or made, such other information or representations must not be relied upon as having been authorized by any of the foregoing. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Series AU Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale. The information set forth herein has been obtained from the State System of Higher Education, and other sources which are believed to be reliable but it is not guaranteed as to accuracy or completeness, and is not to be construed as a representation by the Underwriter or, as to information from other sources, by the Pennsylvania Higher Educational Facilities Authority or the State System of Higher Education. The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in any of the information set forth herein since the date hereof or the date as of which particular information is given, if earlier.

The Series AU Bonds are not and will not be registered under the Securities Act of 1933, as amended, or under any state securities laws, and the Indenture has not been and will not be qualified under the Trust Indenture Act of 1939, as amended, in reliance on exemptions contained in such laws. Neither the Securities and Exchange Commission nor any federal, state, municipal or other governmental agency will pass upon the accuracy, completeness or adequacy of this Official Statement.

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OFFICIAL STATEMENT

$128,260,000
PENNSYLVANIA HIGHER EDUCATIONAL
FACILITIES AUTHORITY
(COMMONWEALTH OF PENNSYLVANIA),
REVENUE BONDS
STATE SYSTEM OF HIGHER EDUCATION SERIES AU

Consisting of:

$36,625,000 Series AU-1 Revenue Bonds	**$76,490,000 Series AU-2 Refunding Revenue Bonds**	**$15,145,000 Series AU-3 Federally Taxable Refunding Revenue Bonds**

INTRODUCTION

This Introduction is qualified in all respects by the more detailed information appearing elsewhere in this Official Statement and in the Appendices hereto.

General

This Official Statement, including the cover page and the Appendices hereto, sets forth certain information concerning the issuance by the Pennsylvania Higher Educational Facilities Authority (the "Authority," the offices of which are located at 1035 Mumma Road, Wormleysburg, Pennsylvania 17043), of the Authority's Revenue Bonds, State System of Higher Education, Series AU consisting of its $36,625,000 Series AU-1 Revenue Bonds (the "Series AU-1 Bonds") and its $76,490,000 Series AU-2 Refunding Revenue Bonds (the "Series AU-2 Bonds") and its $15,145,000 Series AU-3 Federally Taxable Refunding Revenue Bonds (the "Series AU-3 Bonds", and collectively with the Series AU-1 Bonds and the Series AU-2 Bonds, the "Series AU Bonds"). The Authority is a body corporate and politic constituting a public corporation and a public instrumentality of the Commonwealth of Pennsylvania, created by The Pennsylvania Higher Educational Facilities Authority Act of December 6, 1967, P.L. 678, No. 318, as amended (the "Act"). See **"The Authority"** herein for certain information about the Authority.

The Series AU Bonds are being issued on behalf of the State System of Higher Education (the "System" or "SSHE"), a body corporate and politic constituting a public corporation and a governmental instrumentality of the Commonwealth of Pennsylvania, created by the State System of Higher Education Act of November 12, 1982, P.L. 660, No. 188, as amended ("Act 188"). See **Appendix I: "Certain Information Concerning Pennsylvania's State System of Higher Education"** for certain information concerning the System.

Certain capitalized terms used and not otherwise defined herein shall have the meaning assigned to them in **Appendix III: "Summary of Legal Documents -- Definitions of Certain Terms".**

The Series AU Bonds

The Series AU Bonds are being issued by the Authority in the aggregate principal amount of $128,260,000. They will be dated their date of delivery, and will bear interest from such date, payable June 15 and December 15, commencing December 15, 2017, at the rates set forth on the inside of the front cover page hereof and shall be subject to redemption prior to maturity as described herein. See **"The Series AU Bonds -- Redemption Provisions"** herein.

The Series AU Bonds will be issued pursuant to the Act and an Indenture of Trust dated as of June 1, 1985 (the "Original Indenture"), as previously supplemented and as further supplemented by a Forty-Third Supplemental Indenture of Trust dated as of September 1, 2017 (collectively, the "Indenture"), between the Authority and The Bank of New York Mellon Trust Company, N.A., Philadelphia, Pennsylvania, as trustee (the "Trustee"). The Series AU Bonds will be equally and ratably secured (as and to the extent described below) with the Outstanding bonds of forty-five prior series under the Indenture (such prior bonds are referred to collectively herein as the "Prior Bonds"). The Prior Bonds, the Series AU Bonds and any Additional Bonds which may be Outstanding from time to time under the Indenture are referred to collectively herein as "Bonds." As of July 1, 2017, there was a total of $1,140,700,000 in aggregate principal amount of Prior Bonds outstanding. See **"Sources of and Security for Payment of the Series AU Bonds"** herein.

The Series AU Bonds are issuable only as fully registered bonds without coupons, and when issued, will be registered in the name of Cede & Co., as registered owner and nominee for The Depository Trust Company ("DTC"), New York, New York. See "**The Series AU Bonds -- Book-Entry Only System**" herein.

Use of Proceeds

Pursuant to a Loan and Security Agreement dated as of June 1, 1985, between the Authority and the System, as previously supplemented and as further supplemented, in particular by a Forty-Third Supplemental Loan and Security Agreement dated as of September 1, 2017 (collectively, the "Loan Agreement"), the Authority will lend the proceeds of the Series AU Bonds to the System, which will use such proceeds as more fully described herein under **"Sources and Uses of Funds"** and **"Plan of Finance."**

Security for the Series AU Bonds

The Series AU Bonds are being issued on a parity (except as to certain funds held under the Indenture) with the Prior Bonds and any Additional Bonds with respect to the amounts payable by the System under the Loan Agreement and by an assignment to the Trustee of all the right, title, and interest of the Authority in and to the Loan Agreement (except for the Authority's right to payment of certain fees and expenses and to indemnification), including such amounts payable thereunder. **The Loan Agreement is an unsecured general obligation of the System and the full faith and credit of the System is pledged to the payment of all sums due thereunder.** See **"Sources of and Security for Payment of the Series AU Bonds" and Appendix III: "Summary of Legal Documents"** herein.

Neither the general credit of the Authority nor the credit or taxing power of the Commonwealth of Pennsylvania or of any political subdivision thereof is pledged for the payment of the principal of or the interest on the Series AU Bonds, nor shall the Series AU Bonds be deemed to be general obligations of the Authority or obligations of the Commonwealth of Pennsylvania or any political subdivision thereof, nor shall the Commonwealth of Pennsylvania or any political subdivision thereof be liable for the payment of the principal of or interest on the Series AU Bonds. The Authority has no taxing power.

Availability of Documents

The general descriptions of various legal documents set forth in this Official Statement do not purport to be comprehensive or definitive and reference should be made to each document for the terms and provisions thereof. Copies of all documents referred to herein are available for inspection during normal business hours at the designated corporate trust office of the Trustee in Philadelphia, Pennsylvania. All statements herein are qualified in their entirety by the terms of each such document.

THE SERIES AU PROJECT

As further discussed below, the Series AU Bonds are being issued to finance the costs of the Series AU-1 Project, the Series AU-2 Project and the Series AU-3 Project as further discussed and defined below.

Plan of Finance

The Series AU-1 Project. The Series AU-1 Bonds are being issued to provide funds to the System to finance: (i) construction and renovation of academic and athletic renovations at Indiana University of Pennsylvania; (ii) renovation of academic facilities at Slippery Rock University of Pennsylvania; (iii) construction of a guaranteed energy savings act (GESA) project at Slippery Rock University of Pennsylvania; (iv) construction of a parking structure at West Chester University of Pennsylvania; and (v) contingency and issuance costs related to the Series AU-1 Bonds (collectively, the "Series AU-1 Project").

Plan of Refunding

The Series AU-2 Project. The Series AU-2 Bonds are being issued to provide funds to the System to finance: (i) the advance refunding of certain of the Authority's State System of Higher Education Revenue Bonds, Series AH of 2008 and (ii) contingencies and payment of costs and expenses incident to the issuance of the Series AU-2 Bonds (the "Series AU-2 Project").

The Series AU-3 Project. The Series AU-3 Bonds are being issued to provide funds to the System to finance: (i) the advance refunding of certain of the Authority's State System of Higher Education Revenue Bonds, Series AH of 2008 on a federally taxable basis and (ii) contingencies and payment of costs and expenses incident to the issuance of the Series AU-3 Bonds (the "Series AU-3 Project," and collectively with the Series AU-1 Project, and the Series AU-2 Project, the "Series AU Project").

A portion of the proceeds of the Series AU-2 Bonds and the Series AU-3 Bonds will be irrevocably deposited with The Bank of New York Mellon Trust Company, N.A., as escrow agent (the "Escrow Agent"), and applied pursuant to an escrow deposit agreement between the Authority and the Escrow Agent, to the purchase of United States Treasury Securities the principal and interest on which will be sufficient to pay when due the principal and interest on the Refunded Bonds (hereinafter defined) and to redeem such Refunded Bonds on their redemption date at their redemption price in accordance with an Escrow Agreement between the Authority and the Escrow Agent.

The Refunded Bonds

Series AH Bonds being refunded are as set forth below (the "Refunded Bonds").

(June 15) Maturity	Principal	CUSIP
2018	$4,400,000	70917R RQ0
2019	6,290,000	70917R RR8
2020	6,595,000	70917R RS6
2021	6,865,000	70917R RT4
2022	7,140,000	70917R RU1
2023	7,425,000	70917R RV9
2024	6,140,000	70917R RW7
2025	6,395,000	70917R RX5
2026	6,720,000	70917R RY3
2027	7,050,000	70917R RZ0
2028	7,405,000	70917R SA4
2030	7,025,000	70917R SB2
2033	11,825,000	70917R SC0
2038	5,770,000	70917R SD8

Verification of Mathematical Computations

Financial S&Lutions, LLC, (the "Verification Agent") will deliver to the Authority, on or before the date of issuance of the Series AU Bonds, an attestation report (the "Verification Report") to the effect that the Verification Agent has verified the mathematical accuracy of the schedules provided by the Financial Advisor, RBC Capital Markets, LLC, and the Underwriters with respect to the Refunded Bonds and the Series AU Bonds. Included in the scope of its engagement will be a verification of the mathematical accuracy of (a) computations of the adequacy of the cash and the maturing principal of and interest on the securities required under the Indenture which will be placed in escrow to pay, when due, the maturing principal of, interest on the Refunded Bonds and to pay the related price thereof on their redemption date; and (b) any necessary mathematical computations required to support the conclusion of Bond Counsel that the interest on the Series AU-2 Bonds is exempt from federal taxation.

ESTIMATED SOURCES AND USES OF FUNDS

The following table sets forth estimated sources and uses of funds for the Series AU Project:

Sources:

	Series AU-1	Series AU-2	Series AU-3	Total
Series AU Bond Proceeds	$36,625,000.00	$76,490,000.00	$15,145,000.00	$128,260,000.00
Plus Original Issue Premium	3,168,419.25	10,046,582.50	-	13,215,001.75
(Less) Original Issue Discount	(207,974.90)	(175,964.90)	(175,462.20)	(559,402.00)
Total Sources:	$39,585,444.35	$86,360,617.60	$14,969,537.80	$140,915,599.75

Uses:

	Series AU-1 Project	Series AU-2 Project	Series AU-3 Project	Total
Series AU Bond Proceeds (Project) Fund	$39,116,363.97	-	-	$39,116,363.97
Escrow Deposit Account for the Refunded Bonds(1)	-	$85,781,464.48	$14,876,452.01	100,657,916.49
Issuance Costs	88,232.02	204,651.20	41,020.31	333,903.53
Underwriters' Discount	380,848.36	374,501.92	52,065.48	807,415.76
Total Uses:	$39,585,444.35	$86,360,617.60	$14,969,537.80	$140,915,599.75

(1) A portion of the proceeds in the amount of $42.52 with respect to the Series AU-2 Bonds and $45.01 with respect to the Series AU-3 Bonds will be deposited into the Escrow Deposit Accounts for the Refunded Bonds and will be held as cash. The remaining amount will be used to purchase United States Treasury Securities.

(2) Includes fees and expenses of Co-Bond Counsel, the Financial Advisor, the Authority, the Trustee, the Verification Agent, rating agency fees, printing fees and miscellaneous fees and expenses.

THE AUTHORITY

The Authority is a body corporate and politic, constituting a public corporation and a public instrumentality of the Commonwealth of Pennsylvania (the "Commonwealth" or "State"), created by the Pennsylvania Higher Educational Facilities Authority Act of 1967 (Act No. 318 of the General Assembly of the Commonwealth of Pennsylvania, approved December 6, 1967, as amended) (the "Act").

The Authority is authorized under the Act, among other things, to acquire, construct, finance, improve, maintain, operate, hold and use any educational facility (as therein defined) and, with respect to a college, to finance projects by making loans, to lease as lessor or lessee, to transfer or sell any educational facility or property, to charge and collect amounts for the payment of expenses of the Authority and for payment of the principal of and interest on its obligations, to issue bonds and other obligations for the purpose of paying the cost of projects, to issue refunding bonds and to pledge all or any of the revenues of the Authority for all or any of such obligations, and to enter into trust indentures providing for the issuance of such obligations and for their payment and security.

Under the Act, the Board of the Authority (the "Board") consists of the Governor of the Commonwealth, the State Treasurer, the Auditor General, the Secretary of the Department of Education, the Secretary of the Department of General Services, the President Pro Tempore of the Senate, the Speaker of the House of Representatives, the Minority Leader of the House of Representatives and the Minority Leader of the Senate. Pursuant to the Act, the President Pro Tempore of the Senate, the Speaker of the House of Representatives, the Minority Leader of the Senate and the Minority Leader of the House of Representatives may designate a member of their respective legislative bodies to act as a member of the Authority in their stead. The members of the Board serve without compensation but are entitled to reimbursement for all necessary expenses incurred in connection with the performance of their duties as members. The powers of the Authority are exercised by the Board.

The Authority has issued from time to time other series of revenue bonds and notes for the purpose of financing projects for higher educational institutions in the Commonwealth. None of the revenues of the Authority with respect to any of such revenue bonds and notes are pledged as security for the Series AU Bonds and, conversely, such revenue bonds and notes above are not payable from or secured by the revenues of the Authority or other moneys securing the Series AU Bonds.

The Authority may in the future issue other series of bonds for the purpose of financing projects for educational institutions in the Commonwealth. Each such series of bonds will be secured by instruments separate and apart from the Indenture securing the Series AU Bonds, except for any Additional Bonds issued thereunder.

On May 1, 1991, the Authority was unable to make payments to bondholders with respect to a series of revenue bonds issued by the Authority on behalf of a college because of defaults on payment obligations related to such series of revenue bonds by such college. The Florida Department of Banking and Finance, Division of Securities and Investor Protection, generally requires disclosure by any issuer of securities sold in Florida of defaults on any other obligations of such issuer. Because these defaulted bonds were special obligations payable only from revenues received from the particular college or from other limited sources, but not from revenues pledged to pay any series of bonds, and the full faith and credit of the Authority was not pledged to secure the payment of such bonds, such default is not material with respect to the offering and sale of the Series AU Bonds, and further details with respect thereto are not being provided.

The Series AU Bonds are being issued under the Act pursuant to a resolution of the Authority adopted on July 19, 2017, and pursuant to the Indenture.

Except for the Prior Bonds and any Additional Bonds, none of the revenues of the Authority with respect to any of the revenue bonds and notes referred to above are pledged as security for any of the Series AU Bonds and, conversely, the revenue bonds and notes referred to above are not payable from or secured by the revenues of the Authority or other moneys securing the Series AU Bonds. See **"Sources of and Security for Payment of the Series AU Bonds".**

The following are key staff members of the Authority who are involved in the administration of the financing and projects:

Robert Baccon, Executive Director

Mr. Baccon has served as an executive of both the Authority and the State Public School Building Authority (the "SPSBA") since 1984. He is a graduate of St. John's University with a bachelor's degree in management and holds a master's degree in international business from the Columbia University Graduate School of Business. Prior to joining the Authority, Mr. Baccon held financial management positions with multinational U.S. corporations and was Vice President - Finance for a major highway construction contractor.

David Player, Comptroller & Director of Financial Management

Mr. Player serves as the Comptroller & Director of Financial Management of both the SPSBA and the Authority. He has been with the SPSBA and the Authority since 1999. Prior to his present position, he served as Senior Accountant for the SPSBA and the Authority and as an auditor with the Pennsylvania Department of the Auditor General. Mr. Player is a graduate of the Pennsylvania State University with a bachelor's degree in accounting. He is a Certified Public Accountant and Certified Internal Auditor.

Beverly M. Nawa, Administrative Officer

Mrs. Nawa has served as the Administrative Officer of both the Authority and the SPSBA since 2004. She is a graduate of Alvernia University with a bachelor's degree in business administration. Prior to her present employment, Mrs. Nawa served as an Audit Senior Manager and an Accounting Systems Analyst with the Pennsylvania Department of the Auditor General.

THE SERIES AU BONDS

Description of the Series AU Bonds

The Series AU Bonds shall be dated their date of delivery, will mature on the dates and in the amounts and shall be payable as to interest, on June 15 and December 15 of each year commencing December 15, 2017, at the rates set forth on the inside of the cover page hereof. The Series AU Bonds shall be subject to redemption prior to maturity as described below.

The Series AU Bonds will be issued in fully registered form and, when issued, will be registered in the name of Cede & Co., as registered owner and nominee of DTC. Purchases of the Series AU Bonds will be made in book-entry only form, in denominations of $5,000 and any integral multiple thereof. Beneficial Owners will not receive certificates representing their interests in the Series AU Bonds purchased. So long as Cede & Co. is the registered owner, as nominee of DTC, references herein to the registered owners shall mean Cede & Co., as aforesaid, and shall not mean the Beneficial Owners of the Series AU Bonds. See "Book-Entry Only System" below.

Principal of and interest on the Series AU Bonds will be paid by The Bank of New York Mellon Trust Company, N.A., Philadelphia, Pennsylvania, as Trustee. So long as DTC or its nominee, Cede & Co., is the registered owner of the Series AU Bonds, such payments will be made directly to it as registered owner. Disbursement of such payments to the DTC Participants is the responsibility of DTC and disbursement of such payments to the Beneficial Owners is the responsibility of the DTC Participants and the Indirect Participants, as more fully described herein.

Book-Entry-Only System

THE INFORMATION IN THIS SECTION CONCERNING DTC AND DTC'S BOOK-ENTRY SYSTEM HAS BEEN OBTAINED FROM DTC, AND THE SYSTEM, THE AUTHORITY AND THE TRUSTEE TAKE NO RESPONSIBILITY FOR THE ACCURACY THEREOF.

Purchasers of Series AU Bonds (the "Beneficial Owners") will not receive certificates representing their interest in the Series AU Bonds. Purchases of beneficial interests in the Series AU Bonds will be made in book-entry only form in Authorized Denominations by credit to participating broker-dealers and other institutions on the books of DTC as described herein. Payments of principal of and interest on the Series AU Bonds will be made by the Trustee directly to DTC as the registered Owner thereof. Disbursement of such payments to the Direct Participants (as hereinafter defined) is the responsibility of DTC and disbursements of such payments to the Beneficial Owners is the responsibility of the Direct Participants and the Indirect Participants (as hereinafter defined), as more fully described herein. Any purchaser of beneficial interests in the Series AU Bonds must maintain an account with a broker or dealer who is, or acts through, a Direct Participant to receive payment of the principal of and interest on such Series AU Bonds.

The Depository Trust Company, New York, New York ("DTC") will act as securities depository for the Series AU Bonds (the "Bond Depository"). The Series AU Bonds will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered bond certificate will be issued for each maturity of the Series AU Bonds, each in the aggregate principal amount of the Series AU Bonds of such maturity, and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org.

Purchases of Series AU Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series AU Bonds on DTC's records. The ownership interest of each Beneficial Owner is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Series AU Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Series AU Bonds, except in the event that use of the book-entry system for the Series AU Bonds is discontinued.

To facilitate subsequent transfers, all Series AU Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of the Series AU Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series AU Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series AU Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of the Series AU Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series AU Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond Documents. For example, Beneficial Owners of the Series AU Bonds may wish to ascertain that the nominee holding the Series AU Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Series AU Bonds within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Series AU Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Series AU Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Series AU Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Authority or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, the Trustee, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Series AU Bonds at any time by giving reasonable notice to the Authority or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, bond certificates are required to be printed and delivered.

The Authority may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, bond certificates will be printed and delivered.

SO LONG AS CEDE & CO., AS THE NOMINEE FOR DTC, IS THE REGISTERED OWNER OF THE SERIES AU BONDS, THE AUTHORITY AND THE TRUSTEE WILL TREAT CEDE & CO. AS THE ONLY REGISTERED OWNER OF THE SERIES AU BONDS FOR ALL PURPOSES UNDER THE INDENTURE, INCLUDING RECEIPT OF ALL PRINCIPAL OF AND INTEREST ON THE SERIES AU BONDS, RECEIPT OF NOTICES, AND VOTING.

The Trustee will pay principal of and interest on the Series AU Bonds to or upon the order of the respective Owners, as shown on the Bond Register, or upon their respective attorneys duly authorized in writing, as provided in the Indenture, and all such payments will be valid and effective to fully satisfy the Authority's obligations with respect to the payment of principal and interest on the Series AU Bonds to the extent of the sum or sums so paid. Upon delivery by the nominee of DTC to the Trustee of written notice to the effect that DTC has determined to substitute a new nominee in place of the existing nominee, and subject to the provisions of the Indenture with respect to record dates, the word "Cede & Co." in the Indenture will refer to such new nominee of DTC.

In the event the Authority or the Trustee receives written notice from DTC to the effect that DTC is unable or unwilling to discharge its responsibilities, and the Authority is unable to find a substitute depository, in the opinion of the Authority, willing and able to undertake the functions of the Bond Depository upon reasonable and customary terms, then the Series AU Bonds will no longer be restricted to being registered in the Bond Register in the name of the nominee of DTC or DTC, but may be registered in whatever name or names the Beneficial Owners (as certified by DTC) transferring or exchanging the Series AU Bonds will designate, in accordance with the provisions of the Indenture.

In the event the Authority determines that it is in the best interests of the Beneficial Owners of the Series AU Bonds that they be able to obtain bond certificates, the Authority may notify DTC and the Trustee, whereupon DTC will notify the Direct Participants and Indirect Participants of the availability through the nominee or DTC of bond certificates. In such event, the Trustee will issue, transfer, and exchange Series AU Bond certificates as requested by DTC and any other Bondowners in appropriate amounts, and whenever the Bond Depository requests the Authority and the Trustee to do so, the Authority and the Trustee will cooperate with DTC by taking appropriate action after reasonable notice (i) to make available one or more separate certificates evidencing the Series AU Bonds to any nominee or Direct Participant having Series AU Bonds credited to its account or (ii) to arrange for another securities depository to maintain custody of certificates evidencing the Series AU Bonds.

Notwithstanding any other provision described herein or contained in the Indenture to the contrary, so long as any Series AU Bond is registered in the name of the nominee of DTC, all payments with respect to the principal of and interest on such Series AU Bond will be made and given, respectively, to the nominee or DTC in the manner provided in the Blanket Letter of Representation entered into between DTC and the Authority.

In connection with any notice or communication to be provided to Bondowners pursuant to the Indenture by the Authority or the Trustee with respect to any consent or other action to be taken by Bondowners, the Authority, or the Trustee, as the case may be, will establish a record date for such consent or other action and give the nominee or DTC notice of such record date not less than fifteen (15) calendar days in advance of such record date to the extent possible.

THE SYSTEM, THE AUTHORITY AND THE TRUSTEE HAVE NO RESPONSIBILITY OR OBLIGATIONS TO THE DIRECT OR INDIRECT PARTICIPANTS OR THE BENEFICIAL OWNERS WITH RESPECT TO (A) THE ACCURACY OF ANY RECORDS MAINTAINED BY DTC OR ANY DIRECT OR INDIRECT PARTICIPANT; (B) THE PAYMENT BY DTC OR ANY DIRECT OR INDIRECT PARTICIPANT OF ANY AMOUNT DUE TO ANY BENEFICIAL

OWNER IN RESPECT OF THE PRINCIPAL OF AND INTEREST ON THE SERIES AU BONDS; (C) THE DELIVERY OR TIMELINESS OF DELIVERY BY DTC OR ANY DIRECT OR INDIRECT PARTICIPANT OF ANY NOTICE TO ANY BENEFICIAL OWNER THAT IS REQUIRED OR PERMITTED UNDER THE TERMS OF THE INDENTURE TO BE GIVEN TO BONDOWNERS; (D) THE SELECTION OF THE BENEFICIAL OWNERS TO RECEIVE PAYMENTS IN THE EVENT OF ANY PARTIAL REDEMPTION OF THE SERIES AU BONDS; OR (E) ANY CONSENT GIVEN OR OTHER ACTION TAKEN BY DTC, OR ITS NOMINEE, CEDE & CO., AS REGISTERED BONDOWNER.

Redemption Provisions

The Series AU Bonds are subject to redemption as follows:

Optional Redemption: The Series AU-1 Bonds and the Series AU-2 Bonds maturing on and after June 15, 2028 are subject to optional redemption prior to maturity by the Authority at the written direction of the System in whole at any time or in part from time to time, on and after June 15, 2027 at a redemption price equal to one hundred percent (100%) of the principal amount thereof, plus accrued interest thereon to the date of redemption. Any partial redemption may be in any order of maturity and in any principal amount within a maturity as designated by the System by lot within a maturity. The Series AU-1 Bonds and Series AU-2 Bonds to be redeemed within any maturity will be selected by the Trustee by lot.

The Series AU-3 Bonds are not subject to optional redemption.

Extraordinary Optional Redemption: The Series AU Bonds will be subject to redemption prior to maturity at the option of the Authority, at the direction of the System, in whole at any time, or in part from time to time, with respect to the Series AU Bonds in any order of maturity selected by the System, and within any maturity by lot, upon payment of a redemption price equal to one hundred percent (100%) of the principal amount thereof, plus accrued interest to the date of redemption, but only in the event that all or a portion of the Projects financed or refinanced with the proceeds of the Series AU Bonds are damaged, destroyed or condemned, or sold under threat of condemnation, and it is determined that repair or reconstruction is not desirable, practical or financially feasible, from and to the extent of insurance proceeds, condemnation awards or proceeds of sale in lieu of condemnation received by the Trustee as a result of such damage, destruction, condemnation or sale under threat of condemnation.

Notice of Redemption: Notice of any redemption, identifying the Series AU Bonds or portions thereof to be redeemed, will be given not more than 45 nor less than 30 days prior to the redemption date, by first-class mail, postage prepaid, to the registered owners of the Series AU Bonds to be redeemed. Any defect in the notice or the mailing thereof with respect to any Series AU Bond will not affect the validity of the redemption as to any other Series AU Bonds. No further interest will accrue on the principal of any Series AU Bonds called for redemption after the date fixed for redemption if payment of the redemption price thereof has been duly provided for, and the registered owners of such Series AU Bonds will have no rights under the Indenture except to receive payment of the redemption price thereof and unpaid interest accrued to the date fixed for redemption. If the notice so specifies, a call for redemption may be conditioned on the deposit of funds for redemption by the redemption date, in the absence of which deposit the call for redemption would be of no effect. The Trustee will not be responsible for mailing notices of redemption to anyone other than DTC or its nominee as long as DTC acts as securities depository for the Series AU Bonds.

DEBT SERVICE REQUIREMENTS ON THE SERIES AU BONDS AND THE PRIOR BONDS

The following tables set forth, for each of the periods indicated, the amounts required in such periods to be made available for the captioned purposes:

Fiscal Year Ending June 30	Series AU-1 Bonds			Series AU-2 Bonds			Series AU-3 Bonds			Prior Bonds Total Debt Service[1]	Refunded Bonds Debt Service	Net Total Debt Service
	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total			
2018	1,005,000	1,090,539.75	2,095,539.75	1,095,000	2,549,587.77	3,644,587.77	255,000	246,337.12	501,337.12	118,007,885.10	8,904,368.78	115,344,980.96
2019	1,135,000	1,398,437.50	2,533,437.50	2,695,000	3,332,156.26	6,027,156.26	1,370,000	324,050.00	1,694,050.00	119,456,420.10	10,574,368.78	119,136,695.08
2020	1,205,000	1,341,687.50	2,546,687.50	3,575,000	3,197,406.26	6,772,406.26	1,385,000	303,500.00	1,688,500.00	123,660,320.10	10,564,868.78	124,103,045.08
2021	1,285,000	1,281,437.50	2,566,437.50	4,830,000	3,018,656.26	7,848,656.26	1,410,000	282,725.00	1,692,725.00	103,932,926.38	10,571,068.78	105,469,676.36
2022	1,360,000	1,217,187.50	2,577,187.50	5,920,000	2,777,156.26	8,697,156.26	1,435,000	258,050.00	1,693,050.00	100,396,101.38	10,571,468.78	102,792,026.36
2023	1,450,000	1,149,187.50	2,599,187.50	6,225,000	2,481,156.26	8,706,156.26	1,460,000	229,350.00	1,689,350.00	98,058,935.12	10,570,868.78	100,482,760.10
2024	1,535,000	1,076,687.50	2,611,687.50	4,220,000	2,169,906.26	6,389,906.26	1,490,000	200,150.00	1,690,150.00	101,812,715.10	8,914,618.78	103,589,840.08
2025	1,625,000	999,937.50	2,624,937.50	4,510,000	1,958,906.26	6,468,906.26	1,525,000	166,625.00	1,691,625.00	73,419,385.10	8,908,668.78	75,296,185.08
2026	1,720,000	918,687.50	2,638,687.50	5,475,000	1,733,406.26	7,208,406.26	1,565,000	128,500.00	1,693,500.00	68,355,871.38	8,913,918.78	70,982,546.36
2027	1,825,000	832,687.50	2,657,687.50	5,750,000	1,459,656.26	7,209,656.26	1,600,000	89,375.00	1,689,375.00	63,543,501.38	8,907,918.78	66,192,301.36
2028	1,930,000	741,437.50	2,671,437.50	6,035,000	1,172,156.26	7,207,156.26	1,650,000	45,375.00	1,695,375.00	59,756,687.62	8,910,418.78	62,420,237.60
2029	2,030,000	664,237.50	2,694,237.50	3,740,000	870,406.26	4,610,406.26				55,436,700.06	4,616,450.00	58,124,893.82
2030	2,125,000	583,037.50	2,708,037.50	3,895,000	720,806.26	4,615,806.26				51,049,387.56	4,616,875.00	53,756,356.32
2031	2,230,000	498,037.50	2,728,037.50	4,045,000	565,006.26	4,610,006.26				46,812,381.30	4,615,325.00	49,535,100.06
2032	2,315,000	431,137.50	2,746,137.50	4,170,000	443,656.26	4,613,656.26				41,471,906.30	4,617,825.00	44,213,875.06
2033	1,745,000	361,687.50	2,106,687.50	4,295,000	318,556.26	4,613,556.26				41,488,537.54	4,615,825.00	43,592,956.30
2034	1,815,000	309,337.50	2,124,337.50	1,130,000	189,706.26	1,319,706.26				35,979,278.76	1,324,075.00	38,099,247.52
2035	1,885,000	254,887.50	2,139,887.50	1,165,000	155,806.26	1,320,806.26				34,167,736.26	1,324,200.00	36,304,230.02
2036	1,965,000	198,337.50	2,163,337.50	1,200,000	119,400.00	1,319,400.00				33,768,292.50	1,321,950.00	35,929,080.00
2037	2,045,000	139,387.50	2,184,387.50	1,240,000	81,900.00	1,321,900.00				27,019,475.00	1,322,325.00	29,203,437.50
2038	450,000	75,481.26	525,481.26	1,280,000	41,600.00	1,321,600.00				24,235,237.50	1,325,087.50	24,757,231.26
2039	465,000	61,418.76	526,418.76							21,977,200.00		22,503,618.76
2040	480,000	46,887.50	526,887.50							21,680,600.00		22,207,487.50

DEBT SERVICE REQUIREMENTS ON THE SERIES AU BONDS AND THE PRIOR BONDS CONTINUED

	Series AU-1 Bonds			Series AU-2 Bonds			Series AU-3 Bonds			Prior Bonds		
	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total	Total Debt Service[1]	Refunded Bonds Debt Service	Net Total Debt Service
2041	490,000	31,887.50	521,887.50							15,186,650.00		15,708,537.50
2042	510,000	16,575.00	526,575.00							10,275,400.00		10,801,975.00
2043										7,229,000.00		7,229,000.00
2044										2,870,550.00		2,870,550.00
2045										871,900.00		871,900.00
2046										871,000.00		871,000.00
2047										873,750.00		873,750.00
2048										875,000.00		875,000.00
2049										874,750.00		874,750.00
2050										873,000.00		873,000.00
2051										874,750.00		874,750.00
2052										874,750.00		874,750.00
2053										873,000.00		873,000.00
2054										874,500.00		874,500.00
2055										504,000.00		504,000.00
	$36,625,000	$15,720,252.27	$52,345,252.27	$76,490,000.00	$29,356,994.19	$105,846,994.19	$15,145,000.00	$2,274,037.12	$17,419,037.12	$1,510,289,481.54	$136,012,494.08	$1,549,888,271.04

[1] Includes $9,720,000 of principal from the Series AL Bonds of the Authority that was internally defeased.

SOURCES OF AND SECURITY FOR PAYMENT OF THE SERIES AU BONDS

The Series AU Bonds are limited obligations of the Authority, payable solely from (i) payments received from the System under the Loan Agreement, and (ii) moneys held by the Trustee in funds established under the Indenture excepting, however, sinking or Indenture funds pledged to a specific series of Bonds.

Under the Loan Agreement, the System pledges its full faith and credit to the timely payment of the amounts payable and to the performance of the acts required of it thereunder. The Loan Agreement constitutes an unsecured general obligation of the System and does not limit the ability of the System to incur additional indebtedness. In accordance with the Loan Agreement, the System may pledge up to twenty percent (20%) of its tuition receipts and Commonwealth appropriations to secure any indebtedness it may incur or any guaranties it may undertake without providing similar pledges to the owners of the Series AU Bonds. As of the date hereof, no such pledge has been made by the System.

Additional Bonds

The Authority may issue Additional Bonds on parity with the Series AU Bonds (other than with respect to certain funds under the Indenture). In connection with the issuance of Additional Bonds, additional funds may be established under the Indenture for the benefit of such additional series. In such event, the holders of the Series AU Bonds will have no claims or right to any such funds. For a further description of the conditions under which such Additional Bonds may be issued, see **Appendix III: "Summary of Legal Documents: The Indenture -- Additional Bonds".**

No Recourse

All covenants, stipulations, promises, agreements and obligations of the Authority contained in the Indenture are deemed to be covenants, stipulations, promises, agreements and obligations of the Authority and not of any member, officer or employee of the Authority in his or her individual capacity, and no recourse shall be had for the payment of the principal or redemption price of or interest on the Series AU Bonds or for any claim based thereon or on the Indenture against any member, officer or employee of the Authority or any person executing the Series AU Bonds.

CERTAIN BONDHOLDERS' RISKS

Introduction

The Series AU Bonds constitute limited obligations of the Authority, payable solely from the payments to be made by the System pursuant to the Loan Agreement. Future revenues and expenses of the System are subject to change, and no assurance can be given that the System will be able to generate sufficient revenues to meet its obligations, including its obligations under the Loan Agreement.

The purchase of the Series AU Bonds involves numerous investment risks, some of which are referred to in this Official Statement. No representation is made that the risks described or referred to in this Official Statement constitute all of the risks associated with investing in the Series AU Bonds. Accordingly, prior to making a decision to invest in the Series AU Bonds, each prospective purchaser thereof should make an independent evaluation of all of the information presented in this Official Statement, including the Appendices, and should review other pertinent information. **The Authority has made no independent investigation of the extent to which any such factors may have an adverse effect on the revenues of the System.**

General

There are a number of factors affecting institutions of higher education, including the System, that could have an adverse effect on the System's financial position and its ability to make the payments required under the Loan Agreement, including the debt service payments on the Series AU Bonds. These factors include, but are not limited to, competition with other educational institutions; an economic downturn in the regions served by the System; changing demographics in the regions served by the System; declining enrollment; increasing costs of technology; the failure to increase (or a decrease in) the funds obtained by the System from other sources, including appropriations from governmental bodies; the impact at various times of modifications to federal student financial aid programs; and increasing costs of compliance with changes in federal or state regulatory laws or regulations. See **Appendix I: "Certain Information Concerning Pennsylvania's State System of Higher Education".** Appendix I should be read in its entirety.

Certain State Appropriations

A substantial portion of the System's operating revenues consists of appropriations made to the System by the Commonwealth of Pennsylvania. There is a risk that such Commonwealth appropriations may not continue at current levels as a percentage of the System's current unrestricted revenues which, in turn, may require greater than historic rates of tuition increases. See **Appendix I: "Certain Information Concerning Pennsylvania's State System of Higher Education - Commonwealth Appropriations"** for a discussion of such appropriations.

NCHEMS Report

Appendix I refers to a report released on July 21, 2017, by The National Center for Higher Education Management Systems (NCHEMS) which had been engaged by the Board of Governors to assist the System in addressing some of the issues referred to above ("NCHEMS Report"). The NCHEMS Report states in part, in its Executive Summary,

> The twin challenges of demographic decline and diminished state support confront the Pennsylvania State System of Higher Education with a bleak fiscal future. Several of its institutions are now in immediate crisis. If current trends continue, it is just a matter of time before all of the universities become financially unsustainable.

As set forth in Appendix I, the Board of Governors and the System is continuing to review and consider the NCHEMS Report to determine whether and, if so, how, any of the recommendations in the NCHEMS report should be implemented in the future. References herein to the NCHEMS Report should not be construed as an indication that the Board of Governors agrees with any or all of the statements, findings or recommendations contained therein. See **Appendix I – Certain Information Concerning Pennsylvania's State System of Higher Education – Strategic System Review".**

LEGALITY FOR INVESTMENT

Under the Act, the Series AU Bonds are designated securities in which all officers of the Commonwealth and its political subdivisions and municipal officers and administrative departments, boards and commissions of the Commonwealth, all banks, bankers, savings banks, trust companies, savings and loan associations, investment companies and other persons carrying on a banking business, all insurance companies, insurance associations and other persons carrying on an insurance business, and all administrators, executors, guardians, trustees and other fiduciaries, and all other persons whatsoever who are authorized to invest in bonds or other obligations of the Commonwealth, may properly and legally invest any funds, including capital belonging to them or within their control, and the Series AU Bonds are securities which properly and legally may be deposited with, and received by, any Commonwealth or municipal officers or agency of the Commonwealth for any purpose for which the deposit of bonds or other obligations of the Commonwealth is authorized by law.

NEGOTIABILITY

Under the Act, the Series AU Bonds have all the qualities of negotiable instruments under the law merchant and the laws of the Commonwealth relating to negotiable instruments.

TAX MATTERS

Federal – Series AU-1 Bonds and Series AU-2 Bonds

General. Co-Bond Counsel will deliver, concurrently with the issuance of the Series AU-1 Bonds and the Series AU-2 Bonds, their opinion to the effect that under existing statutes, regulations, rulings and court decisions, interest on the Series AU-1 Bonds and the Series AU-2 Bonds is excluded from gross income for federal income tax purposes under the Internal Revenue Code of 1986, as amended (the "Code"). Interest paid on the Series AU-1 Bonds and the Series AU-2 Bonds will not be a specific preference item for purposes of calculating individual or corporate alternative minimum taxable income; however, interest on the Series AU-1 Bonds and the Series AU-2 Bonds is included in adjusted current earnings for purposes of computing the alternative minimum tax imposed on corporations.

Original Issue Discount. Certain maturities of the Series AU-1 Bonds and the Series AU-2 Bonds have been offered at a discount ("original issue discount") equal, generally, to the difference between public offering price and principal amount. For federal income tax purposes, original issue discount on a Series AU-1 Bond or a Series AU-2 Bond accrues periodically over the term of the Bond as interest with the same tax exemption and alternative minimum tax status as regular interest. The accrual of original issue discount increases the holder's tax basis in the Series AU-1 Bond or the Series AU-2 Bond for determining taxable gain or loss from sale or from redemption prior to maturity. Prospective purchasers of the Series AU-1 Bonds and the Series AU-2 Bonds should consult their tax advisers for an explanation of the treatment of original issue discount.

Original Issue Premium. Certain maturities of the Series AU-1 Bonds and Series AU-2 Bonds have been offered at a premium ("original issue premium") over their principal amount. For federal income tax purposes, original issue premium is amortizable periodically to the call date that produces the lowest yield through reductions in the holder's tax basis for the Series AU-1 Bond or the Series AU-2 Bond for determining taxable gain or loss from sale or from redemption prior to maturity. Amortizable premium is accounted for as reducing the tax-exempt interest on the Series AU-1 Bond and Series AU-2 Bond rather than creating a deductible expense or loss. Prospective purchasers of the Series AU-1 Bonds and Series AU-2 Bonds should consult their tax advisers for an explanation of the treatment of original issue premium.

Code Requirements. The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Series AU-1 Bonds and the Series AU-2 Bonds. Ongoing requirements include, among other things, the provisions of Section 148 of the Code which prescribe yield and other limits within which the proceeds of the Series AU Bonds are to be invested and which may require that certain excess earnings on investments made with the proceeds of the Series AU-1 Bonds and the Series AU-2 Bonds be rebated on a periodic basis to the United States. The Authority and the System have made certain representations and undertaken certain agreements and covenants in the Indenture and in their tax compliance agreement to be delivered concurrently with the issuance of the Series AU-1 Bonds and the Series AU-2 Bonds designed to ensure compliance with the applicable provisions of the Code. The inaccuracy of these representations or the failure on the part of the Authority or the System to comply with such covenants and agreements could result in the interest on the Series AU-1 Bonds and the Series AU-2 Bonds being included in the gross income of a holder for federal income tax purposes, in certain cases retroactive to the date of original issuance of the Series AU-1 Bonds and the Series AU-2 Bonds.

Co-Bond Counsel's Assumptions. The opinion of Co-Bond Counsel assumes the accuracy of these representations and the future compliance by the Authority and the System with their covenants and agreements. Moreover, Co-Bond Counsel has not undertaken to evaluate, determine or inform any person, including any holder of Series AU-1 Bonds or Series AU-2 Bonds, whether any actions taken or not taken, events occurring or not occurring, or other matters that might come to the attention of Co-Bond Counsel would adversely affect the value of, or tax status of the interest on, the Series AU-1 Bonds and the Series AU-2 Bonds.

No Opinion as to Collateral Tax Consequences. Ownership of the Series AU-1 Bonds and the Series AU-2 Bonds may result in collateral federal tax consequences to certain taxpayers, including, without limitation, financial institutions, S corporations with excess net passive income, property and casualty insurance companies, individual recipients of social security or railroad retirement benefits and taxpayers who may be deemed to have incurred indebtedness to purchase or carry the Series AU-1 Bonds and the Series AU-2 Bonds. Co-Bond Counsel will express no opinion with respect to these or any other collateral tax consequences of the ownership of the Series AU-1 Bonds and the Series AU-2 Bonds. The nature and extent of the tax benefit to a taxpayer of ownership of the Series AU-1 Bonds and the Series AU-2 Bonds will generally depend upon the particular nature of such taxpayer or such taxpayer's own particular circumstances, including other items of income or deduction. Accordingly, prospective purchasers of the Series AU-1 Bonds and the Series AU-2 Bonds should consult their tax advisers.

Backup Withholding. As a result of the enactment of the Tax Increase Prevention and Reconciliation Act of 2005, interest on obligations such as the Series AU Bonds is subject to information reporting in a manner similar to interest paid on other investment obligations. Backup withholding may be imposed on payments made after March 31, 2007, to any bondholder who fails to provide certain required information including an accurate taxpayer identification number to any person required to collect such information pursuant to Section 6049 of the Code. The new reporting requirement does not in and of itself affect or alter the excludability of interest on the Series AU-1 Bonds and Series AU-2 Bonds from gross income for federal income tax purposes or any other federal tax consequence of purchasing, holding or selling obligations such as the Series AU Bonds.

Possible Adverse Effect of Changes in Law or Policy. There can be no assurance that currently existing or future legislative proposals by the United States Congress limiting or further qualifying the excludability of interest on tax-exempt bonds from gross income for federal tax purposes, or changes in federal tax policy generally, will not adversely affect the tax status of the interest on, or the market for, the Series AU-1 Bonds and the Series AU-2 Bonds.

Federal – Series AU-3 Bonds

In the opinion of Bond Counsel, under existing laws, regulations, rulings and judicial decisions, interest on the Series AU-3 Bonds is NOT EXCLUDABLE from gross income for federal income tax purposes under Section 103 of the Code. Interest on the Series AU-3 Bonds will be fully subject to federal income taxation. Thus, owners of the Series AU-3 Bonds generally must include interest on the Series AU-3 Bonds in gross income for federal income tax purposes.

To ensure compliance with Treasury Circular 230, holders of the Series AU-3 Bonds should be aware and are hereby put on notice that: (a) the discussion in this Official Statement with respect to U.S. federal income tax consequences of owning the Series AU-3 Bonds is not intended or written to be used, and cannot be used, by any taxpayer for the purpose of avoiding penalties that may be imposed on the taxpayer; (b) such discussion was written in connection with the promotion or marketing (within the meaning of Treasury Circular 230) of the transactions or matters addressed by such discussion; and (c) each taxpayer should seek advice based on its particular circumstances from an independent tax advisor.

Commonwealth of Pennsylvania

Co-Bond Counsel will also deliver an opinion to the effect that under existing law as enacted and construed on the date of such opinion, the Series AU Bonds are exempt from personal property taxes in the Commonwealth, and interest on the Series AU Bonds is exempt from the Commonwealth personal income tax and the Commonwealth corporate net income tax.

Attention is called to the fact, however, that any profits, gains or income derived from the sale, exchange or other disposition of the Series AU Bonds will be subject to Commonwealth taxes within the Commonwealth.

Other Jurisdictions

The Series AU Bonds and the interest thereon may be subject to state or local taxes in jurisdictions other than the Commonwealth under applicable state or local tax laws.

PROSPECTIVE PURCHASERS OF THE SERIES AU BONDS SHOULD CONSULT THEIR TAX ADVISERS WITH RESPECT TO THE FEDERAL, STATE AND LOCAL INCOME TAX CONSEQUENCES OF OWNERSHIP OF THE SERIES AU BONDS AND ANY CHANGES IN THE STATUS OF PENDING OR PROPOSED TAX LEGISLATION.

LEGAL MATTERS

Legal matters incident to the authorization, issuance and sale of the Bonds will be passed upon by Kutak Rock LLP and Turner Law, P.C., both of Philadelphia, Pennsylvania, Co-Bond Counsel. Certain legal matters will be passed upon for the Authority by its counsel, Barley Snyder LLP, Lancaster, Pennsylvania and for the System by its Chief Legal Counsel. The proposed form of opinion to be rendered by each of such firms in connection with the issuance of the Series AU Bonds is set forth in Appendix IV attached hereto.

RATINGS

Moody's Investors Service, Inc. ("Moody's") and Fitch Ratings ("Fitch") have assigned their municipal bond ratings of "Aa3" (negative outlook) and "AA-" (negative outlook), respectively, to the Series AU Bonds.

Any explanation of these ratings may be obtained only from the rating agencies issuing such ratings. Generally, rating agencies base their ratings on information and materials supplied to them and on their own investigations, studies and assumptions. There is no assurance that such ratings, once assigned, will remain for any given period of time or that they will not be lowered or withdrawn entirely by either rating agency concerned if in its judgment circumstances so warrant. Any such downward change or withdrawal of such ratings may have an adverse effect on the market price of the Series AU Bonds.

ABSENCE OF LITIGATION

There is no litigation of any nature pending or, to the Authority's knowledge, threatened against the Authority at the date of this Official Statement to restrain or enjoin the issuance, sale, execution or delivery of the Series AU Bonds, or in any way contesting or affecting the validity of the Series AU Bonds or any proceedings of the Board of the Authority taken with respect to the issuance or sale thereof, or the pledge or application of any moneys or the security provided for the payment of the Series AU Bonds or the existence or powers of the Authority or the performance of the Project.

CONTINUING DISCLOSURE

To assist the Underwriter in satisfying the requirements of Rule 15c2-12 (the "Rule") promulgated by the Securities and Exchange Commission, the System will enter into a Continuing Disclosure Agreement with The Bank of New York Mellon Trust Company, N.A., as dissemination agent (in such capacity, the "Dissemination Agent") for the benefit of owners of the Series AU Bonds. Pursuant to such agreement, the System will covenant to provide, through the Dissemination Agent, to the Electronic Municipal Market Access ("EMMA") system of the Municipal Securities Rulemaking Board (the "MSRB"), certain annual financial information and operating data of the nature included in the following sections of Appendix I to this Official Statement: Accreditation; Degrees Awarded; Enrollment; Application and Admissions; Tuition, Student Fees and Competition; Freshman Enrollment Composition; Student Financial Aid; Commonwealth Appropriations; Unrestricted Net Position; Faculty and Staff; and Outstanding Indebtedness. Audited financial statements of the System also will be provided to EMMA when available. The System will covenant to provide such information for a fiscal year within 150 days following the end of such fiscal year, commencing with the fiscal year ending June 30, 2017. The System will covenant to provide notice in a timely manner to EMMA of a failure of the System to provide the required annual financial information on or before the date specified in the Continuing Disclosure Agreement.

In the Continuing Disclosure Agreement, the System also will covenant to provide, within 10 business days, to EMMA notice of the occurrence of any of the following events with respect to the Series AU Bonds: (1) principal and interest payment delinquencies, (2) non-payment related defaults, if material, (3) unscheduled draws on debt service reserves reflecting financial difficulties, (4) unscheduled draws on credit enhancements reflecting financial difficulties, (5) substitution of credit or liquidity providers, or their failure to perform, (6) adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the Series AU Bonds, or other material events affecting the tax status of the Series AU Bonds, (7) modifications to rights of holders of the Series AU Bonds, if material, (8) Series AU Bond calls, if material, and tender offers, (9) defeasances, (10) release, substitution or sale of property securing repayment of the Series AU Bonds, if material, (11) rating changes, (12) bankruptcy, insolvency, receivership or similar event of the System, (13) the consummation of a merger, consolidation, or acquisition involving the System or the sale of all or substantially all of the assets of the System other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material, (14) appointment of a successor or additional trustee or the change of name of a trustee, if material, and (15) failure to provide annual information as required.

The System and the Dissemination Agent may amend the Continuing Disclosure Agreement, including amendments deemed necessary or appropriate in the judgment of the System (whether to reflect changes in the availability of information or in accounting standards or otherwise), and any provision of the Continuing Disclosure Agreement may be waived, provided that the following conditions are satisfied: (a) if the amendment or waiver relates to the undertakings of the System to provide annual financial information and notices, such amendment is made in connection with a change in circumstances that arises from a change in legal requirements, change in law or change in the identity, nature or status of the System or the type of business or operations conducted by the System; (b) the undertakings contained in the Continuing Disclosure Agreement, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Series AU Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and (c) the amendment either (i) is approved by the Holders of the Series AU Bonds in the same manner as provided in the Indenture for amendments to the Indenture with the consent of Holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Series AU Bonds, the Authority or the Dissemination Agent. The System's obligation to provide the foregoing annual financial information and notices of the specified events when material will terminate when the Series AU Bonds have been fully paid or legally defeased or at such other times as such information and notices (or any portion thereof) are no longer required to be provided by the Rule as it applies to the Series AU Bonds. Notice of such amendment will be provided to EMMA.

Under the Continuing Disclosure Agreement, the sole remedy for a breach or default by the System of its covenants to provide annual financial information and notices will be an action to compel specific performance. No action may be brought for monetary damages or otherwise under any circumstances. A breach or default under the Continuing Disclosure Agreement will not constitute an Event of Default under the Indenture or the Loan Agreement.

The Authority has no responsibility for the System's compliance with the Continuing Disclosure Agreement or for the contents of the financial information, operating data or notices provided thereunder or any omissions therefrom.

During the last five years, the System failed to file with EMMA, in a timely manner, certain Annual Financial Information in accordance with the Rule and as required under its previous continuing disclosure undertakings as follows. For the fiscal year ended June 30, 2016, 2015 and 2014, Annual Financial Information otherwise timely filed was not properly associated with certain CUSIPs associated with four series' of the System's prior bonds. The required filings were corrected on EMMA on or before September 1, 2017.

UNDERWRITING

The Series AU-1 Bonds are being purchased for reoffering by a group of banks and investment banking firms represented by Bank of America Merrill Lynch, as representative (collectively, the "Series AU-1 Underwriter"). The Series AU-1 Underwriter has agreed to purchase the Series AU-1 Bonds at an aggregate purchase price of $39,204,595.99.

The Series AU-2 Bonds are being purchased for reoffering by a group of banks and investment banking firms represented by Morgan Stanley & Co., LLC, as representative (the "Series AU-2

Underwriter"). The Series AU-2 Underwriter has agreed to purchase the Series AU-2 Bonds at an aggregate purchase price of $85,986,115.68.

The Series AU-3 Bonds are being purchased for reoffering by a group of banks and investment banking firms represented by J.P. Morgan Securities LLC, as representative (the "Series AU-3 Underwriter" and collectively with the Series AU-1 Underwriter and the Series AU-2 Underwriter, the "Underwriters"). The Series AU-3 Underwriter has agreed to purchase the Series AU-3 Bonds at an aggregate purchase price of $14,917,472.32.

Morgan Stanley & Co. LLC., an underwriter of the Series AU-2 Bonds, has entered into a distribution agreement with its affiliate, Morgan Stanley Smith Barney LLC. As part of the distribution arrangement, Morgan Stanley & Co. LLC may distribute municipal securities to retail investors through the financial advisor network of Morgan Stanley Smith Barney LLC. As part of this arrangement, Morgan Stanley & Co. LLC may compensate Morgan Stanley Smith Barney LLC for its selling efforts with respect to the Series AU-2 Bonds.

FINANCIAL ADVISOR

The System has retained RBC Capital Markets, LLC as its financial advisor in connection with the issuance of the Series AU Bonds. The receipt of a fee by RBC Capital Markets, LLC is contingent upon the issuance of the Series AU Bonds. The Financial Advisor is not obligated to undertake, and has not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness, or fairness of the information in this Official Statement.

The Financial Advisor may also receive a fee for conducting a competitive bidding process regarding the investment of certain proceeds of the Series AU Bonds.

MISCELLANEOUS

All of the summaries of the provisions of the Act, Act 188, the Indenture, the Loan Agreement and of the Series AU Bonds set forth herein are only outlines of certain provisions thereof and are qualified in all respect by reference to all of the particular provisions thereof, to which attention is hereby directed for further information, and do not purport to be complete statements of the provisions of any such document.

Information concerning the System has been provided by the Office of the Chancellor. All estimates, projections and assumptions herein have been made on the best information available and are believed to be reliable, but no representations whatsoever are made that such estimates, projections or assumptions are correct or will be realized. So far as any statements herein involve matters of opinion, whether or not expressly so stated, they are intended merely as such and not as representations of fact.

This Official Statement is not to be construed as a contract or agreement between the Authority or the System and the purchasers or owners of any of the Series AU Bonds. The information hereinabove set forth and that which follows should not be construed as constituting all of the conditions affecting the Authority, the System or the Series AU Bonds.

The distribution of this Official Statement has been duly authorized by the Authority and the System. The Authority has not assisted in the preparation of this Official Statement, except for the statements under the section captioned **"The Authority"** and **"Absence of Litigation"** herein and, except for those sections, the Authority is not responsible for any statements made in this Official Statement. Except for the execution and delivery of documents required to effect the issuance of the

Series AU Bonds, the Authority has not otherwise assisted in the public offer, sale or distribution of the Series AU Bonds. Accordingly, except as aforesaid, the Authority assumes no responsibility for the disclosures set forth in this Official Statement.

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PENNSYLVANIA HIGHER EDUCATIONAL
FACILITIES AUTHORITY

By: /s/Robert Baccon
Robert Baccon
Executive Director

Approved:

STATE SYSTEM OF HIGHER EDUCATION

By: /s/James S. Dillon
James S. Dillon
Vice Chancellor for Administration and Finance

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Appendix I

Certain Information Concerning Pennsylvania's State System of Higher Education

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PENNSYLVANIA'S STATE SYSTEM OF HIGHER EDUCATION

History and Philosophy of the System

Pennsylvania's State System of Higher Education (the "System") is a body corporate and politic constituting a public corporation and a governmental instrumentality of the Commonwealth of Pennsylvania, created by the State System of Higher Education Act of November 12, 1982, P.L. 660, No. 188, as amended ("Act 188").

Act 188 established a Board of Governors and the Office of the Chancellor and awarded university status to the 13 state-owned colleges on July 1, 1983. (Indiana University of Pennsylvania was awarded university status prior to the enactment of Act 188.) On that date, the System, composed of the 14 state-owned universities in the Commonwealth and the Office of the Chancellor, embarked upon its primary mission to provide "instruction for undergraduate and graduate students to and beyond the master's degree in the liberal arts and sciences, and in the applied fields, including the teaching profession." The System universities are herein referred to individually as a "University" or a "System University" and collectively as the "Universities" or "System Universities." The Universities also have specific missions in business, human services, public administration, and technology. The 14 System Universities include:

Bloomsburg University of Pennsylvania
California University of Pennsylvania
Cheyney University of Pennsylvania
Clarion University of Pennsylvania
East Stroudsburg University of Pennsylvania
Edinboro University of Pennsylvania
Indiana University of Pennsylvania
Kutztown University of Pennsylvania
Lock Haven University of Pennsylvania
Mansfield University of Pennsylvania
Millersville University of Pennsylvania
Shippensburg University of Pennsylvania
Slippery Rock University of Pennsylvania
West Chester University of Pennsylvania

Bound together by the mission and by the mandate set forth in Act 188, the Universities strive to provide the highest quality education feasible for their students at the lowest possible cost.

The history of each University evolved from a need to train teachers for the Commonwealth's secondary educational institutions and to elevate the accepted standards of education. The Commonwealth adopted the Normal School Act on May 20, 1857, which provided the standards by which teachers for the Commonwealth's Normal Schools were to be trained. During the 25 years following passage of the Normal School Act, all of the schools that now comprise the System were privately established and were recognized as State Normal Schools.

On September 22, 1921, the Commonwealth enacted legislation for the acquisition of 13 State Normal Schools, adding the 14th State Normal School in 1922. These schools subsequently were redesignated as State Teachers' Colleges in 1929 (the "State Colleges"). The responsibility for certifying teachers then was transferred from the county superintendents to the Commonwealth. Within ten years following this transfer of responsibility, teacher certification requirements changed from a two-year certificate program to a four-year college degree program.

In 1959, the State Teachers' Colleges were redesignated State Colleges and, in 1961, legislation was enacted to allow the State Colleges to offer a wider range of educational opportunities. (See "Degrees Awarded" herein.) Graduate programs soon were approved and instituted at many of the State Colleges. Indiana State College achieved university status in 1965, and the remaining 13 State Colleges were recognized as universities in 1983 with the enactment of Act 188. Each University, with its unique geography and array of academic offerings, serves as a cultural center for its surrounding community.

Additionally, eight of the Universities are involved with the operation of the Chincoteague Bay Field Station of the Marine Science Consortium, a nonprofit educational 501(c)(3) corporation located in Wallops Island, Virginia (the "Consortium"), committed to excellence in education and research in the marine and environmental sciences. The Consortium was founded by eight of the Universities in 1970 and maintains marine stations where both field and laboratory investigations of coastal ecosystems are conducted under the supervision of University faculty and qualified marine education instructors. The Consortium supports precollege, college, and Elder Hostel programs.

The Board of Governors

The System is governed and guided by a Board of Governors (the "Board") composed of 20 members: the Governor of Pennsylvania (or designee), the Secretary of Education (or designee), one senator appointed by the President Pro Tempore of the Senate, one senator appointed by the minority leader of the Senate, one representative appointed by the Speaker of the House of Representatives, one representative appointed by the minority leader of the House of Representatives, and 14 members who are appointed by the Governor of Pennsylvania and confirmed by the Senate. The Board has the authority to exercise all sanctioned corporate powers in the administration of its overall responsibility to plan and to coordinate the development of the System. Members of the Board appointed from the General Assembly serve a term of office concurrent with their respective elective terms as members of the General Assembly with the Governor and Secretary of Education (or their respective designees), serving so long as they continue in office. Eleven members of the Board, appointed by the Governor, customarily will serve four-year appointments, at which time a reappointment for an additional four-year term may be commissioned. Three of the members of the Board, appointed by the Governor, must be undergraduate students presently attending a System University. The student members are selected from the presidents of the local campus student government associations or their local equivalents, and their terms automatically expire upon graduation or separation from the System. Five members of the Board also must hold membership in one of the local councils of trustees serving the Universities with no more than one trustee representing a University. The Board annually elects a chair, and at present there are two vice chairs. Members of the Board receive no compensation for their services; however, all expenses incurred in the performance of their duties may be reimbursed by the System.

The Governor of Pennsylvania and the Secretary of Education, or their designees, as members of the Board are entitled to attend all of the scheduled meetings, to address matters of concern before the Board, and to vote. However, they cannot be elected as officers of the Board.

The Chancellor of the System (the "Chancellor") serves the Board as the chief executive officer of the System. The Chancellor has the authority to address any matters of discussion before the Board but does not have voting privileges.

Act 188 requires that the Board conduct a public meeting quarterly; however, additional meetings may be convened by the chair or upon the request of six members of the Board. Presently, the Board convenes quarterly. The Office of the Chancellor has the responsibility of presenting an agenda to the Board for action at each scheduled meeting. Eleven members of the Board attending any meeting of the Board constitute a quorum.

In accordance with Act 188, the Board has "overall responsibility for planning and coordinating the development and operation of the System." To this end, the Board employs the Chancellor as the chief executive officer of the System. The Board must approve the Chancellor's salary and delineate any duties and responsibilities beyond those prescribed in Act 188.

The president of each University is appointed by the Board originally for a fixed term from a list of qualified candidates submitted by the Chancellor to the Board. Performance evaluations are used to evaluate the services of each president before the term of such president's appointment can be extended.

Through the Chancellor and the 14 presidents of the Universities, the Board administers broad fiscal, personnel, and educational policies and establishes general policies that will be beneficial to the System in attaining its goal to offer an education of high quality to all its students.

The Board approves the annual operating and capital budgets for the System. The Board's request for operating and capital appropriations is submitted to the State Board of Education for comment. As required by statute, the Board then submits its request for operating and capital appropriations to the Governor not later than November 1 of the fiscal year preceding the fiscal year for which the appropriations are requested. The Board independently submits its request for operating and capital appropriations to the General Assembly. When required, the Board or its Chancellor must represent the System before the General Assembly, the Governor of Pennsylvania, and the State Board of Education.

Under Act 188, the Board fixes the levels of tuition fees across the System, including the allowance for a differential between students who are residents of the Commonwealth and those who are nonresidents. The Board has approved a tuition/fee flexibility pilot program that allows for higher or lower tuition and fees based on local market forces.

There are five standing committees which make policy recommendations to the full Board: Academic and Student Affairs; Audit; Executive; Finance, Administration, and Facilities; and Human Resources. The present bylaws provide that members of the Board may attend and participate in the meetings of any of the committees; however, only committee members may vote on an issue under consideration.

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Board of Governors

Cynthia D. Shapira, *Chair*
President
David S. and Karen A. Shapira Foundation
Pittsburgh, PA

Ryan P. Aument
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Senate of Pennsylvania
Harrisburg, PA

Matthew E. Baker
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Pennsylvania House of Representatives
Harrisburg, PA

Audrey F. Bronson
Trustee at Cheyney University of Pennsylvania
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Shaina Marie Hilsey
Student
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State Policy Advisor
Dominion Resources Inc.
Coraopolis, PA

Jonathan B. Mack
Attorney and Partner
Marcus & Mack, P.C.
Indiana, PA

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Of Counsel
Chimicles & Tikellis, LLP
Haverford, PA

Barbara McIlvaine Smith
West Chester, PA

Daniel P. Meuser
Former Secretary of Revenue
Pennsylvania Department of Revenue
Shavertown, PA

Thomas S. Muller
County Executive
Lehigh County
Lower Macungie, PA

Guido M. Pichini
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Security Guards, Inc.
Wyomissing, PA

Pedro A. Rivera
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Pennsylvania Department of Education
Harrisburg, PA

Judith L. Schwank
Member
Senate of Pennsylvania
Harrisburg, PA

Harold C. Shields, *Vice Chair*
Principal
Harold C. Shields HR Consulting, LLC
Allison Park, PA

Brian Swatt
Student
Indiana, PA

Tom Wolf
Governor
Commonwealth of Pennsylvania
Harrisburg, PA

(2 Vacancies)

Office of the Chancellor

Act 188 stipulates that the Chancellor "shall be responsible for the administration of the System under policies prescribed by the Board." As the chief executive officer of the System, the Chancellor advises the Board on budgetary matters, academic program matters, and the formulation of personnel administration policies and procedures. In order to explore and control all of the important daily endeavors of the System, the Chancellor is empowered to employ a central office staff to fulfill the mandates of both Act 188 and the Board. Under the Chancellor's direction, the presidents, line officers, and support staff provide System-wide management in such areas as academic policy, planning, business affairs, faculty and staff affairs, legislative policy, institutional research, legal affairs, capital planning, System relations, advancement, and equal educational opportunities. The Chancellor assists the Board in its appointment of the presidents by submitting to the Board, with his recommendation, the names of individuals recommended for consideration by the councils of trustees. Upon the appointment of each president, an annual evaluation process must be conducted, the results of which are reviewed thoroughly by the Board.

Frank T. Brogan (Retiring 09/01/17)
Chancellor

Mr. Frank T. Brogan became the fourth chancellor of Pennsylvania's State System of Higher Education on October 1, 2013. A lifelong educator, Mr. Brogan previously served as chancellor of the State University System of Florida, was president of Florida Atlantic University, and was twice elected lieutenant governor of the state of Florida. Mr. Brogan began his academic career as a teacher at Port Salerno Elementary School in Martin County, Florida. After working his way up through the Martin County School System, including serving six years as superintendent, he was elected Florida's Commissioner of Education in 1995. He continued his advocacy of education issues as lieutenant governor, steering education policy as legislative liaison for then Governor Jeb Bush. In 2003, he assumed the presidency of Florida Atlantic University. He helped raise more than $120 million in private funds and matching grants for the university, while increasing its focus on research and establishing a four-year medical education program. Mr. Brogan was named chancellor of the State University System of Florida in 2009. As chancellor, he led the development of a new strategic plan that included 39 distinct benchmarks—an integral part of Florida's nationally recognized accountability framework that tracks progress of university and system goals. Mr. Brogan holds a bachelor's degree in education (magna cum laude) from the University of Cincinnati and a master's degree in education from Florida Atlantic University.

The Office of the Chancellor operates with two vice chancellors—an executive vice chancellor and chief academic officer, and a vice chancellor for administration and finance—and a chief of staff. The two vice chancellors and chief of staff serve the System in an important capacity, individually and collectively, and work together to ensure that the academic programs offered on all of the campuses best suit the needs of the public.

Peter H. Garland (Acting Chancellor, until 09/11/17)
Executive Vice Chancellor and Chief Academic Officer

The executive vice chancellor is the System's chief operating officer, overseeing the major functional areas in the Office of the Chancellor; serving as liaison to University presidents and the System's Board of Governors; and leading major System-wide projects, programs, and initiatives. The chief academic officer is responsible for promoting the System's academic mission including the development of new academic directions for the System, thorough program evaluation, and program review. Dr. Garland is responsible for negotiating and administering all collective bargaining agreements covering approximately 11,000 unionized employees of the Office of the Chancellor and the 14 System Universities. He also provides centralized grievance and arbitration services.

Dr. Garland serves as executive vice chancellor, a position to which he was appointed in October 2006, and assumed chief academic officer responsibilities in February 2014. He served as the System's acting chancellor from March 1, 2013, to September 30, 2013. Dr. Garland previously joined the System as executive associate to the chancellor in January 2002 and was named vice chancellor for academic and student affairs in December 2003. Prior to joining the System, Dr. Garland had served as executive director of the State Board of Education since 1993. He also served as assistant commissioner for postsecondary and higher education for the Pennsylvania Department of Education, acting commissioner/deputy secretary for postsecondary and higher education, director of the bureau of postsecondary services, executive assistant to the commissioner for higher education, and senior program analyst in the Office of Higher Education Financing. Dr. Garland holds bachelor's degrees in English and psychology, a master's degree in educational administration from The College of William and Mary, a master's degree in political science, and a doctoral degree in higher education from Penn State. He has numerous publications to his credit and has reviewed articles for the Association for the Study of Higher Education and the American Educational Research Association. He serves as Lecturer in the Graduate School of Education at the University of Pennsylvania.

Karen M. Whitney (Interim Chancellor, effective 09/12/17)
President, Clarion University of Pennsylvania

Dr. Whitney, who began her tenure as president of Clarion University in July 2010, will serve as interim chancellor following Chancellor Frank T. Brogan's retirement from the System next month. Dr. Whitney recently completed a three-year term as chair of the presidents' council for the 14 State System universities and is the longest currently serving president in the System. Dr. Whitney previously was vice chancellor for student life and diversity and dean of students at Indiana University Purdue University Indianapolis (IUPUI) and assistant and associate vice president for student life and director of resident life at the University of Texas at San Antonio. She earned a bachelor's degree in psychology and a master's degree in public administration, both from the University of Houston, and a Ph.D. in higher educational administration from the University of Texas at Austin. She held numerous positions in the area of residence life at the University of Houston. Dr. Whitney also served as an adjunct assistant professor and instructor in the School of Education at Indiana University and taught various courses at both the University of Texas at San Antonio and the University of Houston.

A national search will be conducted to fill the Chancellor position.

James S. Dillon
Vice Chancellor for Administration and Finance

The vice chancellor for administration and finance is charged with leading the administration and management of the financial and administrative affairs of the System. He renders guidance in the development of policy and business procedures to be implemented by the Chancellor and by the Board. Such policy issues include accounting and financial policy and reporting; treasury operations including cash management, commercial banking, and investment programs; capital financing and planning; emergency management; physical plant planning; security management; insurance management; annual System budget development and management; and procurement management. This position also provides leadership for and works in partnership with Universities to establish, implement, and improve human resources management policies and practices for the System.

Mr. Dillon was appointed vice chancellor for administration and finance in June 2005. He joined the System in 1989 as cash and debt manager, was appointed director of cash and debt management in 1995, and was named treasurer in 1997. For five years prior to joining the System, Mr. Dillon held several finance positions at The Equitable in New York, including manager in the Office of the Treasurer. Mr. Dillon holds a bachelor of science in business administration from Shippensburg University and a master of business administration, corporate finance, from Fordham University. He also participated in the Program for Senior Executives in State and Local Government sponsored by Harvard University, John F. Kennedy School of Government. Mr. Dillon has presented case studies at the National Multi-Housing Developers Association Conference and the Annual Treasury Management Conference of the Treasury Management Association.

Randy A. Goin, Jr.
Chief of Staff

The chief of staff and senior policy advisor coordinates the efforts of senior staff in the Office of the Chancellor and works closely with university, government, and business leaders to ensure timely advancement of Board of Governors' initiatives.

Mr. Goin was appointed chief of staff in December 2013. Prior to joining the System's leadership team, Mr. Goin was chief of staff for the Florida Board of Governors, which oversees the second largest university system in America. He also led the public affairs, governmental relations, and communications group, which worked to articulate a clear message and vision with all constituents. He launched his career in the private sector more than two decades ago and later moved into communications management roles in higher education. He ultimately served as associate vice president for marketing at Florida Atlantic University, where he helped build the communications organization and reposition the institution's brand. Mr. Goin was then named university chief of staff and worked closely with the president to reshape the institution's organizational structure by increasing focus on top priorities. He served as a conduit between the administration and the university trustees—enhancing board relations and operations. He earned a bachelor of architecture degree and a master's of arts degree with a focus in corporate and political communication from Florida Atlantic University.

The Presidents of the Universities

The presidents of the 14 Universities are appointed by the Board for a specified term. In an effort to ensure that the presidents are guiding the individual Universities toward the achievement of the System's unified goals, the Chancellor reviews the goals and objectives of each president annually. As the chief executive officers of the Universities, the presidents are responsible for development and implementation of policies and procedures regarding personnel administration, fiscal management, admissions, discipline and expulsion guidelines, instructional programs, research programs, and public service programs within the framework prescribed by the Board.

The presidents must ensure that prudent fiscal policies are followed in the expenditure of all Commonwealth appropriations, tuition, fees, and all other available funds. They have the authority to obligate the System for ongoing contractual liabilities within the limitations of the operating budget of the University. Overall, their primary responsibility is to implement the policies of the Board and to perform all of those operations necessary for the orderly and judicious management of the University. Each president may attend any scheduled meeting of the University's council of trustees and address matters before such council, but may not vote.

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The 14 University presidents are listed below.

Dr. Bashar W. Hanna (Effective 07/07/17)
Bloomsburg University of Pennsylvania

Ms. Geraldine M. Jones
California University of Pennsylvania

Mr. Aaron A. Walton (Interim, effective 05/31/17)
Cheyney University of Pennsylvania

Dr. Karen M. Whitney (Retiring 06/30/18)
Clarion University of Pennsylvania

Dr. Marcia G. Welsh
East Stroudsburg University of Pennsylvania

Dr. H. Fred Walker
Edinboro University of Pennsylvania

Dr. Michael A. Driscoll
Indiana University of Pennsylvania

Dr. Kenneth S. Hawkinson
Kutztown University of Pennsylvania

Dr. Michael Fiorentino, Jr.
Lock Haven University of Pennsylvania

Mr. Scott W.H. Barton (Interim, effective 08/19/17)
Mansfield University of Pennsylvania

Dr. John M. Anderson (Retiring 03/01/18)
Millersville University of Pennsylvania

Dr. Laurie A. Carter (Effective 08/07/17)
Shippensburg University of Pennsylvania

Mr. Philip K. Way (Interim, effective 07/21/17)
Slippery Rock University of Pennsylvania

Dr. Christopher M. Fiorentino
West Chester University of Pennsylvania

The Councils of Trustees

Each University within the System maintains a council of trustees consisting of 11 members who are appointed by the Governor with the advice and consent of the Senate. At least two of these members must be alumni of the institution. Ten of the members serve terms of six years while one member must be a full-time undergraduate student, other than a freshman, enrolled for at least 12 semester hours at the institution of which he/she is a trustee. The student member serves a term of three years or for so long as he/she is a full-time undergraduate student in good academic standing, whichever period is shorter. Six members of a council constitute a quorum, and each council meets at least quarterly and additionally at the call of the president, or its chair, or upon the request of three of its members.

Each council's specific responsibilities include making recommendations to the Chancellor for the appointment, retention, or dismissal of the president of its University following consultation with students, faculty, and alumni; reviewing and approving the recommendations of the president as to the standards for admission, discipline, and expulsion of students; and reviewing and approving the recommendations of the president as to the policies and procedures governing the use of institutional facilities and property, and the policies and procedures for the annual operating and capital budget requirements for submission to the Board. The council has the authority to approve schools and academic programs; to review and approve charges for room, board, and miscellaneous fees; to review and approve all contracts and purchases negotiated or awarded by the president, with or without competitive bidding, and all contracts for consulting services entered into by the president; and to take such action as may be necessary to effectuate the powers and duties delegated by Act 188.

Capital Facilities

The campuses of the 14 Universities encompass more than 4,700 acres. To date, there are almost 900 physical plant structures, with 32.6 million gross square feet. Capital facilities in place prior to the System's inception in 1983, state-appropriated capital renovations of those facilities, and new state-appropriated capital facilities are made available to the System at no cost. In 2002, the Commonwealth transferred custody and control of these facilities to the System. Under this arrangement, the Commonwealth retains fee title for the facilities and continues to provide state appropriations for capital facilities construction and renovations. Capital facilities acquired and constructed after 1983 by the System from other than state appropriations, as well as capitalized renovations and capital assets, such as equipment, furnishings, and library books, are assets on the System's balance sheet and have a book value, as of June 30, 2016, of $1.7 billion net of accumulated depreciation. The current replacement cost of the total System capital facilities and infrastructure is estimated to be in excess of $10 billion.

Educational and General Facilities—The Commonwealth appropriates funds for capital repairs and renovations while the System contributes regular maintenance funded from its operating budget. In July 1996, the Board of Governors approved a facilities renovation partnership with the Commonwealth of Pennsylvania. Currently, the Commonwealth is providing approximately $65 million annually toward capital improvement for the System's academic facilities. The System contributes any additional funding for capital repairs and renovations needed through bond financing, operating funds, or fundraising. The System has expended approximately $1.9 billion for renovation of existing academic facilities since 1996, while the Commonwealth has appropriated approximately $1.7 billion.

Each University's capital budget request for the forthcoming fiscal year is submitted to the Office of the Chancellor. In order for a capital project to be included in the appropriations request to the Governor and to the General Assembly, the Office of the Chancellor assesses the project's priority using criteria that include: University priorities; academic benefit; space requirements; ADA, safety, and code compliance deficiencies; new revenue or matching funds potential; cost savings potential; and impact on deferred maintenance. The equitable distribution of capital funds to each of the Universities is also considered in developing the plan. The Office of the Chancellor conducts an in-depth review of each capital project request to determine the overall contribution of the project to the well-being of the System as a whole.

Auxiliary Facilities—The Board of Governors has determined that additional facilities may be needed at the Universities and has adopted a Construction Finance Policy, which permits the System to seek bond funding to finance construction of new auxiliary facilities such as residence halls, recreation centers, student unions, and such other facilities, equipment, real property, or other needs as the Board decides. Auxiliary facilities are sustained with student fees, not Commonwealth appropriations or tuition. Act 188 requires the maintenance of an Auxiliary Facilities Reserve Fund established from mandatory resident student fees to accumulate funds with which to repair or construct new residence halls. To ensure longevity of existing residence halls, a capital renewal fee is charged per resident student for use in implementing capital maintenance projects. The monies collected are restricted for the specific purpose of roof replacement, floor replacement, or any major repair/replacement project that will significantly prolong the usable life of the building for use as a residence hall. The System has expended over $1.5 billion for auxiliary facilities since 1996.

Accreditation

All of the Universities are fully accredited by the Middle States Association of Colleges and Secondary Schools (Middle States). In November 2015, Cheyney University was placed under probation because of insufficient evidence that the institution is currently in compliance with Standard 3 (Institutional Resources). Recently, Middle States has required the university to show cause, by September 1, 2017, as to why its accreditation should not be withdrawn.

Compliance by the University with the September 1, 2017 date may not be solely dispositive of the University's accreditation and the University and Middle States are expected to go through a number of steps over the upcoming year before a final determination will be made. The University remains accredited while on show-cause status. Interested investors can obtain more information by contacting the Middles States Association of Colleges and Secondary Schools. Certain academic programs are accredited individually by various other national professional organizations.

To maintain Middle States accreditation, Cheyney University has undertaken many steps to address the out-of-compliance status of multiple standards. The University is undertaking an overhaul of the academic enterprise, right sizing the staff and administration, and concentrating operations into fewer buildings. Cheyney University has already insourced business operations to West Chester University, and has outsourced grounds, janitorial, IT services, HVAC, and financial aid. To be in compliance with Middle States' request, Cheyney must submit a plan to mitigate the debt owed to other State System universities through repayment, state appropriations, forgiveness, or any other source of funds. To that end, the University proposes to work toward full loan forgiveness by the State System over a four fiscal year basis, beginning in the current fiscal year 2017/18, based on the following:

- FY 2017/18: Cheyney University demonstrates $7.5 million of annual expense reduction from current operations as verified by the Vice Chancellor for Administration and Finance = 0% forgiven.
- FY 2018/19: Cheyney University maintains a balanced budget of revenues greater or equal to annual expenses = 33.4% of amount outstanding forgiven.
- FY 2019/20: Cheyney University maintains a balanced budget of revenues greater or equal to annual expenses = 50% of amount outstanding forgiven.
- FY 2020/21: Cheyney University maintains a balanced budget of revenues greater or equal to annual expenses = Remainder of outstanding balance forgiven.

This plan should alleviate a considerable component of the out-of-compliance finding for the Middle States financial resources standard, and will result in the forgiveness of all funds lent to or spent on behalf of Cheyney University ($30.5 million State System Loans and $3.9 million from the Office of the Chancellor spent directly on behalf of Cheyney). Failure to meet these requirements during the four fiscal year term will render any and all outstanding amounts due and payable.

Degrees Awarded

A range of undergraduate and graduate degree programs is offered across the System; 190 undergraduate and 123 graduate programs are offered in 30 major academic areas. In addition, certification programs are offered in 144 areas. The System awarded 19,397 undergraduate degrees and 5,075 master's degrees in 2015/16. The System also awarded 186 doctoral degrees through Bloomsburg, Indiana, and Slippery Rock Universities of Pennsylvania and 345 associate's degrees through all the Universities. Education comprised 12.7 percent of the undergraduate degrees and 35.9 percent of the graduate degrees conferred.

Initiatives in Technology

By law and by history, System Universities share a mission of instruction, research, and public service, and through their existing infrastructure and human resources, have the objective of assisting the Commonwealth to achieve statewide goals and to support special programs. Directly and indirectly, these programs benefit students, families, faculty, local communities, professional organizations, government agencies, and the general public. Many programs are provided in partnership with public schools, service agencies, business and industry, other universities, and local to international government bodies.

The System operates a consolidated Enterprise Resource Planning (ERP) system for each University's finance, procurement, human resources, and payroll processes in a single, hosted solution managed from one location. Student administration functional processes, such as admissions, registration, financial aid, and student billing and accounting, are maintained at each University with interfaces to the ERP system as necessary. The State System's Strategic Information Management System (SIMS) has seen much progress this year, with the first module, SIMS v1.0 Student Enrollment, ready to go live this August. SIMS is an Enterprise Data Warehouse that transforms data from the 14 Universities and, when appropriate, combines it with external data to produce a strategic, dynamic, and evolving single statewide higher education source. SIMS is a multiyear endeavor being developed and delivered by modules. While student enrollment is the first module undertaken, it will be followed by course, admissions, financial aid, retention, completions, alumni, student accounts, and external data modules. Ultimately, SIMS will be a modern information delivery platform that will enable efficient and timely decision support, predictive analytics, and data mining. It will support the production of educational intelligence for the 14 Universities and the State System.

The System and its Universities systematically have expanded the technological infrastructure and services provided through networked resources. Following are some highlights of these efforts.

Through the use of technology, the Universities are sharing courses—allowing students not only to take classes that might not otherwise be available at their University, but also to benefit from the expertise of extraordinary faculty at other institutions across the System. The expansion of online courses and programs has created even more opportunities for both traditional students—those who enroll in college right out of high school—and adult learners, many of whom would not be able to take the time away from job and family commitments to take a "regular" class at a campus that might be located literally hundreds of miles away. More than 49,567 System University students took at least one of their courses online during the 2015/16 academic year, earning more than 108,852 online credits. The System Universities now offer more than 179 online certificate and degree programs. During the 2015/16 academic year winter and summer breaks, the Universities offered a combined 2,177 online courses, providing students significant opportunities to stay on track toward graduation or even to get ahead in earning their degree.

The System maintains a wide area network, or SSHEnet, to provide connectivity between the Universities, to coordinate delivery of both commodity Internet and Internet2, and to facilitate resource sharing between System Universities and the Office of the Chancellor. SSHEnet is the main throughway for mission-critical services, such as distance education (university to/from Desire2Learn); student, faculty, and staff access to the Keystone Library Network; access to the Shared Administrative System for finance, procurement, and human resources/payroll processing; access to the Business Warehouse for web-based reporting and analysis templates; access to the enterprise portal for Employee Self-Service (ESS) and Manager Self-Service (MSS); and System-wide videoconferencing capabilities used by faculty and staff. The model of aggregating wide area network services provides the opportunity to leverage best pricing from Internet Service Providers and point-to-point service providers. The ongoing operational costs are also reduced significantly by having a few highly skilled staff of network and video engineers to support the State System Universities and the Office of the Chancellor. In 2014, SSHEnet was transformed to take advantage of connectivity provided by the Keystone Initiative for Network Based Education and Research (KINBER). KINBER supports the Pennsylvania Research and Education Network (PennREN) that was built using funding from a federal broadband grant of almost $100 million to build an education and research network connecting nearly 70 anchor sites and over 1,700 miles of fiber-optic cable. The System was a named participant in preparing the federal grant request. SSHEnet is architected to provide full redundancy that will allow System students, faculty, and staff the connectivity required in today's connected/cyber society.

The System uses several license agreements to provide quality software for students and faculty. Several third-party applications are used in conjunction with the online learning environment to enhance and expand the resources available. These applications include real-time videoconference and presentation resources, antiplagiarism resources, social networking resources, and others. Independent of the online learning environment, students and faculty have access to leading resources specific to mathematics, physics, geography, geology, business, and other disciplines. The System utilizes a Microsoft Campus Agreement that covers all Universities and the Dixon University Center. The agreement provides license coverage for Windows operating systems, the latest releases of Microsoft Office, and several other applications including Windows server, Exchange, and SharePoint, and extends licensing to all University-owned personal computers and work-at-home rights for all employees.

The System and its Universities use the power and potential of existing and emerging technologies to provide a high-quality education to its students and state-of-the-art services to students, faculty, and staff while continuously improving efficiency and lowering the total cost of education to students, their families, and the Commonwealth. Recognizing that the educational landscape is changing rapidly, the System intends to leverage the opportunities presented by emerging technologies to become more flexible in its operations, to remain agile in the face of new demands for content and delivery modes, and to enhance its understanding and responsiveness to the needs of the communities it serves, the Commonwealth, and the nation.

Accountability

The Board of Governors' commitment to accountability and excellence has included a performance funding program that was established in July 2000. This program measures and rewards University performance in key areas of student achievement, University excellence, diversity, and operational efficiency. The Board of Governors has increased the amount of performance funding available to the Universities from $2 million in the first year of the program to the current level of $39 million. The State System's focus on performance has produced results. Since the performance funding program began, student persistence and graduation rates (both four-year and six-year) have increased; the student and faculty populations have become more diverse—minority enrollment this fall reached another record high, now accounting for 17.24 percent of the student population; more community college students are transferring to System Universities; and more academic and professional programs are being accredited by national organizations—a sign of improved academic quality.

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Enrollment

The following data shows the System's fall semester enrollment by headcount and annual full-time equivalent enrollment for the last five academic years.

	2012/13	2013/14	2014/15	2015/16	2016/17
Headcount					
Undergraduate	100,350	98,396	95,804	92,818	89,802
Graduate	14,121	13,632	13,802	14,308	14,977
Total	114,471	112,028	109,606	107,126	104,779
Full-Time	97,823	95,494	92,788	89,845	86,905
Part-Time	16,648	16,534	16,818	17,281	17,874
Total	114,471	112,028	109,606	107,126	104,779
Full-Time Equivalent					
Undergraduate	94,213	92,457	89,478	86,622	83,611
Graduate	8,210	7,801	7,916	8,207	8,606
Total	102,423	100,258	97,394	94,829	92,217

The general economic environment and declining numbers of high school graduates in Pennsylvania are contributing factors in declining enrollment.

Applications and Admissions

The following data shows the fall semester application/enrollment figures for the System for five academic years, including the current year.

	2012/13	2013/14	2014/15	2015/16	2016/17
Applied	93,084	77,826*	78,878	79,468	79,426
Accepted	61,247	60,862	62,312	63,965	63,606
Enrolled	20,084	19,941	19,719	18,913	18,137
% Accepted	65.8%	78.2%	79.0%	80.5%	80.1%
% Enrolled/Accepted	32.8%	32.8%	31.6%	29.6%	28.6%

*The lower number of applications reported by System institutions beginning in FY 2013/14 is largely a result of a change implemented by the System in the method of collecting application information from the individual Universities.

The prior method of collecting application information may have overstated completed applications in prior years.

Tuition, Student Fees, and Competition

The following includes the current and previous four years of System-wide average in-state full-time undergraduate tuition and fees.

Full-Time Undergraduate Tuition and Student Fees

	2012/13	2013/14	2014/15	2015/16	2016/17
System Average	$8,733	$9,004	$9,418	$9,766	$10,436

System Universities compete with many other colleges and universities for qualified applicants. The undergraduate tuition and required fees collected by various higher education sectors in Pennsylvania during the current year are illustrated in the following table. The private colleges and universities listed were chosen because of geographic location, similar academic offerings, and similar selectivity ratios.

	2016/17 Required Fees and Tuition
Selected Private Colleges and Universities	
Washington and Jefferson College	$44,900
Elizabethtown College	$43,490
Juniata College	$42,170
Delaware Valley College	$36,750
Gannon University	$30,042
State-Related Universities (in-state)	
The University of Pittsburgh	$18,618
The Pennsylvania State University	$17,900
Temple University	$15,688
Community Colleges (in-state)	
Community Colleges Average (full-time equivalent course load)	$5,141
Pennsylvania's State System of Higher Education (in-state)	
System Average	$10,436

Source: *The Chronicle of Higher Education*

Freshmen Enrollment Composition

The following tables highlight the high school rank and average SAT scores of the System's incoming freshmen for the years indicated.

Percentage of Freshmen by High School Rank

Quintile	2012	2013	2014	2015	2016
1	22.0%	21.1%	21.4%	20.9%	19.6%
2	31.1%	29.4%	29.4%	28.7%	27.5%
3	26.5%	27.2%	25.6%	26.5%	26.8%
4	15.7%	17.0%	17.5%	17.9%	19.0%
5	4.7%	5.3%	6.1%	6.0%	7.1%

Average SAT Scores

	2012	2013	2014	2015	2016
Verbal	492	490	490	491	488
Math	500	497	496	493	489
Total	992	987	986	984	977

Student Financial Aid

Eighty-nine percent of all first-time, full-time, degree-seeking undergraduate students attending State System Universities during academic year 2015/16 received financial aid. Thirty-six percent of these students received awards from federal grant aid, while 38 percent received awards from the Commonwealth or local agencies. Twenty-seven percent of these students received awards from the institution. Seventy-nine percent of all first-time, full-time undergraduates received a student loan.

The major sources of financial aid available to System students are the Federal Pell Grant Program, Pennsylvania State Grant Program, Federal Supplemental Educational Opportunity Grant Program, Federal Work Study Program, Federal Perkins Loan Program, and Federal Direct Loan Program. Of the financial aid programs available, the three main sources of financial aid received by System students are the Federal Pell Grant, Pennsylvania State Grant, and Federal Direct Loans. Each University maintains a fully functioning student financial aid office.

Commonwealth Appropriations

In Act 188, the General Assembly defined the System as an instrumentality of state government and declared its operating costs ordinary expenses of state government, entitling it to preferred appropriations status under Article III, Section 11, of the Pennsylvania Constitution. Preferred appropriations are authorized only for state government, public schools, and payment of the public debt. Preferred appropriations bills require only a simple majority vote of the General Assembly, while "nonpreferred appropriations" bills, authorized by Article III, Section 30, of the Pennsylvania Constitution to fund state-related universities and private state-aided institutions, require a two-thirds majority vote.

One advantage of preferred appropriations status is that a smaller constitutional majority is required for passage of bills, thereby reducing the possibility of defeat. It also is settled law that, in exigent times, the Governor may reduce or entirely abate nonpreferred appropriations. See *Schnader v. Liveright*, 308 Pa. 35 (1932).

The State System's FY 2017/18 annual appropriation, based on the Commonwealth's spending plan[1] as enacted on July 10, 2017, represents approximately 19.9 percent of total revenues. Receipt of an appropriation in a given year does not ensure an appropriation or the amount of such appropriation in the following year. The chart below shows the current fiscal year and a five-year history of total annual appropriations received by the System.

[1]As of the printing of this Official Statement, the Commonwealth has not passed the FY 2017/18 revenue plan.

Fiscal Year	Appropriations
2017/18	$453,100,000
2016/17	$444,224,000
2015/16	$433,389,000
2014/15	$412,751,000
2013/14	$412,751,000
2012/13	$412,751,000

The FY 2017/18 budget includes an increase of $8.9 million (2 percent) in state appropriations. This increase, along with the $20.6 million (5 percent) provided in FY 2015/16 and the $10.8 million (2.5 percent) increase in FY 2016/17 restores approximately 45 percent of the $90.6 million cut made in FY 2011/12. At its July 2017 meeting, the Board of Governors voted to increase tuition by 3.5 percent. In addition, the State System continues to receive state funding for deferred maintenance through a portion of the realty transfer tax.

Realty Transfer Tax

In 1993, the General Assembly and the Governor of Pennsylvania passed into law a dedicated allocation of 2.7 percent of the Pennsylvania Realty Transfer Tax to the System. These revenues are restricted as to use for deferred maintenance on academic facilities. As a result of budget pressures on the Commonwealth, revenues normally received from this tax for the System were suspended during FY 2009/10 and FY 2010/11. The chart below shows the current fiscal year and a four-year history of revenues the System received from this tax.

Fiscal Year	Revenue
2017/18	$17,106,000
2016/17	$16,081,000*
2015/16	$15,295,000**
2014/15	$13,409,000
2013/14	$13,590,000

*In July 2017, an additional $45,000 was allocated to the State System.
**In July 2016, an additional $2.24 million was allocated to the State System.

Statement of Revenues, Expenses, and Changes in Net Position

This statement reports the revenues earned and the expenses incurred in the fiscal year. The resulting net income or loss is reported as an increase or decrease in net position on the *Balance Sheet.*

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Pennsylvania's State System of Higher Education

Statement of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30, 2016 and 2015
(dollars in thousands)

	2016		2015	
Operating Revenues				
Tuition and fees	$1,065,416		$1,050,135	
Less discounts and allowances	(226,381)		(233,562)	
Net tuition and fees		$839,035		$816,573
Governmental grants and contracts:				
Federal		37,519		34,393
State		104,650		104,967
Local		4,595		4,094
Nongovernmental grants and contracts		8,758		7,208
Sales and services		37,660		41,885
Auxiliary enterprises, net of discounts of $1,782 in 2016 and $1,749 in 2015		323,358		324,007
Other revenues, net		8,446		10,736
Total Operating Revenues		1,364,021		1,343,863
Operating Expenses				
Instruction		749,290		739,633
Research		6,304		5,757
Public service		39,381		37,504
Academic support		184,037		179,055
Student services		184,675		180,958
Institutional support		257,261		248,507
Operations and maintenance of plant		159,904		153,508
Depreciation		121,683		119,652
Student aid		79,136		72,948
Auxiliary enterprises		253,786		255,742
Total Operating Expenses		2,035,457		1,993,264
Operating Loss		(671,436)		(649,401)
Nonoperating Revenues (Expenses)				
State appropriations, general and restricted		433,389		412,751
Commonwealth on-behalf pension contributions		7,952		6,592
Pell grants		138,575		145,658
Investment income, net of related investment expense of $354 in 2016 and $223 in 2015		23,979		31,010
Unrealized gain (loss) on investments		2,551		(13,055)
Gifts for other than capital purposes		28,544		16,557
Interest expense on capital asset-related debt		(33,920)		(36,577)
Loss on disposal/acquisition of assets		(20,490)		(9,622)
Other nonoperating revenue		4,018		1,554
Net Nonoperating Revenues		584,598		554,868
Loss before other revenues		(86,838)		(94,533)
State appropriations, capital		15,714		13,610
Capital gifts and grants		7,620		4,145
Additions to permanent endowments		25		105
Decrease in Net Position		(63,479)		(76,673)
Net position—beginning of year		(58,503)		739,048
Restatement for July 1, 2014, pension liability and related expense				(720,878)
Net position—beginning of year, restated				18,170
Net position—end of year		($121,982)		($58,503)

Investment of Working Capital

The System invests its working capital in accordance with the Board of Governors' Investment Policy. The investment priorities of the System as stated in this policy are, in order of priority: (1) safety of principal, (2) liquidity, and (3) yield. This policy expressly prohibits leverage and speculative investment strategies.

Unrestricted Net Position

Unrestricted net position, which totals -$945.7 million, includes the effects of three unfunded liabilities: the liability of net pension totaled $938.6 million for year ended June 30, 2016 (financial statements note 4); the liability for postretirement benefits for employees who participate in the System plan totaled $1,106.6 million for the year ended June 30, 2016 (see financial statements note 5 for more information); and the liability for compensated absences totaled $115.4 million for the year ended June 30, 2016 (see financial statements note 7 for more information). Without the effect of these liabilities, total unrestricted net position would equal $1,214.9 million.

Faculty and Staff

As of October 31, 2016, System faculty numbered 4,726 full-time members and 1,228 part-time members. Of the full-time faculty members, 3,162 have been awarded tenure, and 984 are tenure-track.

As of October 31, 2016, the System employed 6,117 full-time staff members and 182 part-time staff members. The System believes that it provides a competitive compensation program for its staff, and that it is able to attract persons with outstanding qualifications.

The System participates in three different retirement systems funded in part each year from each University's operating budget: the State Employees' Retirement System (SERS), the Public School Employees' Retirement System (PSERS), and the Alternative Retirement Plan (ARP, which includes VALIC, Fidelity, and TIAA). Liabilities of the respective retirement systems are not the responsibility of the System. The basic benefits for each program are outlined below (see also financial statements note 4).

(1) State Employees' Retirement System (SERS). The employee's contribution rate is 5.00 percent of gross salary for Class A and 6.25 percent of gross salary for Class AA. An employee is vested upon completion of five years of service with the state government for these classes. The employee's contribution rate is 6.25 percent of gross salary for Class A-3 and 9.3 percent of gross salary for Class A-4. Class A-3 and Class A-4 are applicable to new members enrolling after January 1, 2011. An employee in Class A-3 or A-4 is vested upon completion of ten years of service with the state government.

(2) Public School Employees' Retirement System (PSERS). The employee's contribution rate ranges from 5.25 percent to 7.50 percent of gross salary, depending upon class and hire date. Most employees elected the 7.5 percent Class T-D when offered the higher benefit effective January 1, 2002. An employee is vested upon completion of five years of service with the state government for these classes. The employee's contribution rate is 7.5 percent of gross salary for Class T-E and 10.3 percent of gross salary for Class T-F. Class T-E and Class T-F are applicable to new members enrolling after July 1, 2011. An employee in Class T-E or T-F is vested upon completion of ten years of service with the state government.

(3) Alternative Retirement Plan (ARP). The employee's contribution rate is 5.00 percent of gross salary. An employee is immediately vested in this retirement program upon employment. Early retirement can be requested at any age; however, the amount of annuity is based on the employee/employer contributions and investment income.

The following table summarizes the System's contribution rates for employee retirement benefits for five years (including the current year) for each of the above-mentioned retirement plans. All of the figures are a percent of the employee's gross salary. (See financial statements note 4 for the dollar amount of such contributions.)

	SERS*				
	Class A	**Class AA**	**Class A-3 and A-4**	**PSERS**	**ARP**
2017/18	27.55%	34.44%	23.80%	16.29%	9.29%
2016/17	23.96%	29.95%	20.70%	15.02%	9.29%
2015/16	19.89%	24.86%	17.18%	12.92%	9.29%
2014/15	15.94%	19.92%	13.77%	10.70%	9.29%
2013/14	12.10%	15.12%	10.46%	8.465%	9.29%

**There are three different rates for SERS employees, depending on their class. The majority of System employees are in Class AA. Newly enrolled employees hired after January 1, 2011, are in Class A-3 or A-4.*

The System's contribution rates are determined by state legislation. Required employer contribution rates are expected to increase considerably in subsequent years, which will likely have a negative effect on the financial condition of the System.

On June 12, 2017, Governor Tom Wolf signed into law a new retirement plan designed for future employees in the Public School Employees' Retirement System (PSERS) and State Employees' Retirement System (SERS). The new plan provides three retirement benefit options: two "side-by-side" hybrid retirement plans which include a defined benefit and defined contribution component, and a third stand-alone defined contribution retirement plan. Additional information can be found on the Governor's website and Pennsylvania Independent Fiscal Office website.

Most System employees are represented by various labor unions. The two that represent the largest number of employees are the American Federation of State, County and Municipal Employees (AFSCME) (contract termination date June 30, 2019), and the Association of Pennsylvania State College and University Faculties (APSCUF) (contract termination date June 30, 2018 for faculty and June 30, 2019, for nonfaculty coaches, which are two separate bargaining units). Other labor unions include the State College and University Professional Association (SCUPA) (contract termination date June 30, 2019); Office and Professional Employees International Union Healthcare Pennsylvania (OPEIU) (contract termination date June 30, 2019); Security, Police and Fire Professionals of America (SPFPA) (contract termination date August 31, 2017); the Pennsylvania Doctor's Alliance (PDA) (contract termination date June 30, 2016); and the Pennsylvania Social Services Union (PSSU) (contract termination date June 30, 2019). The System has complete autonomy in the negotiation processes for the APSCUF, SCUPA, SPFPA, and OPEIU contracts. However, the System engages in coalition bargaining with the Commonwealth of Pennsylvania on all other labor union contracts. Negotiations are currently underway with PDA for a successor collective bargaining agreement. The System experienced a three-day work stoppage with APSCUF in October 2016, but it did not result in any adverse financial situation.

As of April 1, 2017, five Universities (California, Cheyney, Clarion, Edinboro, and Mansfield) had provided a letter to their local faculty union stating that they were considering the possibility of retrenchment during the next academic year. According to the collective bargaining agreement with APSCUF, a University must notify the union no later than April 1 if it is considering potential retrenchment of faculty during the next academic year. In July 2017, California University officially withdrew its letter of possible retrenchment.

Accounting Matters

The System's financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with the accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (GASB).

As of July 1, 1983, with the enactment of Act 188, the System became responsible for the use of all appropriations for all the Universities. Any funds unexpended at the end of any given fiscal year by any University or the Office of the Chancellor do not lapse to the Commonwealth, but remain in the respective accounts for future use. The presidents have the authority to expend their respective University's allocated funds as they deem proper and necessary, with review by the Office of the Chancellor. The amount of appropriations granted by the General Assembly and the Governor of Pennsylvania for the next fiscal year is not affected adversely by any cumulative amounts remaining unexpended by the Universities and the Office of the Chancellor from the prior fiscal year appropriations.

The System contracted with an external firm that, along with System personnel and in cooperation with the U.S. Department of Education (ED), analyzed and reconciled fiscal years 2011/12, 2012/13, and 2013/14 student financial aid awards of Cheyney University of Pennsylvania, a historically black university (HBCU). Cheyney University is awaiting a response from ED to the University's self-reporting to the ED, in August 2015, of federal student financial aid improperly administered and delivered in the fiscal years under review. In September 2015, the ED placed the University on Heightened Cash Monitoring 2 (HCM2) status, meaning that the University does not receive federal student financial aid funds in advance, but must use its own cash to grant federal financial aid to its students and then request reimbursement from the ED. Currently, the university is still on HCM2 status.

In the opinion of the System's management, there has been no material adverse change in the financial condition of the System since June 30, 2016.

Budgetary Matters

The president of each University is required to submit a projected operating budget for each fiscal year to the Office of the Chancellor. Periodically throughout the fiscal year, each president must submit a rebudget showing actual revenues received and expenditures incurred to date with estimated projections for the remainder of the fiscal year. These financial submissions are one tool that the Office of the Chancellor uses to monitor the financial condition of the respective Universities throughout the year to ensure that deficits are not incurred.

Financial Statements Audit

The financial statements of the System as of and for the year ended June 30, 2016, included in Appendix II of this Official Statement, have been audited by CliftonLarsonAllen LLP, independent auditors, as stated in their report appearing herein.

Legal Matters

It is the opinion of the Chief Counsel to the System that, to the best of his knowledge after reasonable investigation, there is no action, suit, proceeding, or investigation at law or in equity before or by any court, public board, or body, pending or threatened, against or affecting the System, wherein an unfavorable decision, ruling, or finding would materially adversely affect the transactions contemplated by this Official Statement or the validity of the Loan Agreement and the Disclosure Agreement.

Legislative Matters

From time to time, legislation is introduced in the Pennsylvania General Assembly which may affect the System and, therefore, may affect certain portions of the description of the System contained in this Official Statement. The System cannot predict if such legislation or other legislation will be enacted into law now or in the future and, if enacted, how any such legislation may affect the System's ability to perform its obligations with respect to the Bonds.

On March 2, 2017, Senate Resolution 34 was introduced by prime sponsor, Senator David G. Argall, directing the Legislative Budget and Finance Committee to conduct a study and issue a report relating to the State System's long-term sustainability and viability. The resolution was adopted on April 18, 2017. The Legislative Budget and Finance Committee will report its findings and recommendations to the Senate no later than December 31, 2017.

On May 11, 2017, House Resolution 331 was introduced by prime sponsor, Representative Michael K. Hanna, directing the Legislative Budget and Finance Committee to conduct the feasibility study and analyze all 14 Universities in the State System, the state's 14 community colleges, the Thaddeus Stevens College of Technology, the Rural Regional College of Northern Pennsylvania, the Allegheny College of Maryland, and four state-related universities, to discuss and promote a long-term sustainability and viability study of Pennsylvania's public institutions of higher education. The Legislative Budget and Finance Committee will issue its findings and recommendations to the General Assembly within 24 months of the adoption of this resolution. As of the printing of this Official Statement, this resolution has not been adopted.

Contingencies, Commitments, and Concentrations

See financial statements note 13 for more information on such matters.

Future Financing

Currently, there are some additional auxiliary and academic-related capital projects (e.g., student housing, recreational centers, and classroom buildings) under feasibility study and/or design. Although academic projects have Commonwealth capital funding available, not all projects are fully funded by capital appropriations. Some of these projects may come to fruition and require financing in future years. The amount to be financed for all projects is expected to be approximately $75 million in FY 2018/19. The System has wrapped up its procurement of student housing through its affiliated 501(c)(3) organizations. These affiliates have developed student housing both on and off campus on a nonrecourse project finance basis using tax-exempt and taxable debt. To date, such affiliates have financed and completed approximately 22,413 beds for approximately $1.4 billion of financing. Most housing projects are replacement stock, and some are designed to meet perceived needs for more modern housing options.

Outstanding Indebtedness

As of June 30, 2017, the outstanding indebtedness of the System is as follows:

	Issuance Date	Original Issuance Amount	Current Outstanding Principal	Maturity Date
Series AG	03/27/08	$101,335,000	$36,070,000	06/15/24
Series AH	07/17/08	140,760,000	105,695,000	06/15/38
Series AI	08/07/08	32,115,000	15,980,000	06/15/25
Series AJ	07/09/09	123,985,000	89,520,000	06/15/39
Series AK	09/03/09	47,310,000	20,455,000	06/15/24
Series AL	07/08/10	135,410,000	66,420,000	06/15/35
Series AM	07/12/11	119,085,000	94,895,000	06/15/36
Series AN	03/30/12	76,810,000	53,700,000	06/15/23
Series AO	07/18/13	30,915,000	26,775,000	06/15/38
Series AP	05/07/14	46,110,000	39,285,000	06/15/24
Series AQ	05/07/15	94,975,000	86,410,000	06/15/36
Series AR	09/10/15	102,365,000	98,070,000	06/15/40
Series AS	06/07/16	47,280,000	46,430,000	06/15/37
Series AT	09/07/16	298,110,000	293,210,000	06/15/55
Total		$1,396,565,000	$1,072,915,000	

The System has no other existing long-term indebtedness, except for the installment purchase and lease of office equipment, computer equipment, energy conservation equipment, and similar types of acquisitions. See note 3 of the 2016 Audited Financial Statements for further information pertaining to the leases.

Maturities of long-term debt for the current fiscal year, as well as the next five fiscal years, are as follows:

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Series AG	$11,105,000	$6,165,000	—	$4,360,000	$4,565,000	$4,805,000
Series AH	4,890,000	6,680,000	$7,005,000	7,295,000	7,585,000	7,890,000
Series AI	2,070,000	2,150,000	2,235,000	2,330,000	3,465,000	1,920,000
Series AJ	6,080,000	6,570,000	6,995,000	7,515,000	8,145,000	8,680,000
Series AK	4,220,000	4,405,000	3,255,000	—	30,000	75,000
Series AL	5,955,000	6,525,000	6,845,000	6,780,000	4,055,000	4,260,000
Series AM	4,900,000	4,955,000	5,215,000	5,495,000	5,775,000	6,080,000
Series AN	9,705,000	14,400,000	21,530,000	2,825,000	2,965,000	2,275,000
Series AO	1,130,000	1,170,000	1,210,000	1,255,000	1,320,000	1,370,000
Series AP	1,240,000	1,275,000	6,775,000	7,030,000	7,300,000	7,650,000
Series AQ	7,480,000	7,855,000	8,250,000	7,965,000	6,960,000	7,880,000
Series AR	2,595,000	2,725,000	2,860,000	3,000,000	3,150,000	3,315,000
Series AS	2,135,000	3,060,000	3,115,000	3,175,000	3,245,000	2,850,000
Series AT	7,100,000	7,425,000	7,765,000	8,140,000	8,105,000	8,480,000
Total	$70,605,000	$75,360,000	$83,055,000	$67,165,000	$66,665,000	$67,530,000

Strategic System Review

In March 2017, the National Center for Higher Education Management Systems (NCHEMS) was selected as the consulting firm to assist the Board of Governors with a Strategic System Review of the 14 universities and the Office of the Chancellor. On July 21, 2017, NCHEMS released the results of the report, which made various recommendations to increase efficiency throughout the State System. The recommendations included, *inter alia*, shifting from a Board of Governors to a Board of Regents, leveraging system-wide and regional resources to deliver programming, and sharing administrative functions more efficiently. Interested investors can review the report at: http://www.nchemsproject.com/system-review for a more comprehensive list of recommendations and discussion. The findings and recommendations resulting from the NCHEMS report continue to be under review. Neither the Commonwealth nor the State System is required to adopt any of the recommendations nor has either committed to do so.

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Appendix II

2016 Audited Financial Statements

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PENNSYLVANIA'S STATE SYSTEM OF HIGHER EDUCATION

Bloomsburg University CAL U CHEYNEY UNIVERSITY CLARION UNIVERSITY ESU EDINBORO UNIVERSITY IUP KUTZTOWN LOCK HAVEN UNIVERSITY MANSFIELD UNIVERSITY Millersville University SHIPPENSBURG UNIVERSITY SlipperyRock University WCU WEST CHESTER UNIVERSITY

Pennsylvania's
STATE SYSTEM
of Higher Education

FINANCIAL STATEMENTS
JUNE 30, 2016

Pennsylvania's State System of Higher Education
Financial Statements
June 30, 2016

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CliftonLarsonAllen

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INDEPENDENT AUDITORS' REPORT

Board of Governors
Pennsylvania State System of Higher Education
Harrisburg, Pennsylvania

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities and the aggregate discretely presented component units of Pennsylvania's State System of Higher Education ("the State System"), a component unit of the Commonwealth of Pennsylvania as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the State System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of certain of the discretely presented component units, which represent 85.5% percent, 94.7% percent, and 86.4% percent, respectively, of the 2016 assets, net assets, and revenues and 100% percent, 100% percent, and 100% percent, respectively, of the 2015 assets, net assets, and revenues of the discretely presented component units. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for the discretely presented component units, is based solely on the reports of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Board of Governors
Pennsylvania's State System of Higher Education

Opinions

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the aggregate discretely presented component units of the State System as of June 30, 2016 and 2015, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3-19, schedules of funding progress for OPEB on page 52, schedules of proportionate share of SERS/PSERS Net Pension Liability and SERS/PSERS schedules of contributions on page 53 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Harrisburg, Pennsylvania
September 28, 2016

MANAGEMENT'S DISCUSSION AND ANALYSIS

(Unaudited)

As the Commonwealth of Pennsylvania's (Commonwealth) public four-year higher education institutions, the 14 universities of Pennsylvania's State System of Higher Education (State System) are charged with providing high quality education at the lowest possible cost to the students. With more than 100,000 degree-seeking students enrolled, and thousands more enrolled in certificate and other career-development programs, the State System is the state's largest higher education provider. The 14 universities offer the lowest-cost four-year baccalaureate degree programs in the state, with more than 2,300 degree and certificate programs in more than 530 academic areas. The universities function independently, but being part of the State System enables them to share resources and benefit from economies of scale.

The State System financial statements comprise:

- Bloomsburg University of Pennsylvania
- California University of Pennsylvania
- Cheyney University of Pennsylvania
- Clarion University of Pennsylvania
- East Stroudsburg University of Pennsylvania
- Edinboro University of Pennsylvania
- Indiana University of Pennsylvania
- Kutztown University of Pennsylvania
- Lock Haven University of Pennsylvania
- Mansfield University of Pennsylvania
- Millersville University of Pennsylvania
- Shippensburg University of Pennsylvania
- Slippery Rock University of Pennsylvania
- West Chester University of Pennsylvania
- Office of the Chancellor

The universities operate branch campuses in Oil City (Clarion), Freeport and Punxsutawney (Indiana), and Clearfield (Lock Haven), and offer classes and programs at several regional centers, including the Dixon University Center in Harrisburg and Center City in Philadelphia.

Following is an overview of the State System's financial activities for the year ended June 30, 2016, as compared to the year ended June 30, 2015.

FINANCIAL HIGHLIGHTS

In fiscal year 2015/16, the State System received $433.4 million in General Fund **appropriations** from the Commonwealth, a 5% increase over the $412.8 million received in the last four fiscal years. The increase is the first received by the System since 2008/09, and it is $4.2 million less than the level of funding the State System received in fiscal year 1999/00—16 years ago.

The State System received a $15.3 million Realty Transfer Tax allocation from the Commonwealth's **Key '93** (Keystone Recreation, Park and Conservation) Fund, an increase of $1.9 million, or 14.2%, from fiscal year 2014/15. With the exception of fiscal years 2010/11 and 2009/10, when no funding was received, Key '93 funds have provided a consistent revenue stream for university deferred maintenance projects since 1993.

The State System was allocated $65 million in **Commonwealth capital funding**, primarily for renovation or replacement of existing educational and general (E&G) buildings. With the exception of fiscal years 2010/11 and 2009/10, when the Commonwealth's capital funding for the State System was $130 million in each year, the State System has received $65 million annually in Commonwealth capital funding since fiscal year 2000/01. Annual funding is expected to remain at $65 million in fiscal year 2016/17. The capital appropriations reflected in these statements represent the furnishings and equipment for the Commonwealth-funded construction projects and total $15.7 million and $13.6 million in fiscal years 2015/16 and 2014/15, respectively.

As part of its continuing commitment to reward the universities for demonstrated success and continued improvement in student achievement, university excellence, and operational efficiency, the State System's Board of Governors (Board) allocated $38.5 million of the general appropriation for **performance funding** in fiscal year 2015/16, nearly 3% more than the $37.4 million allocated in fiscal year 2014/15. Performance funding allocated in fiscal year 2013/14 was $37.0 million.

Fall 2015 student headcount was 107,126, a decrease of 2,480 students, or 2.3%, from fall 2014. This is the fifth year in a row that the State System has experienced an **enrollment decline**. Fall 2011 was the first year enrollment had declined since 1999, following 14 years of record growth.

Year	Fall Enrollment	% Decrease from Prior Year
2015	107,126	2.3%
2014	109,606	2.2%
2013	112,028	2.1%
2012	114,471	3.2%
2011	118,224	1.0%

Despite the recent decline, the State System's fall enrollment has increased 35% since fall 1983, which was the first year of operation as a System.

Of the 107,126 **students** in the fall 2015 enrollment, 89,845 (84%) were full-time and 17,281 (16%) were part-time students; 92,818 (87%) were undergraduate and 14,308 (13%) were graduate students. These percentages of full- and part-time, graduate and undergraduate students are approximately the same as in fall 2014 and fall 2013.

In academic year 2014/15, the State System awarded 25,556 **degrees**, comprising 20,143 bachelor's degrees, 4,802 master's degrees, 196 doctoral degrees, and 415 associate's degrees. This is slightly up from the 25,516 degrees awarded in academic year 2013/14 and slightly down from the 25,635 degrees awarded in academic year 2012/13.

The Board approved an annual full-time **tuition rate increase** of $240 (3.5%) for undergraduate resident students in fiscal year 2015/16. This compares to an increase of $198 (3.0%) in fiscal year 2014/15. The State System's 2015/16 annual tuition rate of $7,060 for full-time, resident, undergraduate students is the lowest-cost option among all four-year colleges and universities in the state.

The Board approved **new tuition rates for resident graduate students and all nonresident students**. The typical resident graduate tuition rate in 2015/16 was $470 per credit, an increase of $16. Nonresident graduate tuition increased by $24 per credit to $705. Full-time, undergraduate tuition for nonresident students ranged from $10,590 to $17,650, depending on a variety of factors, including the university and program in which a student enrolled, academic preparation, and state of residency. All of the increases average approximately 3.5%.

The Board approved a $14 increase to the **technology tuition fee** ($436 annually) for full-time resident undergraduate students and a $22 increase ($664 annually) for full-time nonresident undergraduate students. All funds raised by the technology tuition fee are used to directly benefit student learning. Universities have used the funds to install new computer labs and design multimedia classrooms, among other projects.

Mandatory student fees set by the universities increased, on average, by 4.4%. These increases, combined with the increase in tuition and reduction in enrollment, resulted in tuition and mandatory fee revenue (before discounts) of $1.09 billion, a 1.4% increase over fiscal year 2014/15. The average increase in mandatory student fees in fiscal year 2014/15 was 3.8% over the prior year.

Auxiliary revenue from **room and board fees** (excluding privatized housing revenue recorded by affiliates) was $265.5 million in fiscal year 2015/16, an increase of $0.2 million, or 0.1%, over fiscal year 2014/15. This compares to a fiscal year 2014/15 decrease of 2.0%, or $5.3 million, in room and board revenues over the prior fiscal year.

The State System's typical **price of attendance** (tuition, mandatory fees, room, and board) of $19,738 in 2015/16 was $190 above the average among all four-year public universities in the United States and $1,889 below the average in the Middle States region (Delaware, Maryland, New Jersey, New York, Pennsylvania, and Washington, D.C.), according to the latest College Board survey.

The State System purchased $190.8 million in **capital assets** in fiscal year 2015/16, including

$158.2 million to build or improve academic and auxiliary facilities across all 14 universities.

During fiscal year 2015/16, the State System issued Series AR bonds, totaling $102.4 million, to undertake various **capital projects** at the universities, comprising:

- $4.1 million for a steam plant upgrade and $6.0 million for new student housing at Bloomsburg;
- $71.8 million for acquisition of affiliate-owned student housing and $10.6 million for renovation of the student center at California; and
- $9.9 million for dining hall renovations at Millersville.

The State System also issued Series AS bonds, totaling $47.3 million, to provide funds to advance refund Series AF revenue bonds.

Bond principal of $57.7 million and bond interest of $41.7 million were paid, while $49.8 million of bonds were refunded, bringing the total outstanding **bond debt** to $842.6 million at June 30, 2016.

The State System's outstanding bonds are assigned an Aa3 rating from Moody's Investors Service, Inc. In August 2016, Moody's revised the outlook for the rating from *negative* to *stable*. Fitch Ratings reaffirmed the State System's rating of AA- with an outlook of *stable*.

THE FINANCIAL STATEMENTS

Balance Sheet

The *Balance Sheet* reports the balances of the assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position of the State System as of the end of the fiscal year.

- *Assets* include cash; investments reported at market value; the value of outstanding receivables due from students and other parties; and land, buildings, and equipment reported at cost, less accumulated depreciation.

- *Deferred Outflows of Resources*, which is defined as a consumption of net position that applies to future periods, reports the deferred loss on bond defeasance and certain items associated with the net pension liability and annual pension expense.

- *Liabilities* include payments due to vendors, employees, and students; revenues received but not yet earned; the balance of bonds payable; and amounts estimated to be due for items such as workers' compensation (the State System is self-insured), compensated absences (the value of sick and annual leave earned by employees), pension benefits, and other postretirement benefits (health and tuition benefits expected to be paid to certain current and future retirees).

- *Deferred Inflows of Resources*, which is defined as an acquisition of net position that applies to future periods, reports the deferred gain on bond defeasance and certain items associated with the net pension liability and annual pension expense.

- *Net Position*, colloquially referred to as *Net Assets* or *Fund Balance*, is the sum of Assets plus Deferred Outflows of Resources less Liabilities less Deferred Inflows of Resources.

Statement of Revenues, Expenses, and Changes in Net Position

The *Statement of Revenues, Expenses, and Changes in Net Position* reports the revenues earned and the expenses incurred during the fiscal year. The result is reported as an increase or decrease in net position.

In accordance with GASB requirements, the State System has classified revenues and expenses as either operating or nonoperating. GASB has determined that all public colleges' and universities' **state appropriations are nonoperating revenues**. In addition, GASB requires classification of gifts, Pell grants, investment income and expenses, unrealized gains and losses on investments, interest expense, and losses on disposals of assets as nonoperating. The State System classifies all of its remaining activities as operating.

Statement of Cash Flows

The *Statement of Cash Flows* provides information about the State System's cash receipts and cash payments. It can be used to determine the State System's ability to generate future net cash flows and meet its obligations as they come due and its need for external financing.

Net Position

In accordance with GASB requirements, the State System reports three components of net position:

- *Net investment in capital assets* is the cost of land, buildings, improvements, equipment, furnishings, and library books, net of accumulated depreciation, less any associated debt (primarily bonds payable). This balance is not available for the State System's use in ongoing operations, since the underlying assets would have to be sold in order to use the balance to pay current or long-term obligations. The Commonwealth prohibits the State System from selling university land and buildings without prior approval.

- *Restricted* net position represents the portion of balances of funds received from the Commonwealth, donors, or grantors who have placed restrictions on the purpose for which the funds must be spent. *Nonexpendable* restricted net position represents the corpus of endowments and similar arrangements in which only the associated investment income can be spent. *Expendable* restricted net position represents the portion of restricted funds that is available for expenditure as long as any external purpose and time restrictions are met.

- *Unrestricted* net position includes funds that the Board or university presidents have designated for specific purposes, auxiliary funds, and all other funds not appropriately classified as restricted or invested in capital assets.

  Unrestricted net position includes three unfunded liabilities. Because these liabilities are expected to be realized gradually over future years, and because of their size, the universities fund them only as they become due.

  - The liability for **compensated absences** represents the dollar value of annual and sick leave that employees have earned and could potentially receive in the form of cash payouts upon retirement or other termination. The dollar value is based on an employee's current salary. All full-time employees are eligible to be paid, upon termination, for the dollar value of the number of days of unused annual, personal, and holiday leave that they have accumulated, with a maximum accumulation of 45 days; the associated liability is calculated based on the total number of days that employees have accumulated at June 30. Sick leave payouts, however, are subject to vesting requirements, and the dollar value of accumulated unused sick leave is paid only to those employees who meet certain service and/or age requirements and is capped at various levels depending upon the number of days accumulated. The associated liability is estimated based on a calculation of historical leave payouts for terminated employees compared to the dollar value of sick days that the terminated employees had accumulated, applied to employees' current leave balances.

    As employees earn and accumulate leave, the compensated absences liability is increased; as employees use leave, and as terminated employees receive payouts, the liability is decreased. The compensated absences liability increased by $0.8 million to $115.4 million for the year ended June 30, 2016, compared to a $0.1 million decrease from the prior year for the year ended June 30, 2015. Universities fund this liability only as cash payouts are made to employees for annual and vested sick leave balances upon termination or retirement.

  - The liability for **other postretirement benefits** represents the estimated future health care costs for current and future retirees who participate in the State System health care plan. The annual increase in the liability is the amount that current employees earn each fiscal year as a retiree health care benefit, actuarially calculated based on years of service, age, and estimates of future service and employee longevity. The liability also increases as health care costs increase. The liability decreases when required contributions by retirees are increased, when the number of eligible employees decrease, and when retirees die. The liability increased by $47.9 million to $1.10 billion for the year ended June 30, 2016. Universities fund this liability on a "pay-as-you-go" basis; that is, they make biweekly contributions to fund the actual claims made by retirees during the year.

  - The **net pension liability** is the State System's allocated share of the difference between the Commonwealth's defined benefit pension obligations and the funding set aside in a qualified trust to pay the future benefits that are promised to current employees, retirees, and their beneficiaries. The annual increase in the liability is the amount that current employees earn each fiscal year as a pension benefit, actuarially calculated based on years of service, age, and estimates of future service and employee longevity. The liability decreases when funding of the qualified trust increases and when employees or retirees leave the pension plans. The liability increased by $139.9 million to $938.6 million for the year ended June 30, 2016. Like the postretirement benefits liability, universities fund this liability on a "pay-as-you-go" basis with annual contractually required contributions to the State Employees Retirement System (SERS) and the Public School Employees Retirement System (PSERS).

Overall, net position decreased by $63.4 million in fiscal year 2015/16. This compares to a decrease from the prior year of $797.5 million in fiscal year 2014/15 (which included a $720.9 million net pension liability restatement), and a decrease of $52.8 million in fiscal year 2013/14 over fiscal year 2012/13.

Following is a summary of the balance sheet at June 30, 2016, 2015, and 2014.

(in millions)

Balance Sheet

	June 30, 2016	Change from Prior Year	June 30, 2015	Change from Prior Year	June 30, 2014	Change from Prior Year
Assets						
Cash and investments	$1,376.2	3.2%	$1,333.9	(2.1%)	$1,363.1	0.0%
Capital assets, net	1,653.3	4.0%	1,589.2	(1.7%)	1,616.8	(0.8%)
Other assets and deferred outflows	376.6	42.7%	263.9	42.8%	184.8	5.1%
Total assets and deferred outflows	$3,406.1	6.9%	$3,187.0	0.7%	$3,164.7	(0.1%)
Liabilities						
Workers' compensation	$22.1	(2.2%)	$22.6	4.1%	$21.7	1.9%
Compensated absences	115.4	0.7%	114.6	(0.1%)	114.7	4.4%
Postretirement benefits	1,106.6	4.5%	1,058.7	5.1%	1,007.1	7.9%
Net pension liability	938.6	17.5%	798.7	N/A	N/A	N/A
Bonds payable	842.6	5.3%	800.5	(6.9%)	859.9	(4.4%)
Other liabilities and deferred inflows	502.8	11.6%	450.4	6.7%	422.3	2.5%
Total liabilities and deferred inflows	3,528.1	8.7%	3,245.5	33.8%	2,425.7	2.1%
Net Position						
Net investment in capital assets	709.3	1.3%	700.3	2.3%	684.4	5.7%
Restricted	114.4	16.6%	98.1	(5.0%)	103.3	11.7%
Unrestricted	(945.7)	(10.4%)	(856.9)	(1,659.5%)	(48.7)	(194.4%)
Total net position	(122.0)	(108.5%)	(58.5)	(107.9%)	739.0	(6.7%)
Total liabilities, deferred inflows, and net position	$3,406.1	6.9%	$3,187.0	0.7%	$3,164.7	(0.1%)

Revenues and Gains
Following is a summary of revenues and gains for the years ending June 30, 2016, 2015, and 2014.

(in millions)

Revenues and Gains

	June 30, 2016	Change from Prior Year	June 30, 2015	Change from Prior Year	June 30, 2014	Change from Prior Year
Operating revenues						
Tuition and fees, net	$839.0	2.7%	$816.6	0.9%	$809.3	0.6%
Grants and contracts	155.5	3.2%	150.7	(6.3%)	160.8	1.8%
Auxiliary enterprises, net	323.4	(0.2%)	324.0	(2.2%)	331.4	(0.5%)
Other	46.1	(12.4%)	52.6	(1.1%)	53.2	19.6%
Total operating revenues	1,364.0	1.5%	1,343.9	(0.8%)	1,354.7	1.1%
Nonoperating revenues and gains						
State appropriations	449.1	5.3%	426.4	(0.2%)	427.1	(0.1%)
Investment income, net	24.0	(22.6%)	31.0	18.3%	26.2	28.4%
Unrealized gain on investments	2.6	-	-	-	-	-
Gifts, nonoperating grants, and other	186.7	6.9%	174.6	4.3%	167.4	(2.6%)
Total nonoperating revenues and gains	662.4	4.8%	632.0	1.8%	620.7	0.1%
Total revenues and gains	$2,026.4	2.6%	$1,975.9	-	$1,975.4	0.8%

Overall, fiscal year 2015/16 **operating revenues** increased by 1.5% from the prior fiscal year. Nonoperating revenues increased by 4.8%, for an overall increase in revenues and gains of 2.6%.

Tuition and fees are shown net of scholarship discounts and allowances and bad debt expense. In accordance with a formula prescribed by the National Association of College and University Business Officers (NACUBO), the State System allocates the cost of scholarships, waivers, and other student financial aid between scholarship discounts and allowances and student aid expense. Scholarships and waivers of room and board fees are reported in Auxiliary enterprises. The cost of tuition waivers granted to employees is reported as employees' benefits expense. Bad debt expense is an estimate of the amount owed by students that will not be collected.

Despite the decline in enrollment, overall net tuition and fee revenue increased by $22.4 million, or 2.7%, over fiscal year 2014/15. This can be attributed to both the increase in the tuition and fee rates and to the continuing execution of 25 new flexible tuition pricing programs, which began to be implemented in fiscal year 2013/14. These pilot programs are designed to address the unique market conditions that affect each of the universities and will be evaluated over a two- or three-year period to determine their effectiveness as well as whether they should be duplicated at other universities.

Auxiliary enterprises revenue, which includes food service sales, housing fees, and fees for the operation, maintenance, debt service, and renewal of student union and recreation centers, decreased by $0.6 million from fiscal year 2014/15. The overall decrease is due to several factors:

- The combination of **university housing fees** and **privatized housing fees** increased in fiscal year 2015/16 over fiscal year 2014/15 by $1.5 million, or 1.1%, to a total of $135.2 million. This compares to a decrease of $8.1 million, or 5.7%, in fiscal year 2014/15 over fiscal year 2013/14. The privatized housing fees result from the privatized housing contracts in which the universities manage the operations on behalf of their affiliates. The fees are used to cover associated expenses, capital expenditures, and debt service, and include some form of profit-sharing between the universities and their respective affiliates.

- The revenue that universities record as university housing fees, versus the revenue recorded as privatized housing fees, is fluctuating, as some universities begin to convert their affiliates' privatized housing into university housing while others have expanded the use of privatized housing. In fiscal year 2015/16, California University acquired all six of the student residence halls on campus property that had been constructed by their affiliate, Student Association, Incorporated, while Clarion and Millersville Universities expanded their privatized housing. In fiscal year 2016/17, Edinboro, Lock Haven, and Mansfield Universities will complete the acquisition of privatized housing from their affiliates.

- Several universities have privatized housing contracts that do not involve the universities in the management of housing operations but primarily provide for **ground lease fees** to be paid to the universities by affiliates who have constructed the housing on university- or Commonwealth-owned land. The universities record these ground lease fees, which totaled $2.1 million in fiscal year 2015/16, as E&G, rather than Auxiliary, revenue. Universities recorded $2.9 million in ground lease fees in E&G in fiscal year 2014/15. The fiscal year 2015/16 decrease reflects contract provisions that vary the amount of the ground lease fees over the term of the agreements.

- **Food service sales** declined by $1.3 million, or 1.0%, in fiscal year 2015/16 over fiscal year 2014/15, compared to an increase of $2.8 million, or 2.2%, in fiscal year 2014/15 over the prior year. Most universities saw relatively small decreases in food service revenue in fiscal year 2015/16, while some had relatively small increases, and the overall decline can be attributed at least in part to the decline in enrollment.

- **Fees for student union and recreation centers** have been increasing slightly, with revenues of $47.4 million, $47.3 million, and $46.7 million recorded in fiscal years 2015/16, 2014/15, and 2013/14, respectively.

State appropriations include cash as well as capital appropriations that are received in the form of noncash furnishings and equipment for the Commonwealth-funded construction projects. The fiscal year 2015/16 general cash appropriation was $433.4 million, a $20.6 million increase over fiscal year 2014/15, while noncash capital appropriations were $15.7 million, a $2.1 million increase over fiscal year 2014/15.

Investment income (net of related investment expenses) for fiscal year 2015/16 was $24.0 million. This represents a decrease of $7.0 million from the prior year. The decrease is due in part to the delayed receipt of the first five months of appropriations, totaling $219.4 million, which were not released to the State System until January 2016. In addition, the reimbursement bond investment portfolio, which is dedicated to pay associated debt service, experienced a decrease of approximately $7.8 million of investment earnings from the prior year, primarily due to the timing in the schedule of maturing securities. Interest rates, which rose slightly in the first half of the fiscal year, remained flat during the second half.

Expenses and Losses
Following is a summary of expenses and losses for the years ending June 30, 2016, 2015, and 2014.

(in millions)

Expenses and Losses

	June 30, 2016	Change from Prior Year	June 30, 2015	Change from Prior Year	June 30, 2014	Change from Prior Year
Operating expenses						
Instruction	$749.3	1.3%	$739.6	2.6%	$721.0	2.3%
Research	6.3	8.6%	5.8	13.7%	5.1	(5.6%)
Public service	39.4	5.1%	37.5	-	37.5	9.6%
Academic support	184.0	2.7%	179.1	4.2%	171.9	0.6%
Student services	184.7	2.0%	181.0	2.5%	176.6	3.7%
Institutional support	257.2	3.5%	248.5	(5.9%)	264.0	2.3%
Operations and maintenance of plant	159.9	4.2%	153.5	0.8%	152.3	6.4%
Depreciation	121.7	1.7%	119.7	(0.4%)	120.2	0.6%
Student aid	79.1	8.5%	72.9	(3.6%)	75.6	1.5%
Auxiliary enterprises	253.8	(0.7%)	255.7	1.5%	251.8	3.5%
Total operating expenses	2,035.4	2.1%	1,993.3	0.9%	1,976.0	2.7%
Other expenses and losses						
Interest expense on capital asset-related debt	33.9	(7.4%)	36.6	(0.8%)	36.9	(2.6%)
Loss on disposal/acquisition of assets	20.5	113.5%	9.6	20.7%	12.1	92.1%
Unrealized loss on investment	-	-	13.1	309.4%	3.2	(37.3%)
Total other expenses and losses	54.4	(8.3%)	59.3	13.6%	52.2	5.7%
Total expenses and losses	$2,089.8	1.8%	$2,052.6	1.2%	$2,028.2	2.8%

Universities spent $749.3 million on **instruction**, or 36.8% of total operating expenses, in fiscal year 2015/16. This represents an increase of $9.7 million, or 1.3%, over fiscal year 2014/15.

Financial aid to students in the form of grants, waivers, and scholarships was $299.4 million in fiscal year 2015/16. In accordance with a formula prescribed by the National Association of College and University Business Officers (NACUBO), in fiscal year 2015/16 the State System reported $219.9 million of financial aid as *discounts,* which are netted against tuition and fees, and $79.5 million as *student aid*, which is reported as an expense. Of these amounts, $1.2 million of discounts and $0.4 million of student aid expense were reported in Auxiliary enterprises.

Including the financial aid that is recorded as a discount against tuition and fees, financial aid decreased in fiscal year 2015/16 by $1.1 million from the previous year. The drop is attributed to a $7.0 million decrease in Federal Pell grants, while all other financial aid increased by a total of $5.9 million. Following is the breakdown of financial aid in fiscal years 2015/16 and 2014/15.

(in millions)

Student Financial Aid

	2015/16	2014/15
Federal Pell grants	$138.6	$145.6
Other federal aid	5.2	5.0
State financial aid including PHEAA grants	93.0	91.5
Local government financial aid	2.6	1.5
Scholarships from endowments and restricted gifts and grants	17.0	16.4
Unrestricted scholarships and fellowships	10.0	10.6
Tuition and fee waivers	31.4	28.5
Housing and dining waivers	1.6	1.4
Total	$299.4	$300.5

Interest expense on capital asset-related debt was $33.9 million, a decrease of $2.7 million over fiscal year 2014/15, even though bonds payable increased by $42.1 million in fiscal year 2015/16 over 2014/15. The decrease in interest expense is primarily because the State System has been annually refunding debt with debt that carries lower interest rates. In addition, the older, more expensive, debt is being amortized at a faster rate, as a higher ratio of debt service is being applied to principal rather than interest.

Salaries and benefits totaled $1.4 billion in fiscal year 2015/16. Salary and wage expenses decreased by $11.6 million, or 1.3%, while benefits expenses increased by $39.1 million, or 8.1%, over fiscal year 2014/15, for an overall increase of $27.5 million. Following is a summary of salaries, wages, and benefits expenses for the years ending June 30, 2016, 2015, and 2014.

(in millions)

Salaries, Wages, and Benefits

	June 30, 2016	Change from Prior Year	June 30, 2015	Change from Prior Year	June 30, 2014	Change from Prior Year
Salaries and wages	$880.4	(1.3%)	$892.0	1.4%	$879.5	1.2%
Benefits						
Employee health care	128.5	5.4%	121.9	3.4%	117.9	8.6%
Health & Welfare Fund	8.6	2.4%	8.4	(5.6%)	8.9	7.2%
Postretirement health care	125.0	4.8%	119.3	(18.4%)	146.2	6.0%
SERS	104.0	24.6%	83.5	92.0%	43.5	42.6%
PSERS	16.0	138.8%	6.7	71.8%	3.9	39.3%
Alternative Retirement Plan (ARP)	43.9	(1.6%)	44.6	1.6%	43.9	1.9%
Other benefits	97.2	(2.5%)	99.7	5.4%	94.6	(2.3%)
Total benefits	523.2	8.1%	484.1	5.5%	458.9	7.2%
Total salaries, wages, and benefits	$1,403.6	2.0%	$1,376.1	2.8%	$1,338.4	3.2%

The decrease in **salaries and wages** primarily is attributed to a 1.1% reduction in total salaried complement in fiscal year 2015/16 from fiscal year 2014/15. Total salaried complement, which includes both permanent and temporary employees but excludes wage employees, was 12,179 in fall 2015, compared to 12,316 in fall 2014, a reduction of 137 employees. Since fall 2010, when total salaried complement was 12,749, the State System has reduced staff by 4.5%, or 570 employees.

Despite the decrease in total salaried complement, employer share of **employee health care costs**, including the Health & Welfare Fund, increased $6.8 million over fiscal year 2014/15, for a total increase of 5.2%. This follows consecutive increases of 2.8% ($3.5 million) and 8.5% ($9.9 million) in fiscal years 2013/14 and 2012/13, respectively, over the prior fiscal years. The increases are directly attributed to rising health care costs as well as employees' increasing use of health benefits.

The **postretirement health care** expense comprises:

- Premium payments to the Retired Employees Health Program (REHP), which is administered by the Commonwealth's Pennsylvania Employee Benefits Trust Fund (PEBTF);
- Claims paid to the third-party vendor for the plan administered by the State System (System Plan); and
- The actuarially calculated expense for the System Plan, in excess of claims paid, to recognize the current year increase in the long-term liability for future benefits expected to be paid from the System Plan for current and future retirees.

(in millions)

Postretirement Health Care

	2015/16	2014/15	2013/14
REHP premiums paid	$37.0	$30.7	$28.6
System Plan claims paid	40.1	36.9	44.2
System Plan actuarially calculated expense in excess of claims paid	47.9	51.7	73.4
Total	$125.0	$119.3	$146.2

The annual **REHP premiums** increased 20.5% ($6.3 million) in fiscal year 2015/16 over 2014/15, following an increase of 7.3% ($2.1 million) in fiscal year 2014/15 over 2013/14. The contribution rate is set at the discretion of the Commonwealth and generally is not known in advance. The State System currently does not record a liability for future benefits related to the REHP plan, but will be required to do so beginning in fiscal year 2017/18 in accordance with GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions.* The amount of the liability is not known but is expected to be significant.

The monthly cash payments made to a third-party health insurance vendor for the **System Plan** are based on estimates of retiree health care claims that are agreed to by the State System and the third-party vendor and are adjusted in the following year for the actual claims paid on behalf of retirees. The State System has seen flat or declining health care spending from retirees for the last several years, and increases are attributed to the increasing population of retirees and rising health care costs rather than the increase in benefits usage by retirees.

Following is a schedule of postretirement medical benefits annual payments, expense, and liability for the years ending June 30, 2016, 2015, and 2014, for the System Plan.

(in millions)

System Plan Postretirement Medical Benefits (referred to as Other Postemployment Benefits or OPEB)

	June 30, 2016	**Change from Prior Year**	**June 30, 2015**	**Change from Prior Year**	**June 30, 2014**	**Change from Prior Year**
Claims paid ("pay-as-you-go")	$40.1	8.7%	$36.9	(16.6%)	$44.2	2.9%
Annual OPEB cost (actuarial expense reported)	$88.0	(0.7%)	$88.5	(24.7%)	$117.6	4.7%
Net OPEB obligation (liability reported on the balance sheet)	$1,106.6	4.5%	$1,058.7	5.1%	$1,007.1	7.9%
Accrued actuarial liability (total liability as estimated by actuaries)	$1,194.8	-	$1,194.8	(18.9%)	$1,473.6	3.7%

- **Employer contributions to SERS**, a defined benefits pension plan, increased 20.6% over fiscal year 2014/15, for a total increase of $11.8 million. This follows consecutive increases of 31.4% ($13.7 million) and 42.6% ($13.0 million) in fiscal years 2014/15 and 2013/14, respectively, over the prior fiscal years. The increases were instituted by SERS to fund its net pension liability, which was $18.2 billion at December 31, 2015, a $3.3 billion increase from the $14.9 billion net pension liability reported at December 31, 2014. Approximately 40% of the State System's employees are enrolled in SERS.

- **Employer contributions to PSERS**, a defined benefits pension plan, increased 15.4% over fiscal year 2014/15, for a total increase of $0.8 million. This follows consecutive increases of 32.9% ($1.3 million) and 39.3% ($1.1 million) in fiscal years 2014/15 and 2013/14, respectively, over the prior fiscal years. The increases were instituted by PSERS to fund its net pension liability, which was $43.3 billion at June 30, 2015, up from the $39.6 billion net pension liability reported at June 30, 2014. Since approximately only 7% of the State System's employees are enrolled in PSERS, the impact of contribution rate increases from PSERS is far less than the impact from SERS. The Commonwealth makes annual pension contributions to PSERS on behalf of State System employees at the same annual rate.

- **Employer contributions to the ARP** (Alternative Retirement Plan), a defined contribution plan, decreased 1.6% over fiscal year 2014/15, for a total decrease of $0.7 million. This follows consecutive increases of 1.7% ($0.7 million) and 1.9% ($0.8 million) in fiscal years 2014/15 and 2013/14, respectively, over the prior fiscal years. The changes in annual contributions are attributed to fluctuating employee participation and salary increases. The employer contribution rate (9.29%) has been the same since the plan's inception. Since the ARP is a defined contribution plan, the State

System has no liabilities related to future benefits. Approximately 49% of the State System's employees are enrolled in the ARP.

Following is a summary of pension benefits annual contributions, expense, and liability for the years ending June 30, 2016, 2015, and 2014.

(in millions)

Pension Benefits

	June 30, 2016	Change from Prior Year	June 30, 2015	Change from Prior Year	June 30, 2014	Change from Prior Year
Employer contributions						
SERS	$69.0	20.6%	$57.2	31.4%	$43.5	42.6%
PSERS	$6.0	15.4%	$5.2	32.9%	$3.9	39.3%
ARP	$43.9	(1.6%)	$44.6	1.7%	$43.9	1.9%
Pension expense						
SERS	$104.0	24.6%	$83.5	92.0%	$43.5	42.6%
PSERS	$16.0	138.8%	$6.7	71.8%	$3.9	39.3%
ARP	$43.9	(1.6%)	$44.6	1.7%	$43.9	1.9%
Net pension liability						
SERS	$858.4	17.9%	$728.1	7.4%	$677.9	Not calculated
PSERS	$80.2	13.4%	$70.7	(0.4%)	$71.0	Not calculated
ARP	$0.0	-	$0.0	-	$0.0	-

- The cost for **all other employee benefits**, such as Social Security and workers' compensation, decreased by a total of $2.5 million, or 2.5% less than fiscal year 2014/15, compared to a fiscal year 2014/15 increase of $5.1 million, or 5.4%, over fiscal year 2013/14. The decreases can be attributed to the decrease in the number of employees.

Future Economic Factors

The **Commonwealth** ended fiscal year 2015/16 with General Fund collections that were $29.9 million, or 0.1%, more than estimated. The Commonwealth budget, which is highly dependent on a growing economy, faces continued challenges, such as increasing pension obligations, wages and benefits, debt service, and medical and entitlement costs. These mandated cost drivers are expected to consume virtually all revenue growth if there is no change in current revenue sources. In its March 24, 2016, *Issuer Comment* on the Commonwealth, Moody's Investors Service, Inc., stated:

> *The authorized 2016 budget plan modestly increases spending without approving any of the taxes the governor had proposed to improve fiscal balance. The approved budget relies on nearly $1 billion of one-time measures to balance the budget, does not include a pension contribution at the full actuarially required level, and casts no light on the government's ability to reach compromise on its long-term fiscal challenges.*
>
> *Pennsylvania faces sharply higher pension contributions in the coming years, and we expect its economy to underperform due to weak demographics and poor fiscal conditions over the long term. The commonwealth's willingness to adhere to this pension contribution schedule in spite of what could be slow tax revenue growth will be a major factor in the commonwealth's credit profile over that time horizon.*

Cash Flow

The universities record their share of the State System pooled deposits and investments account at cost; that is, without regard to the fair value of the underlying investments. The associated markup or markdown for the fair value, and annual unrealized gains or losses on investments, is recorded only at the consolidated level. In fiscal year 2015/16, the unrealized gain on the State System pooled deposits and investments account was $2.6 million, and the accumulated fair value markup at June 30, 2016, was $118.5 million. This compares to an unrealized loss on investments in fiscal year 2014/15 of $13.1 million and an accumulated fair value markup of $115.2 million at June 30, 2015.

The combination of factors such as years of stagnant appropriations, declining enrollment, low interest rates, increasing personnel costs, and high long-term debt is causing cash flow pressures for several State System universities, especially during the summer months between spring and fall tuition collections. Although cash and investments that are attributed to Restricted and Auxiliary activities must be kept separate from the cash and investments that result from E&G operations, some universities are beginning to temporarily borrow from Auxiliary funds to meet payroll requirements, even though their Auxiliary operations also are experiencing significant declines in cash balances. Cash flow weaknesses, which can seriously threaten financial viability, are affecting the smaller more than the larger State System universities, whose cash flows remain relatively strong.

- Cheyney University has been borrowing from the State System pooled deposits and investments account since August 2013. The balance owed at June 30, 2016, stands at $19 million, which, along with a line of credit of an additional $3.5 million, is projected to sustain operations through most of fiscal year 2016/17. Drawdowns are taken on an as-needed basis and paid back on an as-available basis, with an interest rate based on the five-year U.S. Treasury Bond rate plus 25 basis points. The university's E&G and Auxiliary cash both would be in deficits without the borrowed funds. To ensure the security of cash inflows that have been restricted as to purpose by the donor or grantor, separate bank and investment accounts have been established for these funds, and access to them requires the approval of the Office of the Chancellor. It is anticipated that additional lines of credit will be made available to Cheyney University until break-even status is achieved. The Office of the Chancellor is working closely with the university to manage the lines of credit.

- Over the last four years, Clarion University's E&G cash has decreased by $14.1 million, or nearly 61%, from $23.3 million at June 30, 2013, to $9.2 million at June 30, 2016. Auxiliary cash has decreased by $8.4 million, or more than 55%, from $15.2 million at June 30, 2013, to $6.8 million at June 30, 2016. In fiscal year 2015/16, E&G operating and plant expenditures exceeded revenue by $7.0 million, while Auxiliary operating and plant expenditures exceeded revenue by $7.6 million. The steep decline in cash, as well as the deficits in current year operations, can be attributed in part to Clarion's use of $11.6 million of cash for capital expenditures in fiscal year 2015/16: E&G capital expenditures included $1.6 million for academic building renovations and $1.2 million for equipment and other improvements; Auxiliary capital expenditures included $5.2 million in leasehold improvements, $2.1 million in renovations for the student services facility, and $1.5 million in equipment and other improvements. The Office of the Chancellor has begun to work with Clarion University to closely monitor its cash flows.

- Over the last four years, Mansfield University's E&G cash has decreased by $10.1 million, or more than 57%, from $17.6 million at June 30, 2013, to $7.5 million at June 30, 2016. Auxiliary cash has decreased by $2.4 million, or more than 24%, from $9.8 million at June 30, 2013, to $7.4 million at June 30, 2016. In fiscal year 2015/16, E&G operating and plant expenditures exceeded revenue by $3.9 million, while Auxiliary operating and plant expenditures exceeded revenue by $1.9 million. In response, the university has reduced staff and engaged in other cost-cutting measures. The university also is instituting a per-credit tuition pilot in fiscal year 2016/17, which could help to stabilize tuition revenue despite an anticipated decline in enrollment. The Office of the Chancellor has been working with Mansfield University to closely monitor its cash flows.

- A few of the remaining universities have experienced sharp declines in E&G and/or Auxiliary cash, and although these universities have not reached critical cash levels, a continual erosion of revenue could soon cause cash flow concerns for some. The other universities have relatively strong cash balances, with several universities close to or exceeding $100 million at June 30, 2016, and West Chester's unrestricted cash balance alone close to $220 million. Overall, university E&G cash increased by $8.2 million, for a cash balance of $659.0 million at June 30, 2016, while Auxiliary cash increased by $25.6 million, for a cash balance of $336.6 million at June 30, 2016. The Office of the Chancellor is monitoring universities whose cash balance, revenue, expenditure, and enrollment trends may be an indication of future cash flow weaknesses.

Privatized Housing Acquisitions

In order to decrease operational expenses and lower the cost of debt service, several universities are purchasing the student residence halls that were constructed by their affiliated organizations by issuing tax-exempt bonds through State System bond financing and paying off affiliates' debt. Since the transactions are between related parties, GAAP requires that the universities record the assets (the buildings) at the depreciated value that was recorded on the affiliates' books at the time of acquisition by the universities. Consequently, the debt being assumed by the universities significantly exceeds the value of the asset recorded, because not only did the funds that were originally borrowed by the affiliates include noncapitalized items such as furnishings and debt service fees, but also because the annual depreciation on the housing recorded by the affiliates exceeded the annual payments that were made to reduce debt principal.

In fiscal year 2015/16, California University acquired all six of the student residence halls on campus property that had been constructed by their affiliate, Student Association, Incorporated. The book value of the housing at the time of acquisition was $55.7 million, but the debt assumed was $71.3 million, resulting in a **loss on acquisition of $15.6 million**. Despite the negative effect on its balance sheet, over the 25-year debt term the university expects to reduce debt service payments by about $34 million and avoid an estimated $18 million in operating costs such as ground lease payments, management fees, insurance, and payments in lieu of taxes.

In fiscal year 2016/17, Edinboro, Lock Haven, and Mansfield Universities are undertaking similar acquisitions of housing built by their affiliated organizations, and similar results are expected.

Revenue
In fiscal year 2016/17, the State System will receive $444.2 million in **General Fund appropriations**, an increase of $10.8 million, or 2.5%, over fiscal year 2015/16. This compares to a 5% increase received in 2015/16 over the prior fiscal year. Even with the consecutive increases in Commonwealth support, the State System will receive about $40 million less from the Commonwealth in fiscal year 2016/17 than it did in 2007/08, just before the onset of the recession that severely weakened both the state and national economies and led to several years of funding cuts to the State System.

The Commonwealth has continued its commitment to fund the State System's deferred maintenance projects with a Realty Transfer Tax allocation from the **Key '93** funds. The State System has received $16.0 million from this revenue stream in fiscal year 2016/17, a 4.6% increase from the $15.3 million received in fiscal year 2015/16. The annual amount received is an estimate and may be adjusted based upon the health of the real estate market.

The 14 State System universities have eliminated nearly $300 million in expenditures from their combined operating budgets over the last decade in order to balance their budgets and to help hold down student costs. This, combined with the Commonwealth's boosted funding to the State System by about $31.5 million over the last two years, after seven straight years of flat or reduced general fund appropriations, has enabled the Board to approve the **smallest percentage tuition increase in more than a decade**. The $178 academic year increase approved by the Board for the 2016/17 academic year will set the base tuition rate for most full-time Pennsylvania residents—who comprise about 90 percent of all State System students—at $3,619 per semester, or $7,238 for the full year. Even with this modest increase, the State System universities will remain the lowest-cost option among all four-year colleges and universities in the state.

Nonresident, undergraduate tuition also will increase by 2.5% and will range from $10,858 to $18,096 for the 2016/17 academic year. The technology fee will be $448 for full-time resident students, and $682 for full-time nonresidents. The typical resident, graduate tuition rate will be $483 per credit, an increase of $13. The nonresident, graduate tuition rate will increase by $20 per credit, to $725.

The tuition rate increase, coupled with the increase in state appropriations, will provide almost all of the additional funds the universities need to balance their budgets. Significant cost increases are expected this year in several areas, including health care and pension contributions, over which the universities essentially have no control, as well as potential increases in salaries as a result of new collective bargaining agreements. As the number of high school graduates in the state continues to drop, most of the universities are expecting their enrollments to decline slightly, resulting in reduced revenue.

Enrollment
With an undergraduate population comprising approximately 90% Pennsylvania residents—and the majority of those being traditional-age students enrolling right out of high school—the State

System's enrollment historically has been closely tied to the state's high school demographic trends. Following is the projected number of Pennsylvania **high school graduates** based on estimates from the Pennsylvania Department of Education.

Projected Pennsylvania High School Graduates

Fiscal Year	Number of Graduates	% Increase (Decrease)
2015/16	124,737	0.4%
2016/17	123,878	(0.7%)
2017/18	124,636	0.6%
2018/19	124,394	(0.2%)
2019/20	121,683	(2.2%)
2020/21	122,923	1.0%
2021/22	123,582	0.5%
2022/23	121,918	(1.3%)
2023/24	123,769	1.5%

Pension Costs

In June 2016, the Pennsylvania Senate rejected a pension reform bill passed by the Pennsylvania House of Representatives that would have reduced pension benefits for future public school employees and most future state workers. The bill provided for a "stacked" plan, which required that employees change from a defined benefit plan to a defined contribution plan once their salaries exceeded $50,000, and would have increased the new employees' pension contributions to 7.5% of salary. The Senate favors a "side-by-side" plan that would be part defined benefit plan and part defined contribution plan for an employee's entire salary. Both legislative chambers have pledged to work together to come up with a compromise plan for pension reform. As of the date of these statements, there has been no consensus on pension reform and no new pension legislation enacted.

SERS

- In fiscal year 2015/16, SERS continued its increases in employer pension contribution rates. The most predominant employer-paid SERS rates for State System employees rose nearly 25% in 2015/16, after increases of 32% in 2014/15 and more than 44% in 2013/14. The rates have increased by an additional 20.5% in 2016/17, bringing the **contribution rate to 29.95%** of employees' eligible salaries. According to SERS, the rate is expected to grow to 33.3% of employees' eligible salaries in fiscal year 2017/18.

- As of December 31, 2015, the SERS **net pension liability** was $18.2 billion, compared to $14.9 billion and $13.7 billion at December 31, 2014 and 2013, respectively.

- SERS **funded ratio**, which is the actuarial value of assets compared to the actuarial accrued liability, was approximately 58.0% at December 31, 2015, compared to 59.4% and 59.2% at December 31, 2014 and 2013, respectively. For comparison, the funded ratio at December 31, 2003, was 104.9%, while SERS projects the funded ratio at December 31, 2026, to be only 69.5%.

- In 2015, more than 6,700 **new retirees** were added to the annuity payroll, with an average annual benefit of approximately $26,100; however, just 4,303 retirees, who had average annual benefits of about $14,600, were removed from the rolls. The rolls have increased by 22,629 members, or 22.2%, since 2006.

- In 2015, SERS assets produced **investment returns** of 0.4%, down from 6.4% in 2014, and far short of the 7.5% assumed long-term rate of return.

- At December 31, 2015, State System employees represented 4.69% of active SERS members.

PSERS

- In fiscal year 2015/16, PSERS also continued its increases in employer pension contribution rates. The employer-paid PSERS rates for State System employees rose nearly 21% in 2015/16, after increases of more than 26% in 2014/15 and more than 37% in 2013/14. The rates have increased by an additional 16.8% in 2016/17, bringing the **contribution rate to 15.015%** of employees' eligible salaries. This rate comprises a 14.6% rate for pension costs and 0.415% for premium assistance payments, a health care benefit given to retirees who meet certain eligibility requirements. This rate is estimated to increase an additional 6.7% in fiscal year 2017/18.

- As of June 30, 2015, the PSERS **net pension liability** was $43.3 billion, compared to $39.6 billion at June 30, 2014.

- PSERS plan **fiduciary net position** as a percentage of the total pension liability was approximately 54.4% at June 30, 2015, compared to 57.2% at June 30, 2014.

- At June 30, 2015, State System employees represented less than 0.2% of reported member salaries covered under PSERS.

ARP
The contribution rate for the ARP, a defined contribution pension plan, remains unchanged at 9.29% of employees' eligible salaries. There is no employer pension liability associated with the ARP.

Compensation Costs
All collective bargaining agreements have expired.

The Commonwealth has reached a tentative three-year labor agreement with the American Federation of State, County and Municipal Employees (**AFSCME**), which applies to State System AFSCME employees. The agreement provides general pay increases of 2.75% on October 1, 2016; 2% on July 2, 2017; and 2.5% on July 1, 2018; with longevity increases in January 2018 and 2019. In addition, the agreement increases employee contributions to the Pennsylvania Employee Benefit Trust Fund (PEBTF), which administers the health care plan for Commonwealth employees, including AFSCME employees. In conjunction with the collective bargaining process, the PEBTF approved changes to the health plan design for active and retired employees that introduce deductibles for certain in-network services and increase copays for office and emergency room visits and prescription drugs. The Commonwealth projects that these changes will help to ensure the continued financial stability of the PEBTF fund and bring the Commonwealth's benefits into closer alignment with those offered by other public and private sector employers. It is estimated that the net amount of these contract changes will cost the State System **$54.3 million** in additional salary and benefits costs through June 30, 2020.

The Association of Pennsylvania State College and University Faculties (**APSCUF**), which represents all faculty and coaches, has been working under the terms of a contract that expired June 30, 2015. In September 2016, after more than a year of negotiations with the State System, 93% of the 82% of faculty members, and 94% of the 97% of coaches, who submitted a ballot voted to authorize union leaders to call a **strike** if and when it is considered necessary. Although there has never been a strike by State System faculty or coaches, APSCUF has previously held strike authorization votes in 1999, 2003, 2007, and 2012. The short- or long-term financial impact of a strike on the universities and their students cannot be estimated but could be severely detrimental. As of the date of these financial statements, negotiations are continuing.

Negotiations continue but remain unresolved with the State College and University Professional Association (**SCUPA**), the Security Police and Fire Professionals of America (**SPFPA**), and the Office and Professional Employees International Union (**OPEIU**); however, these bargaining units are continuing to work under the terms of their most recent contracts.

Effective January 2016, the State System implemented plan design changes to the health care program for **nonrepresented employees** and employees of SPFPA and OPEIU. The changes increase employee contributions for health care through new provisions for deductibles and coinsurance and higher copays. These design changes will reduce health care costs by an estimated $3.5 million in fiscal year 2016/17.

In addition, nonrepresented employees and employees of SPFPA, OPEIU, and SCUPA hired on or after January 16, 2016, will be ineligible to participate in the State System's retiree health care plan upon their retirement. The estimated savings have not yet been calculated, but this change is expected to help ensure that a State System university education will remain affordable for future students and their families.

Performance Funding
Calls for increased accountability among colleges and universities have come from various sources across the nation. The State System has more than 15 years of experience in this area, having introduced performance funding in 2000/01 and having grown it into a national model. The State System continues to be one of the few public university systems in the nation to voluntarily implement this type of performance program.

State System universities have "earned" over **$455 million** through performance since this program's inception. This initiative has resulted in increased graduation and retention rates, especially among underrepresented student groups; greater diversity among both the student population and all employee groups—executives, faculty, and professional staff; and higher fundraising results for the universities despite a still sluggish economy.

The State System is committed to funding its performance program at a level equal to 2.4% of the E&G budget. The Board allocated **$39.06 million** in performance funding for fiscal year 2016/17, an increase of $0.6 million over fiscal year 2015/16.

Pricing Flexibility Pilot Program

The State System's founding legislation and Board policies provide the framework under which the Board annually sets tuition and university councils of trustees set university fees. In 2014, the Board established a **Pricing Flexibility Pilot Program** to allow State System universities to develop more market-driven pricing practices and assume the financial and operational risks of doing so. This requires Board approval of particular exceptions to existing policy. To date, approval has been granted for 27 pricing pilots, and 20 of the pilots have been implemented, while five are scheduled to be implemented in fall 2016.

The pricing pilots vary among the universities, and include differential pricing for high cost/high demand programs or courses, elimination of block tuition for 12–18 credits, reduced tuition for military, reduced tuition for off-campus sites, and/or variable out-of-state student pricing. The intent of the pricing pilots is to increase enrollment, graduation, and revenue, as well as to generate more funding for need-based financial aid. In addition, this new practice is part of the Board's efforts to strike a better balance between State System coordination and more local decision-making.

Cheyney University of Pennsylvania

Cheyney University ended fiscal year 2015/16 with a $4.3 million loss in E&G activity and a $1.4 million loss in Auxiliary activity, for a total unrestricted loss of $5.7 million, bringing the university's unrestricted net position deficit to $17.6 million at June 30, 2016 (excluding unfunded pension, postretirement, and compensated absences liabilities). This follows a $5.5 million loss in unrestricted funds in fiscal year 2014/15 and a $4.2 million loss in fiscal year 2013/14. Gross tuition and fees dropped $2.3 million, from $9.8 million in fiscal year 2014/15 to $7.5 million in fiscal year 2015/16. Auxiliary revenue dropped $2.1 million, from $7.4 million in fiscal year 2014/15 to $5.3 million in fiscal year 2015/16.

The university's preliminary projections reflect a $10.4 million loss in E&G activity and a $3.8 million loss in Auxiliary activity in fiscal year 2016/17, which would bring the university's unrestricted net position to a projected deficit of $31.8 million (excluding unfunded pension, postretirement, and compensated absences liabilities) at June 30, 2017. Cheyney's fall 2016 enrollment was 739 students, approximately the same as its fall 2015 enrollment, but a 31% decrease from the 1,022 students enrolled in fall 2014.

As of June 30, 2016, the university has borrowed $19 million from the State System pooled investment account; without this line of credit, the university's unrestricted E&G and Auxiliary cash balances would be a negative $15.4 million. To ensure the security of cash inflows that have been restricted as to purpose by the donor or grantor, separate bank and investment accounts have been established for these funds, and access to them requires the approval of the Office of the Chancellor.

As detailed in the disclosures attached to these financial statements under Note (13), *Contingencies and Commitments*, Cheyney University is awaiting a response from the U.S. Department of Education (ED) to the university's voluntary self-reporting to the ED in August 2015 that $29.6 million of federal student financial aid was improperly administered and delivered in fiscal years 2011/12, 2012/13, and 2013/14, covering almost 4,400 student records. The State System has been engaged with the ED since reporting these findings. In addition, in January 2016, the U.S. Department of Justice (DOJ) notified the State System that it was investigating the application and use of federal student financial aid by Cheyney University and the oversight of the university by the State System. The DOJ requested that the university and State System preserve and produce certain documents. The State System has fully complied with DOJ's request. No action has been taken at this point by the DOJ, and the possible resulting outcomes from the investigation are uncertain until communication is received from the DOJ.

The third party hired by the State System to administer the university's federal financial aid programs for 2014/15, 2015/16, and 2016/17 has successfully implemented processes to ensure that the university's administrative policies and procedures, information systems, and data are properly aligned and integrated to support the award and distribution of financial aid. The State System believes that these efforts will ensure that Cheyney University's federal student aid programs are administered in compliance with federal regulations.

One consequence of the university's past deficiencies in administering federal student aid is that in September 2015 the ED placed the university on Heightened Cash Monitoring 2 (HCM2) status, meaning that the university does not receive federal student financial aid funds in advance, but must use its own cash to grant federal financial aid to its students and then request reimbursement from the ED. After demonstrating compliance with HCM2 requirements, the university received its spring 2016 federal student aid funds in July, but has not yet received its fall 2016 federal student aid funds. The delay in receipt of funds is causing further pressure on the university's severe cash shortage.

As further detailed in Note (13), Cheyney University was placed on probation by the Middle States Commission on Higher Education (Middle States) in November 2015, jeopardizing its accreditation. The university has been given two years to address the deficiencies noted by Middle States. In September 2016, the university submitted the first required monitoring report, documenting its plan for remediation. As part of this plan, the university has contracted with a third party to administer its information technology systems and has begun the outsourcing of its administrative functions, including finance, human resources, and facilities, to nearby West Chester University. The State System, through the Office of the Chancellor, continues to provide oversight to Cheyney's leadership in an attempt to stabilize its financial condition and implement a comprehensive plan that includes timely and accurate financial aid processing, increasing student enrollment, restructuring course offerings, revitalizing its academic program array, and right-sizing personnel and facilities.

Moody's Rating and Outlook
In August 2016, Moody's Investors Service, Inc. (Moody's), reaffirmed the State System's **bond rating of Aa3**, but revised the outlook from *negative* to *stable*, "reflecting demonstrated ability to adjust to ongoing enrollment pressures combined with a more predictable near term state funding environment with the budget enactments from the Commonwealth of Pennsylvania." In its August 10, 2016, *Credit Opinion*, Moody's stated:

> *PASSHE's Aa3 rating reflects its large scale as a public university system of 14 campuses located throughout the Commonwealth of Pennsylvania, strong liquidity and very good system management and governance addressing system-wide revenue and expense pressures, and significant debt principal repayments scheduled over the next two years. Also incorporated is our expectation of stabilizing enrollment, continued net tuition revenue growth, and good cash flow. Offsetting factors include high leverage including significant pension and other post-retirement benefit liabilities, and rising expenses in part driven by these employee benefits. Also, some member universities have significant financial and enrollment challenges which will likely be addressed over a multi-year period.*

Moody's details as State System **challenges** high leverage, with $2.4 billion of total debt, including foundation student housing; limitations to cost management efforts because of the high percentage of staff, including faculty, that are subject to collective bargaining agreements; significant pension and OPEB liabilities with required contributions; pressured operations with thinning cash flow; and management of enrollment and financial challenges at certain campuses.

Moody's details as State System **strengths** its substantial balance sheet reserves; its significant scale as one of the nation's largest higher education systems; effective System governance and management, including strong fiscal oversight and debt management; positive cash flow; and modest near-term debt plans with rapidly amortizing debt.

Moody's predicts that a ratings upgrade could result from consistently stronger operating performance and cash flow generation, significantly strengthened and growing enrollment across the State System, and a restructuring of postretirement benefits to significantly reduce the OPEB liability and pension costs. Conversely, a ratings downgrade could result from a decrease in unrestricted liquidity, the inability to manage expense growth to accommodate rising employee benefit costs, continued enrollment declines despite stabilization of college-age population statewide, prolonged inability to address challenges at struggling campuses, and a weakening of the Commonwealth's credit profile.

For ***further information*** *about these financial statements, contact Pennsylvania's State System of Higher Education, Accounting Office, 2986 North Second Street, Harrisburg, PA 17110.*

Pennsylvania's State System of Higher Education

Balance Sheet

(dollars in thousands)

Assets and Deferred Outflows of Resources

	June 30, 2016	June 30, 2015
Current Assets		
Cash and cash equivalents	$ 20,519	$ 20,314
Short-term investments	649,417	534,596
Accounts receivable, students, net of allowance for doubtful accounts of $30,049 in 2016 and $30,578 in 2015	42,765	44,397
Accounts receivable, other	30,827	24,742
Governmental grants and contracts receivable	16,986	23,121
Inventories	2,958	3,569
Prepaid expenses	14,031	11,723
Current portion of loans receivable, net	8,638	8,681
Due from component units	23,015	26,393
Other current assets	2,646	2,366
Total Current Assets	811,802	699,902
Noncurrent Assets		
Restricted cash and cash equivalents	25	131
Endowment investments	29,596	30,270
Other long-term investments	676,630	748,621
Loans receivable, net	32,474	33,505
Due from component units	9,160	10,324
Capital Assets:		
Land	32,360	32,360
Buildings, including improvements	2,213,463	2,056,185
Improvements other than buildings	285,136	274,779
Equipment and furnishings	470,347	454,128
Library books	81,314	81,940
Construction in progress	80,012	99,144
	3,162,632	2,998,536
Less accumulated depreciation	(1,509,343)	(1,409,352)
Capital assets, net	1,653,289	1,589,184
Other noncurrent assets	1,873	1,497
Total Noncurrent Assets	2,403,047	2,413,532
Total Assets	3,214,849	3,113,434
Deferred Outflows of Resources	191,221	73,556
Total Assets and Deferred Outflows of Resources	$ 3,406,070	$ 3,186,990

See accompanying notes to financial statements.

Pennsylvania's State System of Higher Education

Balance Sheet

(dollars in thousands)

Liabilities, Deferred Inflows of Resources, and Net Position

	June 30, 2016	June 30, 2015
Current Liabilities		
Accounts payable and accrued expenses	$ 162,520	$ 154,790
Unearned revenue	50,448	50,309
Deposits	40,691	45,974
Current portion of workers' compensation liability	4,419	4,686
Current portion of compensated absences liability	9,990	10,670
Current portion of capitalized lease obligations	3,476	3,364
Current portion of bonds payable	62,885	55,890
Due to component units	10,693	10,562
Other current liabilities	77,241	39,235
Total Current Liabilities	422,363	375,480
Noncurrent Liabilities		
Unearned revenue	4,615	4,173
Workers' compensation liability, net of current portion	17,672	17,864
Compensated absences liability, net of current portion	105,433	103,970
Capitalized lease obligations, net of current portion	45,170	48,228
Bonds payable, net of current portion	779,705	744,565
Postretirement benefits liability	1,106,643	1,058,749
Net pension liability	938,637	798,744
Other noncurrent liabilities	77,652	78,409
Total Noncurrent Liabilities	3,075,527	2,854,702
Total Liabilities	3,497,890	3,230,182
Deferred Inflows of Resources	30,162	15,311
Net Position		
Net investment in capital assets	709,271	700,280
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	32,505	29,696
Student loans	4,538	4,034
Other	3,961	7,563
Expendable:		
Scholarships and fellowships	21,074	16,537
Research	248	1,330
Capital projects	37,406	20,270
Other	14,723	18,643
Unrestricted	(945,708)	(856,856)
Total Net Position	(121,982)	(58,503)
Total Liabilities, Deferred Inflows of Resources, and Net Position	$ 3,406,070	$ 3,186,990

See accompanying notes to financial statements.

Pennsylvania's State System of Higher Education

Statement of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30, 2016 and 2015

(dollars in thousands)

	2016		2015	
Operating Revenues				
Tuition and fees	$ 1,065,416		$ 1,050,135	
Less discounts and allowances	(226,381)		(233,562)	
Net tuition and fees		$ 839,035		$ 816,573
Governmental grants and contracts:				
Federal		37,519		34,393
State		104,650		104,967
Local		4,595		4,094
Nongovernmental grants and contracts		8,758		7,208
Sales and services		37,660		41,885
Auxiliary enterprises, net of discounts of $1,782 in 2016 and $1,749 in 2015		323,358		324,007
Other revenues, net		8,446		10,736
Total Operating Revenues		1,364,021		1,343,863
Operating Expenses				
Instruction		749,290		739,633
Research		6,304		5,757
Public service		39,381		37,504
Academic support		184,037		179,055
Student services		184,675		180,958
Institutional support		257,261		248,507
Operations and maintenance of plant		159,904		153,508
Depreciation		121,683		119,652
Student aid		79,136		72,948
Auxiliary enterprises		253,786		255,742
Total Operating Expenses		2,035,457		1,993,264
Operating Loss		(671,436)		(649,401)
Nonoperating Revenues (Expenses)				
State appropriations, general and restricted		433,389		412,751
Commonwealth on-behalf pension contributions		7,952		6,592
Pell grants		138,575		145,658
Investment income, net of related investment expense of $354 in 2016 and $223 in 2015		23,979		31,010
Unrealized gain (loss) on investments		2,551		(13,055)
Gifts for other than capital purposes		28,544		16,557
Interest expense on capital asset-related debt		(33,920)		(36,577)
Loss on disposal/acquisition of assets		(20,490)		(9,622)
Other nonoperating revenue		4,018		1,554
Net Nonoperating Revenues		584,598		554,868
Loss before other revenues		(86,838)		(94,533)
State appropriations, capital		15,714		13,610
Capital gifts and grants		7,620		4,145
Additions to permanent endowments		25		105
Decrease in Net Position		(63,479)		(76,673)
Net position—beginning of year		(58,503)		739,048
Restatement for July 1, 2014, pension liability and related expense				(720,878)
Net position—beginning of year, restated				18,170
Net position—end of year		$ (121,982)		$ (58,503)

See accompanying notes to financial statements.

Pennsylvania's State System of Higher Education

Statement of Cash Flows
For the Years Ended June 30, 2016 and 2015
(dollars in thousands)

	2016	2015
Cash Flows from Operating Activities		
Tuition and fees	$ 840,059	$ 816,148
Grants and contracts	160,543	151,234
Payments to suppliers for goods and services	(442,726)	(422,825)
Payments to employees	(1,304,770)	(1,288,967)
Loans issued to students	(5,374)	(7,763)
Loans collected from students	6,442	7,034
Student aid	(79,503)	(74,020)
Auxiliary enterprise charges	324,031	322,451
Sales and services	37,044	41,694
Other receipts (payments)	42,606	4,709
Net cash used in operating activities	(421,648)	(450,305)
Cash Flows from Noncapital Financing Activities		
State appropriations	433,389	412,751
Gifts and nonoperating grants for other than capital purposes	162,524	162,424
PLUS, Stafford, and other loans receipts (non-Perkins)	1,144,667	893,464
PLUS, Stafford, and other loans disbursements (non-Perkins)	(1,144,646)	(893,505)
Agency transactions, net	(3,598)	1,843
Other	4,018	1,555
Net cash provided by noncapital financing activities	596,354	578,532
Cash Flows from Capital Financing Activities		
Proceeds from capital debt and leases	86,798	106,909
Capital appropriations	15,714	13,607
Capital grants and gifts received	4,184	3,369
Proceeds from sales of capital assets	101	194
Purchases of capital assets	(115,657)	(96,657)
Principal paid on capital debt and leases	(110,963)	(157,849)
Interest paid on capital debt and leases	(43,450)	(45,429)
Net cash used in capital financing activities	(163,273)	(175,856)
Cash Flows from Investing Activities		
Proceeds from sales and maturities of investments	20,624,557	17,772,937
Interest on investments	23,672	30,866
Purchase of investments	(20,659,563)	(17,784,282)
Net cash provided by investing activities	(11,334)	19,521
Net Increase in Cash and Cash Equivalents	99	(28,108)
Cash and cash equivalents—beginning of year	20,445	48,553
Cash and cash equivalents—end of year	$ 20,544	$ 20,445

See accompanying notes to financial statements.

Pennsylvania's State System of Higher Education

Statement of Cash Flows
For the Years Ended June 30, 2016 and 2015
(dollars in thousands)

	2016	2015
Reconciliation of Operating Loss to Net Cash Used in Operating Activities		
Operating loss	$ (671,436)	$ (649,401)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation expense	121,683	119,652
Expenses paid by Commonwealth or donor	7,062	6,032
Effect of changes in operating assets and liabilities:		
Receivables, net	7,614	898
Inventories	611	(98)
Other assets	(4,180)	(12,746)
Accounts payable	(5,119)	135
Unearned revenue	602	(1,332)
Student deposits	(1,148)	(173)
Compensated absences	783	(82)
Loans to students and employees	1,067	(728)
Other liabilities	120,813	87,538
Net cash used in operating activities	$ (421,648)	$ (450,305)
Noncash Activities		
Capital assets included in payables	$ 14,602	$ 5,902
Capital assets acquired through capital leases or assumption of debt	$ 56,131	$ 1,161
Capital assets acquired by gift or appropriation	$ 4,391	$ 1,190
Debt assumed in acquisition of capital assets	$ 71,299	$ -
Like-kind exchanges	$ 4	$ 15
Commonwealth on-behalf contributions to PSERS	$ 7,952	$ 6,592

See accompanying notes to financial statements.

Pennsylvania's State System of Higher Education

Component Units Statement of Financial Position

(dollars in thousands)

	June 30, 2016	(Restated) June 30, 2015
Assets		
Cash and cash equivalents	$ 147,696	$ 141,796
Accounts receivable	7,014	6,926
Contributions/pledges receivable	18,540	16,568
Due from universities	12,128	10,711
Prepaid expenses	2,377	3,162
Inventories	7,340	8,701
Short-term investments	71,077	70,229
Investments	398,311	464,466
Capital assets:		
Land	32,471	31,724
Buildings	1,308,775	1,282,094
Building improvements	18,538	19,313
Improvements other than buildings	9,023	10,370
Equipment and furnishings	89,355	93,383
Construction in progress	50,587	99,614
	1,508,749	1,536,498
Less accumulated depreciation	(276,262)	(287,022)
Capital assets, net	1,232,487	1,249,476
Other assets	114,891	131,723
Total Assets	$ 2,011,861	$ 2,103,758
Liabilities		
Accounts payable and accrued expenses	$ 32,539	$ 31,117
Deferred revenue	10,682	10,221
Interest payable	11,091	10,402
Annuity liabilities	7,012	7,538
Due to universities	31,899	36,417
Deposits payable	22,409	22,140
Interest rate swap agreements	84,662	60,596
Capitalized leases	28,428	29,151
Bonds payable	1,131,757	1,232,289
Notes payable	307,299	296,239
Other liabilities	10,819	20,046
Total Liabilities	1,678,597	1,756,156
Net Assets		
Unrestricted	(13,833)	9,873
Temporarily restricted	97,878	95,560
Permanently restricted	249,219	242,169
Total Net Assets	333,264	347,602
Total Liabilities and Net Assets	$ 2,011,861	$ 2,103,758

See accompanying notes to financial statements.

Pennsylvania's State System of Higher Education

Component Units Statement of Activities
For the Years Ended June 30, 2016 and 2015
(dollars in thousands)

	2016	(Restated) 2015
Revenues and Gains		
Contributions	$ 40,443	$ 38,537
Sales and services	47,255	47,792
Student fees	33,853	34,351
Grants and contracts	11,162	11,591
Rental income	171,073	169,980
Investment income, gains, and losses	9,365	17,115
Other revenues and gains	37,430	16,092
Total Revenues and Gains	350,581	335,458
Expenses and Losses		
Program services:		
Scholarships and grants	16,456	14,106
Student activities and programs	31,020	31,830
University stores	29,141	30,687
Housing	157,866	162,946
Other university support	21,533	16,313
Other programs	19,986	16,448
Management and general	34,626	28,667
Fundraising	10,821	9,908
Other expenses and losses	43,470	16,796
Total Expenses and Losses	364,919	327,701
Change in Net Assets	(14,338)	7,757
Net assets—beginning of year	347,602	357,765
Restatement for July 1, 2015, change in reporting entity	-	(17,920)
Net assets—beginning of year, restated	347,602	339,845
Net assets—end of year	$ 333,264	$ 347,602

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

Years Ended June 30, 2016 and 2015

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Pennsylvania's State System of Higher Education (State System) is a body corporate and politic, created by the State System of Higher Education Act of November 12, 1982, P.L. 660, No. 188, as amended (Act 188). The State System is a component unit of the Commonwealth of Pennsylvania (Commonwealth) and is governed by a Board of Governors (Board), as provided for in Act 188. The State System comprises the 14 universities and the Office of the Chancellor.

Reporting Entity

The State System functions as a Business Type Activity, as defined by the Governmental Accounting Standards Board (GASB).

Certain affiliated organizations are included in the State System's financial statements as discretely presented component units. Some of the organizations, such as university student associations, are included because the Board has oversight responsibility for the organizations. The criteria used in determining the organizations for which the State System has oversight responsibility include financial interdependency, the ability to select members of the governing body, the ability to designate management, the ability to influence operations significantly, and accountability for fiscal matters. Other affiliated organizations for which the Board does not have oversight responsibility, such as university foundations and alumni associations, are included when the economic resources received or held by the organization are entirely or almost entirely for the direct benefit of the State System, the activity of the organization is significant to the State System universities, and the State System historically has received a majority of these economic resources. Neither the State System nor its universities control the timing or amount of receipts from these organizations.

During fiscal year 2015/16, Mansfield University of Pennsylvania disaffiliated the Mansfield University Foundation, Inc., a former component unit. The combined component unit financial statements for fiscal year 2014/15 have been restated accordingly and result in a reduction of $18,669,000 of component unit assets, and a reduction of $357,000 of component unit liabilities, which, when combined with the fiscal year 2014/15 respective change in net assets of $392,000, result in a restatement of beginning net assets of $17,920,000.

The State System does not consider any of its component units to be major, and has aggregated all component unit information into a separate set of financial statements. Information on individual component units can be obtained by contacting the respective universities.

Transactions between the universities and the Office of the Chancellor have been eliminated in the accompanying financial statements.

Measurement Focus, Basis of Accounting, and Basis of Presentation

The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP), as prescribed by GASB. The economic resources measurement focus reports all inflows, outflows, and balances that affect an entity's net assets. Under the accrual basis of accounting, revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

The accompanying financial statements of the component units, which are all private nonprofit organizations, are reported in accordance with

Financial Accounting Standards Board (FASB) requirements, including FASB Statement No. 117, *Financial Reporting for Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications for these differences have been made to the component units' financial information presented herein.

Operating Revenues and Expenses
The State System records tuition; all academic, instructional, and other student fees; student financial aid; auxiliary activity; corporate partnerships; and revenue from cogeneration sales as operating revenue. In addition, governmental and private grants and contracts in which the grantor receives equal value for the funds given to the university are recorded as operating revenue. All expenses, with the exception of interest expense, loss on investments, loss on the disposal of assets, and extraordinary expenses, are recorded as operating expenses. Appropriations, gifts, investment income, capital grants, gains on investments, gains on the disposal of assets, parking and library fines, and governmental and private research grants and contracts in which the grantor does not receive equal value for the funds given to the university are reported as nonoperating revenue.

Deferred Outflows and Deferred Inflows of Resources
The balance sheet reports separate sections for *Deferred Outflows of Resources* and *Deferred Inflows of Resources*.

Deferred Outflows of Resources, reported after *Total Assets,* is defined by GASB as a consumption of net position that applies to future periods. The expense is recognized in the applicable future period(s). *Deferred Inflows of Resources,* reported after *Total Liabilities,* is defined by GASB as an acquisition of net position that applies to future periods. The revenue is recognized in the applicable future period(s).

Transactions are classified as deferred outflows of resources or deferred inflows of resources only when specifically prescribed by GASB standards.

The State System is required to report the following as Deferred Outflows of Resources or Deferred Inflows of Resources.

- Deferred gain or loss on bond refundings, which results when the carrying value of a refunded bond is greater or less than its reacquisition price. The difference is deferred and amortized over the remaining life of the old bond or the life of the new bond, whichever is shorter.
- For defined benefit pension plans: the difference between expected (actuarial) and actual experience, changes in actuarial assumptions, net difference between projected (actuarial) and actual earnings on pension plan investments, changes in the State System's proportion of expenses and liabilities to the pension as a whole, differences between the State System's pension contributions and its proportionate share of contributions, and State System pension contributions subsequent to the pension valuation measurement date.

Net Position
Net position is the residual of Assets, plus Deferred Outflows of Resources, less Liabilities, less Deferred Inflows of Resources. The State System maintains the following classifications of net position.

Net investment in capital assets: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, repair, or improvement of those assets.

Restricted—nonexpendable: The portion of net position subject to externally imposed conditions requiring that it be maintained by the State System in perpetuity.

Restricted—expendable: The portion of net position use of which is subject to externally imposed conditions that can be fulfilled by the actions of the State System or by the passage of time.

Unrestricted: All other categories of net position. Unrestricted net position may be designated for specific purposes by the Board.

When both restricted and unrestricted funds are available for expenditure, the decision as to which funds are used first is left to the discretion of the universities.

Cash Equivalents and Investments
The State System considers all demand and time deposits and money market funds to be cash

equivalents. Investments purchased are stated at fair value. Investments received as gifts are recorded at their fair value or appraised value as of the date of the gift. The State System classifies investments as short-term when they are readily marketable and intended to be converted to cash within one year.

Accounts and Loans Receivable

Accounts and loans receivable consist of tuition and fees charged to current and former students and amounts due from federal and state governments in connection with reimbursements of allowable expenditures made pursuant to grants, contracts, and other miscellaneous sources.

Accounts and loans receivable are reported at net realizable value. Accounts are written off when they are determined to be uncollectible based upon management's assessment of individual accounts. The allowance for doubtful accounts is estimated based upon the universities' historical losses and periodic review of individual accounts.

Inventories

Inventories are stated at the lower of cost or market, with cost being determined principally on the weighted average method.

Capital Assets

Land and buildings at the 14 university campuses acquired or constructed prior to its creation on July 1, 1983, are owned by the Commonwealth and made available to the universities of the State System. Since the State System neither owns such assets nor is responsible to service associated bond indebtedness, no value is ascribed thereto in the accompanying financial statements. Likewise, no value is ascribed to the portion of any land or buildings acquired or constructed using capital funds appropriated by the Commonwealth after June 30, 1983, and made available to the universities.

All assets with a purchase cost, or fair value if acquired by gift, in excess of $5,000, with an estimated useful life of two years or greater, are capitalized. Buildings, portions of buildings, and capital improvements acquired or constructed by the universities after June 30, 1983, through the expenditure of university funds or the incurring of debt are stated at cost less accumulated depreciation.

Equipment and furnishings are stated at cost less accumulated depreciation. Library books are capitalized on a composite basis in the year of purchase. Assets under capital leases are recorded at the lower of the present value of the minimum lease payments or the fair value of the asset. The State System provides for depreciation on the straight-line method over the estimated useful lives of the related assets. Buildings and improvements are depreciated over useful lives ranging from 10 to 40 years. Equipment and furnishings are depreciated over useful lives ranging from 3 to 10 years. Library books are depreciated over 10 years. Amortization of assets under capital leases is included in depreciation expense. Normal repair and maintenance expenditures are not capitalized because they neither add to the value of the property nor materially prolong its useful life.

The State System does not capitalize collections of art, rare books, historical items, etc., as they are held for public exhibition, education, or research rather than financial gain.

Impairment of Capital Assets

Management reviews capital assets for impairment whenever events or changes in circumstances indicate that the service utility of an asset has declined significantly and unexpectedly. Any write-downs due to impairment are charged to operations at the time impairment is identified. No write-down of capital assets was required for the years ended June 30, 2016 and 2015.

Unearned Revenue

Unearned revenue includes amounts for tuition and fees, grants, corporate sponsorship payments, and certain auxiliary activities received prior to the end of the fiscal year but earned in a subsequent accounting period.

Compensated Absences

The estimated cost of future payouts of annual leave and sick leave that employees have earned for services rendered, and which the employees may be entitled to receive upon termination or retirement, is recorded as a liability.

Pension Plans

Employees of the State System enroll in one of three available retirement plans immediately upon employment. The Commonwealth of Pennsylvania State Employees' Retirement System (SERS) and the Public School Employees' Retirement System

(PSERS) are governmental cost-sharing multiple-employer defined benefit plans. The Alternative Retirement Plan (ARP) is a defined contribution plan administered by the State System.

Scholarships and Waivers
In accordance with a formula prescribed by the National Association of College and University Business Officers (NACUBO), the State System allocates the cost of scholarships, waivers, and other student financial aid between *Discounts and allowances* (netted against tuition and fees) and *Student aid expense*. Scholarships and waivers of room and board fees are reported in Auxiliary enterprises. The cost of tuition waivers granted to employees is reported as employees' benefits expense.

Income Taxes
The State System and its member universities are tax-exempt; accordingly, no provision for income taxes has been made in the accompanying financial statements.

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, disclosures 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 amounts in the prior period presented have been reclassified to conform to the current period financial statement presentation. These reclassifications have no effect on the previously reported net position or changes therein.

New Accounting Standards
The State System has implemented GASB Statement No. 72, *Fair Value Measurement and Application*. This statement addresses accounting and financial reporting issues related to fair value measurements. In accordance with Statement No. 72, the State System has classified its investments as *Level 1*, *Level 2*, or *Level 3*, to indicate the degree of certainty around the assets' underlying values (note 2).

In June 2015, GASB issued Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, and Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. These statements establish new accounting and financial reporting requirements for governments whose employees are provided with OPEB (other postemployment benefits), as well as for certain nonemployer governments that have a legal obligation to provide financial support for OPEB provided to the employees of other entities. These statements will require the State System to record its postretirement health care liability in its entirety: in its most recent actuarial valuation dated July 1, 2014, the State System's accrued postretirement health care liability, as calculated by the actuaries, was $1,194,849,000, but under current GASB requirements, the amount recorded on the balance sheet as a liability at June 30, 2016, was $1,106,643,000. The State System expects that the amount recorded on the balance sheet as a postretirement health care liability will increase when Statement No. 75 is implemented, but the amount cannot be calculated until a new actuarial valuation is performed under the new standards. Furthermore, Statement No. 75 will require that the State System record the liability for its employees who participate in the Commonwealth's Retired Employees Health Plan (REHP). Under current GASB standards, the State System does not report a share of the REHP's unfunded liability since the REHP is a multiple-employer cost-sharing plan administered by the Pennsylvania Employee Benefits Trust Fund (PEBTF). The amount that the State System will have to record as its share of the liability when Statement No. 75 becomes effective is unknown; however, the amount is expected to have a material negative effect on the State System's balance sheet. The provisions in Statement No. 74 are effective for fiscal years beginning after June 15, 2016; the provisions in Statement No. 75 are effective for fiscal years beginning after June 15, 2017.

In December 2015, GASB issued Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*. Statement No. 78 excludes certain pensions from the provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*. The State System has determined that Statement No. 78 does not apply to its pension plans and has no effect on its financial statements.

In December 2015, GASB issued Statement No. 79, *Certain External Investment Pools and Pool Participants.* Statement No. 79 applies to arrangements that commingle the moneys of more than one legally separate entity and invest on the participants' behalf in an investment portfolio. The State System has determined that Statement No. 79 does not apply to its investments and has no effect on its financial statements.

In June 2016, GASB issued Statement No. 80, *Blending Requirements for Certain Component Units—an amendment of GASB Statement No. 14.* Statement No. 80 requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government (university) is the sole corporate member. The State System has determined that Statement No. 80 does not apply to its component units and has no effect on its financial statements.

In March 2016, GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements.* Statement No. 81 provides recognition and measurement guidance for gifts received from donors who have transferred the gifts to an intermediary to hold and administer for the government (university) and at least one other beneficiary. An example of a split-interest agreement is a charitable remainder trust. The provisions in Statement No. 81 are effective for reporting periods beginning after December 15, 2016. The State System has determined that Statement No. 81 applies to a small number of certain local university investments and will have an immaterial effect on its financial statements.

In March 2016, GASB issued Statement No. 82, *Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73.* Statement No. 82 addresses technical issues related to previous GASB guidance on pensions. The State System has determined that Statement No. 82 will have no effect on its financial statements.

(2) Deposits and Investments

On June 30, 2016 and 2015, the carrying amount of the State System's demand and time deposits and certificates of deposit for all funds was $20,558,000 and $20,458,000, respectively, compared to bank balances of $20,280,000 and $19,970,000, respectively. The difference is caused primarily by items in transit. Of the bank balances, $4,214,000 and $3,200,000, respectively, were covered by federal government depository insurance or collateralized by a pledge of U.S. Treasury obligations held by Federal Reserve banks in the name of the banking institutions; $608,000 and $660,000, respectively, were uninsured and uncollateralized; and $15,458,000 and $16,110,000, respectively, were uninsured and uncollateralized but covered under the collateralization provisions of the Commonwealth of Pennsylvania Act 72 of 1971, as amended. Act 72 allows banking institutions to satisfy the collateralization requirements by pooling eligible investments to cover total public funds on deposit in excess of federal insurance. Such pooled collateral is pledged with the financial institutions' trust departments.

Board of Governors' Policy 1986-02-A: *Investment*, authorizes the State System to invest in obligations of the U.S. Treasury, repurchase agreements, commercial paper, certificates of deposit, banker's acceptances, U.S. money market funds, municipal bonds, corporate bonds, collateralized mortgage obligations (CMOs), asset-backed securities, and internal loan funds. Restricted nonexpendable funds and amounts designated by the Board or university trustees may be invested in the investments described above as well as in corporate equities and approved pooled common funds. For purposes of convenience and expedience, universities use local financial institutions for activities such as deposits of cash. In addition, universities may accept gifts of investments from donors as long as risk is limited to the investment itself. Restricted gifts of investments fall outside the scope of the investment policy.

In keeping with its legal status as a system of public universities, the State System recognizes a fiduciary responsibility to invest all funds prudently and in accordance with ethical and prevailing legal standards. Investment decisions are intended to minimize risk while maximizing asset value. Adequate liquidity is maintained so that assets can be held to maturity. High quality investments are preferred. Reasonable portfolio diversification is pursued to ensure that no single security or investment or class of securities or investments will have a disproportionate or significant impact on the total portfolio. Investments may be made in U.S. dollar-denominated debt of high quality U.S. and non-U.S. corporations. Investment performance is monitored on a frequent and regular basis to ensure that objectives are attained and guidelines are followed.

Safety of principal and liquidity are the top priorities for the investment of the State System's operating funds. Within those guidelines, income optimization is pursued. Speculative investment activity is not allowed: this includes investing in asset classes such as commodities, futures, short-sales, equities, real or personal property, options, venture capital investments, private placements, letter stocks, and unlisted securities.

The State System's operating funds are invested and reinvested in the following types of instruments with qualifications as provided. (See Board of Governors' Policy 1986-02-A: *Investment*, for a complete list of and more details on permissible investments and associated qualifications.)

Investment Categories	Qualifications/Moody's Ratings Requirements
United States Government Securities	Together with repurchase agreements, must comprise at least 20% of the market value of the fund.
Repurchase Agreements	Underlying collateral must be direct obligations of the U.S. Treasury and be in the State System's or its agent's custody.
Commercial Paper	P-1 and P-2 notes only, with no more than 5% and 3%, respectively, of the market value of the fund invested in any single issuer. Total may not exceed 20% of the market value of the fund.
Municipal Bonds	Bonds must carry long-term debt rating of A or better. Total may not exceed 20% of the market value of the fund.
Corporate Bonds	15% must carry long-term debt rating of A or better; 5% may be rated Baa2 or better. Total may not exceed 20% of the market value of the fund.
Collateralized Mortgage Obligations (CMOs)	Must be rated Aaa and guaranteed by the U.S. government. Total may not exceed 20% of the market value of the fund.
Asset-Backed Securities	Must be Aaa rated. Total may not exceed 20% of the market value of the fund, with no more than 5% invested in any single issuer.
System Investment Fund Loans (university loans and bridge notes)	Total may not exceed 20% of the market value of the fund, and loan terms may not exceed 5 years.

CMO Risk: CMOs sometimes are based on cash flows from interest-only (IO) payments or principal-only (PO) payments and are sensitive to prepayment risks. The CMOs in the State System's portfolio do not have IO or PO structures; however, they are subject to extension or contraction risk based on movements in interest rates.

Moody's Rating: The State System uses ratings from Moody's Investors Service, Inc., to indicate the credit risk of investments; i.e., the risk that an issuer or other counterparty to an investment will not fulfill its obligations. An *Aaa* rating indicates the highest quality obligations with minimal credit risk. Ratings that begin with *Aa* indicate high quality obligations subject to very low credit risk; ratings that begin with *A* indicate upper-medium-grade obligations subject to low credit risk; and ratings that begin with *Baa* indicate medium-grade obligations, subject to moderate credit risk, that may possess certain speculative characteristics. Moody's appends the ratings with numerical modifiers *1*, *2*, and *3*, with *1* indicating a higher ranking and *3* indicating a lower ranking within the category. For short-term obligations, a rating of *P-1* indicates that issuers have a superior ability to repay short-term debt obligations, and a rating of *P-2* indicates that issuers have a strong ability to repay short-term debt obligations.

Modified Duration: The State System denotes interest rate risk, or the risk that changes in interest rates will affect the fair value of an investment, using *modified duration*. *Duration* is a measurement in years of how long it takes for the price of a bond to be repaid by its internal cash flows. *Modified duration* takes into account changing interest rates. The State System maintains a portfolio duration target of 1.8 years with an upper limit of 2.5 years for the intermediate-term component of the operating portion of the investment portfolio. The State System's duration targets are not applicable to its long-term investments.

Fair Value Hierarchy: GASB Statement No. 72, *Fair Value Measurement and Application*, requires that investments be classified according to a "fair value hierarchy." With respect to Statement No. 72's fair value hierarchy, GASB defines "inputs" as "the assumptions that market participants would use when pricing an asset or liability, including assumptions about risk." Statement No. 72 further categorizes inputs as *observable* or *unobservable*: *Observable inputs* are "inputs that are developed using market data, such as publicly available information about actual events or transactions, and which reflect the assumptions that market participants would use when pricing an asset or liability"; *Unobservable inputs* are "inputs for which market data are not available and that are developed using the best information available about the assumptions that market participants would use when pricing an asset or liability."

Statement No. 72's fair value hierarchy categorizes the inputs to valuation techniques used to measure fair value into three "levels":

Level 1: Investments whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market, such as stocks listed in the S&P 500 or NASDAQ. If an up-to-date price of the investment can be found on a major exchange, it is a Level 1 investment.

Level 2: Investments whose values are based on their quoted prices in inactive markets or whose values are based on models, and the inputs to those models are observable either directly or indirectly for substantially the full term of the asset or liability.

Level 3: Investments that trade infrequently, and as a result do not have many reliable market prices. Valuations of Level 3 investments typically are based on management assumptions or expectations. For example, a private equity investment or complex derivative would likely be a Level 3 investment.

In addition, the fair value of certain investments that do not have a readily determinable fair value is classified as *NAV*, meaning Net Asset Value per share, when the fair value is calculated in a manner consistent with the Financial Accounting Standards Board's measurement principles for investment companies.

Debt and equity securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Debt and equity securities classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. Securities classified in Level 3 of the fair value hierarchy lack an independent pricing source and so are valued using an internal fair value as provided by the investment manager.

Commonfund investments, held locally by some of the universities, are valued based upon the unit values (NAV) of the funds held by the universities at year end. Unit values are based upon the underlying assets of the funds derived from inputs principally from or corroborated by observable market data, by correlation, or other means. Redemption restrictions for the Commonfund vary, depending upon the type of fund in which the universities have invested, and are restricted to withdrawals only on a weekly basis or the last business day of the month. All withdrawals require five days' notice.

State System Pooled Deposits and Investments
The carrying values (fair values) of deposits and investments for the State System's pooled funds in M&T Bank on June 30, 2016 and 2015, follow.

State System Pooled Deposits and Investments
June 30, 2016
(in thousands)

	Fair Value Hierarchy Level	Moody's Rating (if applicable)	Modified Duration (if applicable)	Fair Value
Deposits				
Demand and time deposits				$28
Money market funds				5,296
Total deposits				5,324
Investments				
Commercial paper	2	P1	0.17	265,251
Government money market mutual fund	2	Aaa	0.00	79,979
U.S. government and agency obligations	2	Aaa	2.45	414,573
Asset-backed securities	2	Aaa	0.48	93,876
	2	P1	0.15	14,988
Collateralized mortgage obligations (CMOs)	2	Aaa	2.15	193,070
Corporate bonds and notes	2	Aaa	1.34	6,197
	2	Aa1	1.33	6,740
	2	Aa2	1.41	9,670
	2	Aa3	1.51	3,332
	2	A1	1.26	63,506
	2	A2	1.33	66,345
	2	A3	2.54	36,713
	2	Baa1	1.91	27,436
	2	Baa2	0.99	21,771
	2	Baa3	0.00	727
Total investments				1,304,174
Total deposits and investments				$1,309,498

State System Pooled Deposits and Investments
June 30, 2015
(in thousands)

	Fair Value Hierarchy Level	Moody's Rating (if applicable)	Modified Duration (if applicable)	Fair Value
Deposits				
Demand and time deposits				$114
Money market funds				7,968
Total deposits				8,082
Investments				
Commercial paper	2	Aaa	0.06	7,602
	2	P1	0.31	150,938
Government money market mutual fund	2	Aaa	0.00	62,832
U.S. government and agency obligations	2	Aaa	2.62	440,072
Asset-backed securities	2	Aaa	0.76	88,060
	2	Aa1	1.71	6,225
	2	P1	0.40	17,426
Collateralized mortgage obligations (CMOs)	2	Aaa	4.10	251,458
Corporate bonds and notes	2	Aaa	1.12	11,300
	2	Aa1	2.73	7,690
	2	Aa2	0.63	18,395
	2	Aa3	1.10	8,803
	2	A1	1.33	34,951
	2	A2	1.51	64,851
	2	A3	1.39	39,524
	2	Baa1	1.14	33,932
	2	Baa2	1.03	22,203
	2	Baa3	0.00	725
Total investments				1,266,987
Total deposits and investments				$1,275,069

Of the investments noted above at June 30, 2016 and 2015, $13,527,000 and $4,569,000, respectively, were held by a trustee to be used for projects funded under the Pennsylvania Higher Educational Facilities Authority/State System of Higher Education bond issues (note 8). Such investments are made subject to the restrictions of the bond indenture and may be liquidated only for the payment of costs associated with the projects described in the bond indenture.

University Local Deposits and Investments

The carrying values (fair values) of local university deposits and investments on June 30, 2016 and 2015, follow.

University Local Deposits and Investments
June 30, 2016
(in thousands)

	Fair Value Hierarchy Level	Moody's Rating (if applicable)	Modified Duration (if applicable)	Fair Value
Deposits				
Demand and time deposits				$15,220
Certificates of deposit				14
Total deposits				15,234
Investments				
U.S. government and agency obligations	2	Aaa	0.47	164
Bond mutual funds	2		4.98	1,744
	NAV		4.43	11,143
Debt securities	2	AA	1.10	25
	2	Aa1	5.25	26
	2	Aa2	2.76	31
Equity/balanced mutual funds	1			2,385
	2			3,345
	3			7,006
	NAV			23,267
Common stock	1			2,319
Total investments				51,455
Total deposits and investments				$66,689

University Local Deposits and Investments
June 30, 2015
(in thousands)

	Fair Value Hierarchy Level	Moody's Rating (if applicable)	Modified Duration (if applicable)	Fair Value
Deposits				
Demand and time deposits				$12,362
Certificates of deposit				14
Total deposits				12,376
Investments				
U.S. government and agency obligations	2	Aaa	0.55	72
Bond mutual funds	2		4.40	1,466
	NAV		4.84	4,438
Debt securities	2	AA	2.10	25
	2	Aa1	6.80	26
	2	Aa2	3.70	30
Equity/balanced mutual funds	1			1,624
	2			3,168
	3			2,369
	NAV			30,651
Common stock	1			2,618
Total investments				46,487
Total deposits and investments				$58,863

Of the local investments noted above, the exposure to foreign currency risk is as follows.

(in thousands)

Investment	Currency	Fair Value June 30, 2016	Fair Value June 30, 2015
Deposit	British Pound	$0	$6

The universities are beneficiaries of trust funds held by others with an approximate fair value of $4,087,000 and $3,795,000 on June 30, 2016 and 2015, respectively. Since the universities have neither possession nor control of these trusts, the principal is not included in the accompanying balance sheet.

(3) Leases

Total rent expense for the State System operating leases amounted to $15,955,000 and $16,371,000 for the years ended June 30, 2016 and 2015, respectively.

Capital assets acquired through leases that have been capitalized are as follows.

(in thousands)

	June 30, 2016	June 30, 2015
Cost:		
Buildings	$76,431	$76,416
Equipment	3,074	3,520
Total	$79,505	$79,936
Accumulated Depreciation:		
Buildings	$38,027	$33,748
Equipment	1,501	1,805
Total	$39,528	$35,553

Future minimum payments, by year and in the aggregate, under capital and noncancelable operating leases, with initial or remaining terms of one year or more, are as follows.

(in thousands)

	Operating Leases	Capital Leases
2017	$7,525	$5,697
2018	5,573	5,570
2019	4,654	5,501
2020	3,721	5,193
2021	2,843	5,059
Thereafter	56,516	37,824
Total minimum lease payments	$80,832	64,844
Amount representing interest on capital leases		16,198
Present value of net minimum capital lease payments		$48,646

Changes in the liability for capital leases in fiscal years 2016 and 2015 follow.

(in thousands)

Year	Beginning Balance	Capital Lease Additions	Capital Lease Payments	Ending Balance
2015	$53,791	$1,161	$3,360	$51,592
2016	$51,592	$431	$3,377	$48,646

(4) Pension Benefits

Employees of the State System enroll in one of three available retirement plans immediately upon employment: the Commonwealth of Pennsylvania State Employees' Retirement System (SERS), the Public School Employees' Retirement System (PSERS), or the Alternative Retirement Plan (ARP).

Following is the total of the State System's pension liabilities, deferred outflows and inflows of resources related to pensions, and the pension expense for the fiscal years ended June 30, 2016 and 2015.

(in thousands)

	SERS		PSERS		ARP		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Net pension liabilities	**$858,417**	**$728,094**	**$80,220**	**$70,650**	**$0**	**$0**	**$938,637**	**$798,744**
Deferred outflows of resources:								
Difference between expected and actual experience	$17,381	$3,953					$17,381	$3,953
Net difference between projected and actual investment earnings on pension plan investments	87,404	21,036					87,404	21,036
Changes in assumptions	25,503						25,503	
Difference between employer contributions and proportionate share of contributions			$568	$295			568	295
Changes in proportion			3,550	1,682			3,550	1,682
Contributions after the measurement date	41,639	32,028	6,012	5,213			47,651	37,241
Total deferred outflows of resources	**$171,927**	**$57,017**	**$10,130**	**$7,190**	**$0**	**$0**	**$182,057**	**$64,207**
Deferred inflows of resources:								
Difference between expected and actual experience			$331				$331	
Net difference between projected and actual investment earnings on pension plan investments			162	$5,051			162	$5,051
Difference between employer contributions and proportionate share of contributions	$2,389	$2,182					2,389	2,182
Changes in proportion	26,207	6,867					26,207	6,867
Total deferred inflows of resources	**$28,596**	**$9,049**	**$493**	**$5,051**	**$0**	**$0**	**$29,089**	**$14,100**
Pension expense	**$103,982**	**$83,545**	**$16,035**	**$6,663**	**$43,933**	**$44,619**	**$163,950**	**$134,827**
Contributions recognized by pension plans	**$69,021**	**$57,234**	**$6,012**	**$5,236**	**N/A**	**N/A**	**$75,033**	**$62,470**

The State System will recognize the $41,639,000 reported as 2016 SERS deferred outflows of resources resulting from pension contributions after the measurement date, and the $6,012,000 reported as 2016 PSERS deferred outflows of resources resulting from pension contributions after the measurement date, as reductions of the respective net pension liabilities in the year ended June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows.

(in thousands)

	Amortization	
Fiscal Year Ended	**SERS**	**PSERS**
June 30, 2017	$26,357	$680
June 30, 2018	$26,357	$680
June 30, 2019	$26,357	$680
June 30, 2020	$21,746	$1,585
June 30, 2021	$875	$0

SERS

Plan Description

SERS is the administrator of a cost-sharing multiple-employer defined benefit plan established by the Commonwealth to provide pension benefits for employees of state government and certain independent agencies. SERS is a component unit of the Commonwealth and is included in the Commonwealth's financial report as a pension trust fund. Membership in SERS is mandatory for most state employees. Members and employees of the General Assembly, certain elected or appointed officials in the executive branch, department heads, and certain employees in the field of education are not required, but are given the option, to participate. SERS issues a publicly available annual financial report that includes financial statements and required supplementary information for the plan. A copy of the report may be obtained from the SERS website at www.sers.state.pa.us.

Benefits Provided

SERS provides retirement, death, and disability benefits. Article II of the Commonwealth's Constitution assigns the authority to establish and amend the benefit provision of the plan to the General Assembly. Cost of Living Adjustments (COLA) are provided ad hoc at the discretion of the General Assembly.

Employees who were hired prior to January 1, 2011, and retire at age 60 with three years of service, or with 35 years of service if under age 60, are entitled to a normal annual retirement benefit; members of the General Assembly and certain employees classified in hazardous duty positions can retire with full benefits at age 50 with at least three years of service. Act 120 of 2010 (Act 120) preserved all benefits in place for members, but mandated a number of benefit reductions for new members effective January 1, 2011. The benefit reduction included a new class of membership that accrues benefits at 2% of members' final average salary instead of the previous 2.5%. The new vesting period changed from 5 to 10 years of credited service, and the option to withdraw lump-sum accumulated deductions was eliminated. The new normal retirement age is 65 for most employees and 55 for members of the General Assembly and certain employees classified in hazardous duty positions.

According to the State Employees' Retirement Code (SERC), all obligations of SERS will be assumed by the Commonwealth should SERS terminate.

Contributions

The contribution rate for both active members and the State System depends upon when the active member was hired and what benefits class was selected. Section 5507 of the SERC (71 Pa. C.S. §5507) requires the Commonwealth and other employers whose employees are SERS members to make contributions to the fund on behalf of all active members and annuitants necessary to fund the liabilities and provide the annuity reserves required to pay benefits. The SERS funding policy, as set by the SERS Board, provides for periodic active member contributions at statutory rates. The SERS funding policy also provides for periodic employer contributions at actuarially determined rates based on SERS' funding valuation, expressed as a percentage of annual retirement covered payroll, such that the employer contributions, along with employee contributions and an actuarially determined rate of investment return, are adequate to accumulate assets to pay benefits when due. Act 120, however, imposed rate increase collars (limits on annual rate increases) on employer contributions. The collar for Commonwealth fiscal year 2014/15 was 4.5% and will remain at that rate until no longer needed.

The State System contributed at actuarially determined rates of between 17.18% and 24.86% of active members' annual covered payroll at June 30, 2016. The State System's contributions to SERS for the years ended June 30, 2016, 2015, and 2014, were $69,021,000, $57,234,000, and $43,548,000, respectively, equal to the required contractual contribution.

Contribution rates for most active members is 6.25% of gross salary. The contribution rate for other members ranges between 5% and 9.3% of salary, depending upon when the member was hired and what class of membership was elected.

Assumptions
The total SERS pension liabilities used to calculate the net pension liabilities were determined by actuarial valuations as of December 31, 2015 and 2014, using the following actuarial assumptions, applied to all periods included in the measurement.

- Entry age actuarial cost method.
- Straight-line amortization of investments over five years and amortization of assumption changes and noninvestment gains/losses over the average expected remaining service lives of all employees that are provided benefits.
- Inflation of 2.75%.
- Investment return of 7.50%, net of expenses and including inflation.
- Salary increases based on an average of 5.70%, with a range of 3.85% to 9.05%, including inflation.
- Asset valuation using fair (market) value.
- Mortality rates based on the projected RP-2000 Mortality Tables, adjusted for actual plan experience and future improvement.
- Ad hoc cost of living adjustments (COLAs).

Some of the methods and assumptions mentioned above are based on the 18th *Investigation of Actuarial Experience,* an actuarial experience study conducted by SERS to determine whether the assumptions used in its annual actuarial valuations remain accurate based on current and anticipated demographic trends and economic conditions. Published in March 2016, it analyzed experience from 2011 through 2016. The actuary, under oversight of the SERS Board, reviewed economic assumptions (such as the assumed future investment returns and salary increases) as well as demographic assumptions (such as employee turnover, retirement, disability, and death rates). Some assumption adjustments increased projected cost and some decreased projected cost, but the overall result was a slight increase to the net pension liability.

The long-term expected real rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in SERS' current and target asset allocation as of December 31, 2015, are summarized below.

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Alternative investments	15.00%	8.50%
Global public equity	40.00%	5.40%
Real assets	17.00%	4.95%
Diversifying assets	10.00%	5.00%
Fixed income	15.00%	1.50%
Liquidity reserve	3.00%	0.00%
	100.00%	

The discount rate used to measure the total SERS pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the rates applicable for each member and that employer contributions will be made based on rates determined by the actuary and as set by statute. Based on those assumptions, SERS' fiduciary net position was projected to be available to make all projected future benefit payments of current and nonactive SERS members. The long-term expected rate of return on SERS' investments, therefore, was applied to all periods of projected benefit payments to determine the total pension liability.

The following presents the State System's proportionate share of the SERS net pension liability calculated using the discount rate of 7.50%, as well as what the SERS net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.50%) or one percentage point higher (8.50%) than the current rate.

Sensitivity of the State System's Proportionate Share of the SERS Net Pension Liability to Changes in the Discount Rate
(in thousands)

	1% Decrease 6.50%	Current Rate 7.50%	1% Increase 8.50%
2015	$1,066,316	$858,417	$680,156
2014	$931,943	$728,094	$552,817

Fiduciary Net Position
The fiduciary net positions of SERS, as well as additions to and deductions from SERS fiduciary

net positions, have been determined on the same basis as they are reported in the SERS financial statements, which can be found at www.sers.state.pa.us. The plan schedules of SERS are prepared using the accrual basis of accounting and economic resources measurement focus in accordance with U.S. GAAP as prescribed by GASB. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has a legal requirement to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. Investment purchases and sales are recorded on a trade-date basis. Detailed information on investment valuation can be found in the SERS financial statements. Management of SERS has made certain estimates and assumptions relating to employer allocation schedules, and actual results could differ.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions
At June 30, 2016, the amount recognized as the State System's proportionate share of the SERS net pension liability, measured at December 31, 2015, was $858,417,000. At June 30, 2015, the amount recognized as the State System's proportionate share of the SERS net pension liability, measured at December 31, 2014, was $728,094,000.

The allocation percentage assigned to each participating employer is based on a projected-contribution method. For the allocation of the 2015 amounts, this methodology applies the most recently calculated contribution rates for fiscal year 2016/17, from the December 31, 2015, funding valuation, to the expected funding payroll. For the allocation of the 2014 amounts, this methodology applies the most recently calculated contribution rates for fiscal year 2015/16, from the December 31, 2014, funding valuation, to the expected funding payroll. At the December 31, 2015, measurement date, the State System's proportion was 4.721%, a decrease of .018% from its proportion calculated as of the December 31, 2014, measurement date.

PSERS
Plan Description
PSERS is a governmental cost-sharing multiple-employer defined benefit pension plan that provides retirement, disability, and death benefits to public school employees of the Commonwealth. The members eligible to participate in PSERS include all full-time public school employees, part-time hourly public school employees who render at least 500 hours of service in the school year, and part-time per diem public school employees who render at least 80 days of service in the school year in any of the reporting entities in Pennsylvania. The Public School Employees' Retirement Code (Act No. 96 of October 2, 1975, as amended) (24 Pa. C.S. §§8101–8535) (the Code) is the authority by which PSERS benefits provisions and contribution requirements are established and may be amended. The Code requires contributions by active members, the employer (State System), and the Commonwealth. PSERS is a component unit of the Commonwealth and is included in the Commonwealth's financial report as a pension trust fund. PSERS issues a comprehensive annual financial report that may be obtained at www.psers.state.pa.us.

Benefits Provided
Members who joined prior to July 1, 2011, are eligible for monthly retirement benefits upon reaching age 62 with at least one year of credited service, age 60 with 30 or more years of credited service, or any age with 35 or more years of service. Act 120 preserved the benefits of members who joined prior to July 1, 2011, and introduced benefit reductions for individuals who become new members on or after July 1, 2011, by creating two new membership classes: Class T-E and Class T-F. To qualify for normal retirement, Class T-E and Class T-F members must complete a minimum of 35 years of service with a combination of age and service that totals 92 or greater, or they must work until age 65 with a minimum of three years of service.

Depending upon membership class, benefits are generally 2% or 2.5% of the member's final average salary (as defined in the Code) multiplied by the number of years of credited service. Members who joined prior to July 1, 2011, vest after completion of five years of service and may elect early retirement benefits. Class T-E and Class T-F members vest after completion of 10 years of service.

Participants are eligible for disability retirement benefits after completion of five years of credited service. Such benefits are generally equal to 2% or 2.5%, depending upon membership class, of the member's final average salary (as defined in the Code) multiplied by the number of years of credited service, but not less than one-third of such salary nor greater than the benefit the member would have had at normal retirement age. Members over normal retirement age may apply for disability benefits.

Death benefits are payable upon the death of an active member who has reached age 62 with at least one year of credited service (age 65 with at least three years of credited service for Class T-E and Class T-F members) or has at least five years of credited service (10 years for Class T-E and Class T-F members). Such benefits are actuarially equivalent to the benefit that would have been effective if the member had retired on the day before death.

Member Contributions
Active members who joined PSERS prior to July 22, 1983, contribute at 5.25% (Class T-C members) or at 6.50% (Class T-D members) of the member's qualifying compensation. Members who joined PSERS on or after July 22, 1983, and who were active or inactive as of July 1, 2001, contribute at 6.25% (Class T-C) or at 7.5% (Class T-D) of the member's qualifying compensation. Members who joined PSERS after June 30, 2001, and before July 1, 2011, contribute at 7.5% (Class T-D). For these hires and for members who elected Class T-D, the 7.5% contribution rate began with service rendered on or after January 1, 2002. Members who joined PSERS after June 30, 2011, contribute at the rate of 7.5% (Class T-E) or 10.3% (Class T-F) of their qualifying compensation. Class T-E and Class T-F members are subject to a "shared risk" provision in Act 120 that could cause the rate in future years to fluctuate between 7.5% and 9.5% for Class T-E and 10.3% and 12.3% for Class T-F.

Employer Contributions
The State System's contractually required contribution rate for PSERS for fiscal year ended June 30, 2016, was 25.0% of covered payroll, actuarially determined as an amount that, when combined with employee contributions, is expected to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. Per §8327 of the Code, the Commonwealth is required to contribute 50% of the contribution rate directly to PSERS on behalf of the State System, meaning that the amount that the State System actually contributed was 12.5% of covered payroll. The State System's contribution to PSERS for the year ending June 30, 2016, June 30, 2015, and June 30, 2014 was $6,012,000, $5,236,000, and $3,940,000, respectively, equal to the required contractual contribution.

Actuarial Assumptions
The total PSERS pension liability as of June 30, 2015, was determined by rolling forward PSERS' total pension liability as of the June 30, 2014, actuarial valuation to June 30, 2015, using the following actuarial assumptions, applied to all periods included in the measurement.

- Actuarial cost method is entry age normal, level percent of pay.
- Inflation of 3%.
- Investment return of 7.50%, including inflation.
- Salary increases based on an effective average of 5.5%, which reflects an allowance for inflation, real wage growth of 1.0%, and merit or seniority increases of 1.50%.
- Mortality rates based on the RP-2000 Combined Healthy Annuitant Tables (male and female) with age set back three years for both males and females; for disabled annuitants, the RP-2000 Combined Disabled Tables (male and female) with age set back seven years for males and three years for females.

The actuarial assumptions used in the June 30, 2014, valuation were based on the experience study that was performed for the five-year period ending June 30, 2010. The recommended assumption changes based on this experience study were adopted by the PSERS Board of Trustees at its March 11, 2011, meeting and were effective beginning with the June 30, 2011, actuarial valuation.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

PSERS' policy in regard to the allocation of invested plan assets is established and may be amended by the PSERS Board of Trustees. Plan assets are managed with a long-term objective of achieving and maintaining a fully funded status for the benefits provided through the pension. Following is the PSERS Board of Trustees' adopted asset allocation policy and best estimates of geometric real rates of return for each major asset class as of June 30, 2015.

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Public markets global equity	22.5%	4.8%
Private markets (equity)	15.0%	6.6%
Private real estate	12.0%	4.5%
Global fixed income	7.5%	2.4%
U.S. long treasuries	3.0%	1.4%
TIPS	12.0%	1.1%
High-yield bonds	6.0%	3.3%
Cash	3.0%	0.7%
Absolute return	10.0%	4.9%
Risk parity	10.0%	3.7%
MLPs/Infrastructure	5.0%	5.2%
Commodities	8.0%	3.1%
Financing (LIBOR)	(14.0%)	1.1%
	100.0%	

The discount rate used to measure the total PSERS pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current contribution rate and that contributions from employers will be made at contractually required rates, actuarially determined. Based on those assumptions, PSERS' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on PSERS' investments was applied to all periods of projected benefit payments to determine the total pension liability.

The following presents the State System's proportionate share of the PSERS net pension liability calculated using the discount rate of 7.50%, as well as what the PSERS net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.50%) or one percentage point higher (8.50%) than the current rate.

Sensitivity of the State System's Proportionate Share of the PSERS Net Pension Liability to Changes in the Discount Rate
(in thousands)

	1% Decrease 6.50%	Current Rate 7.50%	1% Increase 8.50%
2015	$98,879	$80,220	$64,537
2014	$88,128	$70,650	$55,731

Fiduciary Net Position
For purposes of measuring the net pension liability, deferred outflows of resources, and deferred inflows of resources related to pensions and pension expense, the fiduciary net position of PSERS and additions to or deductions from PSERS' fiduciary net position have been determined on the same basis as they are reported in the PSERS' financial statements. For this purpose, benefit payments, including refunds of employee contributions, are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value. Detailed information about PSERS' fiduciary net position is available in the PSERS Comprehensive Annual Financial Report, which can be found at www.psers.state.pa.us.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions
The amount recognized as the State System's proportionate share of the PSERS net pension liability, plus the related PSERS pension support provided by the Commonwealth, is as follows.

(in thousands)	2016	2015
Total PSERS net pension liability associated with the State System	$160,440	$141,300
Commonwealth's proportionate share of the PSERS net pension liability associated with the State System	80,220	70,650
State System's proportionate share of the PSERS net pension liability	$80,220	$70,650

PSERS measured the net pension liability as of June 30, 2015. The total PSERS pension liability used to calculate the net pension liability was determined by rolling forward the total pension liability calculated as of June 30, 2014, to June 30, 2015. PSERS calculated the employer's proportion of the net pension liability using the employer's one-year reported covered payroll in relation to all participating employers' one-year reported covered payroll. At June 30, 2015, the State System's proportion was .1852%, an increase of .0067% from its proportion calculated as of June 30, 2014.

ARP

The ARP is a defined contribution plan administered by the State System. Benefits equal amounts contributed to the plan plus investment earnings. Act 188 empowers the Board to establish and amend benefits provisions. The State Employees' Retirement Code establishes the employer contribution rate for the ARP, while the Board establishes the employee contribution rates. Active members contribute at a rate of 5% of their qualifying compensation. The State System recognizes annual pension expenditures equal to its contractually required contributions to the plan. The State System's contribution rate on June 30, 2016 and 2015, was 9.29% of qualifying compensation. The contributions to the ARP for the years ended June 30, 2016 and 2015, were $43,933,000 and $44,619,000, respectively, from the State System; and $24,022,000 and $23,903,000, respectively, from active members. No liability is recognized for the ARP.

(5) Postretirement Benefits

State System employees who retire after meeting specified service and age requirements become eligible for participation in one of two defined health care benefits plans, referred to here as the *System Plan* and the *Retired Employees Health Program*. These plans include hospital, medical/surgical, and major medical coverage, and provide a Medicare supplement for individuals over age 65.

System Plan

Plan Description

Employee members of the Association of Pennsylvania State College and University Faculties (APSCUF), the State College and University Professional Association (SCUPA), Security Police and Fire Professionals of America (SPFPA), Office and Professional Employees International Union (OPEIU), and nonrepresented employees participate in a single-employer defined benefits health care plan administered by the State System (System Plan). The System Plan provides eligible retirees and their eligible dependents with health care benefits and tuition waivers at any of the 14 State System universities. Act 188 empowers the Board to establish and amend benefits provisions. The System Plan has no plan assets and no financial report is prepared.

Funding Policy

The contribution requirements of plan members and the State System are established and may be amended by the Board. The System Plan is funded on a pay-as-you-go basis; i.e., premiums are paid to an insurance company and various health maintenance organizations to fund the health care benefits provided to current retirees. Tuition waivers are provided by the retiree's sponsoring university as they are granted. The State System paid premiums of $40,060,000 and $36,869,000 for the fiscal years ending June 30, 2016 and 2015, respectively. Plan members receiving benefits contribute at various rates, depending upon when they retire, whether they are eligible for Medicare, the contribution rate in effect on the day of their retirement, the contribution rate for active employees, and applicable collective bargaining agreements. Following are the contribution rates of plan members as of June 30, 2016.

- Eligible plan members receiving benefits who retired prior to July 1, 2005, are not required to make contributions.
- Nonfaculty coaches who retired on or after July 1, 2005, pay a percentage of their final annual gross salary at the time of retirement.
- Eligible annuitants who retired on or after July 1, 2005, and prior to July 1, 2008, and who are under age 65 pay the same dollar amount they paid as active employees on the day of retirement. When these annuitants become eligible for Medicare, they pay 18% of the current cost of their Medicare coverage and current cost of coverage for covered dependents. The rate changes annually, and future adjustments will apply if contributions increase for active employees.
- Eligible annuitants who retire on or after July 1, 2008, pay 18% of the plan premium in effect for active employees on their retirement date. Future adjustments will apply if contributions increase for active employees.
- Employee members of SPFPA, OPEIU, and SCUPA, and nonrepresented employees, hired after January 15, 2016, receive no postretirement benefits.

Total contributions made by plan members were $4,866,000 and $4,272,000, or approximately 10.8% and 10.4% of the total premiums, for the fiscal years ending June 30, 2016 and 2015, respectively.

Annual OPEB Cost and Net OPEB Obligation
The State System's annual other postemployment benefit (OPEB) cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.* The ARC represents a level of funding that, if paid annually, is projected to cover normal cost plus the annual portion of the unfunded actuarial liability amortized over 30 years. The following shows the components of the State System's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the State System's net OPEB obligation.

(in thousands)	June 30, 2016	June 30, 2015
Annual required contribution	$102,000	$102,000
Interest on net OPEB obligation	44,690	42,800
Adjustment to ARC	(58,736)	(56,253)
Annual OPEB cost (expense)	87,954	88,547
Contributions made	(40,060)	(36,869)
Increase in net OPEB obligation	47,894	51,678
Net OPEB obligation at July 1	1,058,749	1,007,071
Net OPEB obligation at June 30	$1,106,643	$1,058,749

The State System's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for June 30, 2016, and the two preceding years were as follows.

(in thousands) Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
June 30, 2014	$117,582	37.6%	$1,007,071
June 30, 2015	$88,547	41.6%	$1,058,749
June 30, 2016	$87,954	45.6%	$1,106,643

Funded Status and Funding Progress
The funded status of the plan as of July 1, 2014, the most recent actuarial valuation date, was as follows.

(in thousands)	
Actuarial accrued liability (AAL)	$1,194,849
Actuarial value of plan assets	0
Unfunded actuarial accrued liability (UAAL)	$1,194,849
Funded ratio (actuarial value of plan assets/AAL)	0%
Covered payroll (active plan members)	$589,917
UAAL as a percentage of covered payroll	203%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions
Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefits costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the July 1, 2014, actuarial valuation, the projected unit credit method was used with a 4.25% investment rate of return, which is the rate expected to be earned on the State System's operating portfolio. The health care cost trend rate used was 6.5% in 2014, 6.0% in 2015, and 5.5% in 2016 through 2020, with rates gradually decreasing from 5.4% in 2021 to 3.8% in 2075 and later based on the Society of Actuaries Long-Run Medical Cost Trend Model. The UAAL is being amortized as a level percentage of payroll on a closed basis. The remaining amortization period at July 1, 2014, was 21 years.

Retired Employees Health Program
Plan Description
Employee members of the American Federation of State, County and Municipal Employees (AFSCME), Pennsylvania Doctors Alliance (PDA), and Pennsylvania Social Services Union (PSSU) participate in the Retired Employees Health Program (REHP), which is sponsored by the Commonwealth and administered by the Pennsylvania Employee Benefits Trust Fund (PEBTF). The REHP provides eligible retirees and their eligible dependents with health care benefits. Benefits provisions are established and may be amended under pertinent statutory authority. The REHP neither issues a stand-alone financial report nor is it included in the report of a public employee retirement system or other entity.

Funding Policy
The contribution requirements of plan members covered under collective bargaining agreements are established by the collective bargaining agreements. The contribution requirements of nonrepresented plan members and contributing entities are established and may be amended by the Commonwealth's Office of Administration and the Governor's Budget Office. Plan members who enrolled prior to July 1, 2005, are not required to make contributions. Plan members who enrolled after July 1, 2005, contribute a percentage of their final salary, the rate of which varies based on the plan member's enrollment date. Agency member (employer) contributions are established primarily on a pay-as-you-go basis. In fiscal year 2015/16, the State System contributed $418 for each current active employee per biweekly pay period. The State System made contributions of $37,026,000, $30,765,000, and $28,584,000 for the fiscal years ending June 30, 2016, 2015, and 2014, respectively, equal to the required contributions for the year. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

(6) Workers' Compensation

The State System is self-insured for workers' compensation losses. For claims occurring prior to July 1, 1995, State System universities must pay up to $100,000; for claims occurring on or after July 1, 1995, State System universities must pay up to $200,000. Claims in excess of the self-insurance limits are funded through the Workers' Compensation Collective Reserve Fund (Reserve Fund), to which all State System universities contribute an amount determined by an independent actuarial study. Based on updated actuarial studies, the universities contributed $372,000, $1,405,000, and $1,875,000 to the Reserve Fund during the years ended June 30, 2016, 2015, and 2014, respectively.

For the years ended June 30, 2016, 2015, and 2014, the aggregate liability for claims under the self-insurance limit was $9,345,000, $9,825,000, and $9,902,000, respectively. The Reserve Fund assets of $12,746,000, $12,724,000, and $11,808,000 are equal to the liability for claims in excess of the self-insurance limits for the years ended June 30, 2016, 2015, and 2014, respectively. Changes in the workers' compensation claims liability in fiscal years 2016, 2015, and 2014 follow.

(in thousands)

Year	Beginning Balance	Current Year Claims and Changes in Estimates	Claim Payments	Ending Balance
2014	$21,344	$5,244	$4,878	$21,710
2015	$21,710	$5,177	$4,337	$22,550
2016	$22,550	$3,465	$3,924	$22,091

(7) Compensated Absences

Changes in the compensated absences liability in fiscal years 2016 and 2015 are as follows.

(in thousands)

Year	Beginning Balance	Current Changes in Estimates	Less Payouts	Ending Balance
2015	$114,710	$11,272	$11,342	$114,640
2016	$114,640	$9,799	$9,016	$115,423

(8) Bonds Payable

Bonds payable on June 30, 2016 and 2015, consisted of several outstanding tax-exempt revenue bond series issued by the Pennsylvania Higher Educational Facilities Authority (PHEFA). In connection with the bond issuance, the State System entered into a loan agreement with PHEFA under which the State System has pledged its full faith and credit for the repayment of the bonds. The loan constitutes an unsecured general obligation of the State System. The bonds were issued to provide funds to undertake various capital projects at the universities or to advance refund certain previously issued bonds.

Activity for the various bond series for the years ended June 30, 2016 and 2015, was as follows.

Bonds Payable
June 30, 2016 and 2015
(in thousands)

Description	Original Issuance	Weighted Average Interest Rate	Balance June 30, 2014	2015 Bonds Issued	2015 Bonds Redeemed/ Refunded	Balance June 30, 2015	2016 Bonds Issued	2016 Bonds Redeemed/ Refunded	Balance June 30, 2016	Current Portion
Series AC issued July 2005, final maturity June 2025	$52,650	N/A	$31,095	-	$31,095	-	-	-	-	-
Series AE issued July 2006, final maturity June 2036	103,290	N/A	75,805	-	75,805	-	-	-	-	-
Series AF issued July 2007, final maturity June 2037	68,230	5.00%	54,525	-	2,305	$52,220	-	$52,220	-	-
Series AG issued March 2008, final maturity June 2024	101,335	4.81%	70,505	-	10,875	59,630	-	11,485	$48,145	$12,075
Series AH issued July 2008, final maturity June 2038	140,760	4.66%	119,005	-	4,220	114,785	-	4,435	110,350	4,655
Series AI issued August 2008, final maturity June 2025	32,115	4.21%	21,725	-	1,845	19,880	-	1,910	17,970	1,990
Series AJ issued July 2009, final maturity June 2039	123,985	4.88%	105,285	-	4,835	100,450	-	5,245	95,205	5,685
Series AK issued Sept. 2009, final maturity June 2024	47,310	4.00%	32,240	-	3,795	28,445	-	3,910	24,535	4,080
Series AL issued July 2010, final maturity June 2035	135,410	5.00%	90,065	-	7,710	82,355	-	7,935	74,420	8,000
Series AM issued July 2011, final maturity June 2036	119,085	4.64%	108,170	-	4,200	103,970	-	4,420	99,550	4,655
Series AN issued March 2012, final maturity June 2023	76,810	5.00%	75,365	-	4,000	71,365	-	8,235	63,130	9,430
Series AO issued July 2013, final maturity June 2038	30,915	4.32%	29,995	-	1,040	28,995	-	1,075	27,880	1,105
Series AP issued May 2014, final maturity June 2024	46,110	4.51%	46,110	-	2,685	43,425	-	2,940	40,485	1,200
Series AQ issued May 2015, final maturity June 2036	94,975	4.70%	-	$94,975	-	94,975	-	1,880	93,095	6,685
Series AR issued Sept. 2015, final maturity June 2040	102,365	4.01%	-	-	-	-	$102,365	1,820	100,545	2,475
Series AS issued June 2016, final maturity June 2037	47,280	3.72%	-	-	-	-	47,280	-	47,280	850
Total	**$1,322,625**	-	**$859,890**	**$94,975**	**$154,410**	**$800,455**	**$149,645**	**$107,510**	**$842,590**	**$62,885**

Principal and interest requirements to maturity are as follows.

(in thousands)	Principal	Interest	Total
2017	$62,885	$38,570	$101,455
2018	63,505	35,525	99,030
2019	67,935	32,543	100,478
2020	75,290	29,399	104,689
2021	59,025	25,926	84,951
2022–2026	261,165	88,074	349,239
2027–2031	143,720	40,059	183,779
2032–2036	78,960	15,083	94,043
2037–2040	30,105	2,815	32,920
Total	**$842,590**	**$307,994**	**$1,150,584**

(9) Debt Refunding

In June 2016, the net proceeds from the Series AS revenue bonds were used to purchase U.S. Government Securities that were deposited irrevocably in trust with an escrow agent to advance refund the Series AF revenue bonds. Although it resulted in an accounting loss of $1,115,000, the refunding was performed to reduce debt service by approximately $8,842,000 and resulted in an economic gain (difference between the present values of the old and new debt service payments) of approximately $7,469,000. The accounting loss, or deferred loss on refunding, is reported as a deferred outflow of resources. As of June 30, 2016, $49,800,000 of Series AF revenue bonds remained outstanding, and the fair market of the escrow account was $51,934,000. The funds in escrow will be used to pay the December 15, 2016, interest payment and the June 15, 2017, principal and interest payment of Series AF. Neither the funds in escrow nor the outstanding balance of Series AF is reflected on the balance sheet.

(10) Rating Actions

The State System's outstanding bonds are assigned an Aa3 rating from Moody's Investors Service, Inc. In August 2016, Moody's revised the outlook for the rating from *negative* to *stable.* Fitch Ratings reaffirmed the State System's rating of AA- with an outlook of *stable*.

(11) Capital Assets

The classifications of capital assets and related depreciation at June 30, 2016 and 2015, follow.

(in thousands)	Balance June 30, 2014	2014/15 Additions	2014/15 Retirements/ Adjustments	Balance June 30, 2015	2015/16 Additions	2015/16 Retirements/ Adjustments	Balance June 30, 2016
Land	$32,360	-	-	$32,360	-	-	$32,360
Construction in progress	70,206	$65,737	($36,799)	99,144	$56,475	($75,607)	80,012
Total capital assets not being depreciated	102,566	65,737	(36,799)	131,504	56,475	(75,607)	112,372
Buildings, including improvements	2,039,800	18,588	(2,203)	2,056,185	101,691	55,587	2,213,463
Improvements other than buildings	264,498	4,414	5,867	274,779	7,472	2,885	285,136
Equipment and furnishings	454,757	15,292	(15,921)	454,128	24,278	(8,059)	470,347
Library books	83,690	894	(2,644)	81,940	869	(1,495)	81,314
Total capital assets being depreciated	2,842,745	39,188	(14,901)	2,867,032	134,310	48,918	3,050,260
Less accumulated depreciation:							
Buildings and improvements	(777,255)	(79,045)	13,342	(842,958)	(82,671)	8,923	(916,706)
Land improvements	(121,584)	(10,379)	439	(131,524)	(9,355)	1,593	(139,286)
Equipment and furnishings	(355,366)	(28,215)	22,374	(361,207)	(27,789)	9,681	(379,315)
Library books	(74,298)	(2,013)	2,648	(73,663)	(1,868)	1,495	(74,036)
Total accumulated depreciation	(1,328,503)	(119,652)	38,803	(1,409,352)	(121,683)	21,692	(1,509,343)
Total capital assets being depreciated, net	1,514,242	(80,464)	23,902	1,457,680	12,627	70,610	1,540,917
Capital assets, net	$1,616,808	($14,727)	($12,897)	$1,589,184	$69,102	($4,997)	$1,653,289

(12) Deferred Outflows of Resources and Deferred Inflows of Resources

The classifications of deferred outflows of resources and deferred inflows of resources at June 30, 2016 and 2015, follow.

(in thousands)	June 30, 2016	June 30, 2015
Deferred Outflows of Resources		
Net pension liability related (see note 4)	$182,057	$64,207
Unamortized loss on refunding of debt	9,164	9,349
Total Deferred Outflows of Resources	$191,221	$73,556
Deferred Inflows of Resources		
Net pension liability related (see note 4)	$29,089	$14,100
Unamortized gain on refunding of debt	1,073	1,211
Total Deferred Inflows of Resources	$30,162	$15,311

(13) Contingencies and Commitments

Contingencies

The nature of the educational industry is such that, from time to time, the State System is exposed to various risks of loss related to torts; alleged negligence; acts of discrimination; breach of contract; labor disputes; disagreements arising from the interpretation of laws or regulations; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. While some of these claims may be for substantial amounts, they are not unusual in the ordinary course of providing educational services in a higher education system.

The State System receives support from federal and Commonwealth grant programs, primarily for student financial assistance. Entitlement to the resources requires compliance with terms of the grant agreements and applicable regulations, including the expenditure of the resources for eligible purposes. Substantially all grants are subject to financial and compliance audits by the grantors. As of June 30, 2016, the State System estimates that adjustments, if any, as a result of such audits would not have a material adverse effect on the accompanying financial statements, with the exception of potential adjustments related to Cheyney University of Pennsylvania, as detailed in the following section.

Cheyney University of Pennsylvania

In August 2015, the State System completed an analysis and reconciliation of almost 4,400 student accounts at Cheyney University for fiscal years 2011/12, 2012/13, and 2013/14. It was determined that, as a result of deficiencies in the university's policies, processes, and procedures related to the financial aid function, noncompliance with federal regulations in the administration and delivery of federal financial aid totaled $29.6 million over the three years. The State System, which undertook the analysis in consultation with the U.S. Department of Education (ED), self-reported the findings to the ED in August 2015. The ED has not yet given its determination of any amounts to be repaid; however, in September 2015 it placed the university on Heightened Cash Monitoring 2 (HCM2) status, meaning that the university no longer receives federal financial aid funds under the advance payment method, but instead must make financial aid disbursements to students from its own institutional funds and request reimbursement from the ED. The delayed receipt of funds, combined with continued enrollment declines, has resulted in a significant drop in cash that has not been matched with a corresponding drop in expenses, exacerbating the university's severe cash flow problems. The State System has appealed to the ED to remove the university from HCM2 status, citing the improvement of financial aid administration under the leadership of the Office of the Chancellor and a third-party consultant as well as other improvements in administration.

In January 2016, the U.S. Department of Justice (DOJ) notified the State System that it was investigating the application and use of federal student financial aid by Cheyney University and the oversight of the university by the State System. The DOJ requested that the university and State System preserve and produce certain documents. The State System has fully complied with DOJ's request. No action has been taken at this point by the DOJ, and the possible resulting outcomes from the investigation are uncertain until communication is received from the DOJ.

In November 2015, the Middle States Commission on Higher Education (Middle States) placed Cheyney University on probation "because of insufficient evidence that the institution is currently in compliance with Standard 3 (Institutional Resources)." Standard 3 requires, among other things, that an institution demonstrate that it has sufficient resources to support both its programs of study and students' academic progress. As required by Middle States, the university submitted a monitoring report on September 1, 2016, documenting the implementation of a technology plan, the development and implementation of a long-term financial plan, steps taken to strengthen the institution's finances, and cash and financial projections for the next five years. As further required, the report details steps taken to assure continuity and stability of institutional leadership and the use of assessment results to improve programs and services.

To address the above, the university has furloughed senior management employees and realigned staff positions and responsibilities. It has discontinued seven graduate degree programs and eight baccalaureate degree programs, and has placed another 11 undergraduate degree programs into moratorium status while students are being taught out. The university continues to contract with the third-party consultant who completed the financial aid analysis to provide full service administration of the university's federal financial aid programs and functions. With assistance from the Office of the Chancellor, the university has contracted with a third party to administer its information technology systems and has begun the outsourcing of its administrative functions, including finance, human resources, and facilities, to nearby West Chester University of Pennsylvania. This outsourcing, which is expected to improve services and achieve costs savings, will be fully implemented by spring 2017.

Insurance

The State System is self-insured for workers' compensation up to stated limits (note 6). For all other risks of loss, the State System pays annual premiums to the Commonwealth to participate in its Risk Management Program. The State System does not participate in any public entity risk pools, and does not retain risk related to any aforementioned exposure, except for those amounts incurred relative to policy deductibles that are not significant. The State System has not significantly reduced any of its insurance coverage from the prior year. Settled claims have not significantly exceeded the State

System's insurance coverage in any of the past three years. It is not expected that the resolution of any outstanding claims and litigation will have a material adverse effect on the accompanying financial statements.

Construction Commitments

Authorized expenditures for construction projects unexpended as of June 30, 2016 and 2015, were approximately $91,192,000 and $69,604,000, respectively.

(14) Subsequent Events

In September 2016, PHEFA issued Series AT-1 tax-exempt revenue bonds in the amount of $279,050,000 and Series AT-2 taxable revenue bonds in the amount of $19,060,000. The net proceeds from the Series AT revenue bonds were used to finance capital projects at several universities and to purchase certain student housing projects constructed by respective affiliated organizations. In connection with the bond issuance, the State System entered into a loan agreement with PHEFA under which the State System pledged its full faith and credit for repayment of bonds.

In September 2016, after more than a year of contract negotiations with the State System, the Association of Pennsylvania State College and University Faculties (APSCUF), which represents all faculty and coaches, voted to authorize union leaders to call a strike if and when it is considered necessary. APSCUF has been working under the terms of a contract that expired June 30, 2015. The short- or long-term financial impact of a strike on the universities and their students cannot be estimated but could be severely detrimental. As of the date of these financial statements, negotiations between the State System and APSCUF are continuing.

REQUIRED SUPPLEMENTARY INFORMATION

Years Ended June 30, 2016 and 2015
(Unaudited)

Schedule of Funding Progress for the System Plan (OPEB)

(in thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ([b-a]/c)
July 1, 2012	$0	$1,420,502	$1,420,502	0%	$566,753	251%
July 1, 2013	$0	$1,473,632	$1,473,632	0%	$583,755	252%
July 1, 2014	$0	$1,194,849	$1,194,849	0%	$589,917	203%

Schedule of Funding Progress for the REHP (OPEB)

(in thousands)

The information below relates to the Commonwealth's REHP as a whole; i.e., it is inclusive of all participating Commonwealth agencies and instrumentalities. Nearly all Commonwealth agencies and instrumentalities participate in the REHP.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ([b-a]/c)
July 1, 2012	$71,630	$12,843,700	$12,772,070	.56%	$4,130,000	309%
July 1, 2013	$82,060	$13,234,040	$13,151,980	.62%	$4,264,000	308%
January 1, 2015	$144,744	$16,134,419	$15,989,675	.90%	$4,289,000	373%

Schedule of Proportionate Share of SERS Net Pension Liability (NPL)

Determined as of SERS December 31 measurement date
(in thousands)

Fiscal Year	State System's Proportion	State System's Proportionate Share	State System's Covered-Employee Payroll	State System's Proportionate Share of NPL as a Percentage of Covered-Employee Payroll	SERS Fiduciary Net Position as a Percentage of Total Pension Liability
2014/15	4.901%	$728,094	$296,967	245%	64.8%
2015/16	4.721%	$858,417	$297,714	288%	58.9%

SERS Schedule of Contributions

Determined as of State System June 30 fiscal year end
(in thousands)

Fiscal Year	Contractually Required Contributions	Contributions Recognized by SERS in FY 2014/15	Contribution Deficiency (Excess)	Covered-Employee Payroll	Contributions as a Percentage of Covered-Employee Payroll
2014/15	$57,234	$57,234	$0	$293,506	19.50%
2015/16	$69,021	$69,021	$0	$291,594	23.67%

Schedule of Proportionate Share of PSERS Net Pension Liability

Determined as of PSERS June 30 measurement date
(in thousands)

	PSERS Net Pension Liability						
Fiscal Year	State System's Proportion	State System's Proportionate Share	Commonwealth's Proportionate Share	Total	State System's Covered-Employee Payroll	State System's Proportionate Share of NPL as a Percentage of Covered-Employee Payroll	PSERS Fiduciary Net Position as a Percentage of Total Pension Liability
2014/15	.1785%	$70,650	$70,650	$141,350	$45,552	155%	57.2%
2015/16	.1852%	$80,220	$80,220	$160,440	$47,670	168%	54.4%

PSERS Schedule of Contributions

Determined as of State System June 30 fiscal year end
(in thousands)

Fiscal Year	Contractually Required Contributions	Contributions Recognized by PSERS in FY 2014/15	Contribution Deficiency (Excess)	Covered-Employee Payroll	Contributions as a Percentage of Covered-Employee Payroll
2014/15	$5,236	$5,236	$0	$51,086	10.25%
2015/16	$6,012	$6,012	$0	$48,419	12.41%

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Appendix III

Summary of Legal Documents

Appendix III

SUMMARY OF LEGAL DOCUMENTS

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DEFINITIONS OF CERTAIN TERMS

The following definitions apply to the summaries of the Indenture and the Loan Agreement and to terms not otherwise defined in the Official Statement.

"Act" shall mean the Pennsylvania Higher Educational Facilities Authority Act of 1967, Act of December 6, 1967, P.L. 678, as from time to time amended or supplemented.

"Additional Bonds" shall mean Bonds duly executed, authenticated and delivered pursuant to the provisions of the Indenture, but shall not refer to or apply to any bonds issued under any other indenture or resolution of the Authority.

"Administrative Expenses" shall mean those expenses reasonably and properly incurred by the Authority in carrying out its responsibilities and duties, or in providing its services and facilities to the State System, under the Act or the Indenture or pursuant to the Loan Agreement or by the Authority in protecting its rights to indemnification pursuant to the Indenture and shall include the fees and expenses of the Trustee with respect to its duties under the Indenture.

"Annual Administrative Fee" shall mean the annual fee for the general administrative services of the Authority.

"Authority" shall mean the Pennsylvania Higher Educational Facilities Authority. "Authority Board" shall mean the governing body of the Authority.

"Authorized Officer" of the Authority or the State System shall mean a "Responsible Officer."

"Bond" or "Bonds" shall mean one of the notes or bonds or all of the notes or bonds, as the case may be, to be authenticated and delivered pursuant to the Indenture, including any Bond issued in lieu of or in exchange for such Bond.

"Bond Proceeds Fund" shall mean the special account so designated which is established and created pursuant to the Indenture.

"Bondowner", "owner" or "registered owner" or words of similar import, when used with reference to a Bond, shall mean any person who shall from time to time be the registered owner of any Outstanding Bond.

"Business Day" shall mean a date when the Trustee and the Authority are open for business.

"Certificate" shall mean (i) a signed document either attesting to or acknowledging the circumstances, representations or other matters therein stated or setting forth matters to be determined pursuant to the Indenture or (ii) the report of an accountant as to audit or other procedures called for by the Indenture.

"<u>Certified Resolution</u>" of the Authority or the State System shall mean a copy of one or more resolutions certified by the Secretary or Assistant Secretary of the Authority or the State System, as the case may be, under its seal to have been duly adopted by the Board of the Authority or the State System board, as the case may be, and to be in effect on the date of such certification.

"<u>Code</u>" shall mean the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

"<u>Commonwealth</u>" shall mean the Commonwealth of Pennsylvania.

"<u>Cost</u>" or "<u>Costs</u>" in connection with any Project, shall mean all expenses which are properly chargeable thereto under Generally Accepted Accounting Principles or which are incidental to the financing, acquisition and construction of such Project, including, but without limiting the generality of the foregoing:

amounts payable to contractors and costs incident to the award of contracts;

costs for labor, facilities and services furnished by or for the State System or an institution thereof or the Authority and their employees or others, materials and supplies purchased by the State System or an institution thereof or the Authority or others, and permits and licenses obtained by the State System, an institution thereof, the Authority or others;

engineering, legal, accounting and other professional and advisory fees;

premiums for surety bonds and insurance during construction and costs on account of personal injuries and property damage in the course of construction and insurance against the same;

interest during construction;

the Authority's initial fee and the Annual Administrative Fee and Administrative Expenses during the period prior to completion of any Project;

Costs of issuance of the Bonds;

fees and expenses in connection with the acquisition of real and personal property or rights therein, including premiums for title insurance;

costs of equipment purchased by the State System or an institution thereof and necessary for the completion and proper operation of any Project or property in question;

amounts required to repay temporary loans or advances from other funds of the State System or an institution thereof made to finance the Costs of any Project;

Costs of acquisition of real estate, construction and prior construction and/or site costs and improvements performed by the State System or any institution thereof in anticipation of any Project; and

moneys necessary to fund the Funds created under the Indenture.

"Debt Service" shall mean, with respect to any particular calendar year or Fiscal Year, an amount equal to the sum of (i) all interest payable on the Outstanding Bonds during such calendar year or Fiscal Year, respectively, plus (ii) the principal due on such Bonds during such calendar year or Fiscal Year, respectively.

"Debt Service Payment" shall mean with respect to any Interest Payment Date, the amount of interest and principal due.

"Depositary" shall mean any bank, trust company, national banking association, savings bank or savings and loan association, the unsecured debt obligations of which are rated at least an "A+" rating with the Rating Agency, selected by the Authority or the Trustee as a depositary of moneys or securities held under the provisions of the Indenture and permitted by law to be a depositary of Authority funds, and may include the Trustee, provided that all amounts held by the Depositary shall be in the name of the Trustee.

"Educational Facility" shall have the same meaning as used in the Act.

"Event of Default" shall mean any of the events specified in the Indenture or the Loan Agreement.

"Fiscal Year" shall mean a twelve-month period commencing on the first day of July of any year or any other twelve-month period as the Authority may by resolution determine from time to time, and shall include such shorter or longer period as the Authority shall deem advisable for transitional purposes.

"Forty-Third Supplemental Indenture" shall mean the Forty-Third Supplemental Indenture of Trust dated as of September 1, 2017, between the Authority and the Trustee and under which the Series AU Bonds will be issued.

"Forty-Third Supplemental Loan Agreement" shall mean the Forty-Third Supplemental Loan and Security Agreement dated as of September 1, 2016, between the Authority and the State System.

"Fund" shall mean one of the special funds created pursuant to the Indenture.

"Generally Accepted Accounting Principles" shall mean those accounting principles, not contrary to those promulgated by a nationally recognized financial standards body, applicable to the preparation of financial statements of institutions of higher learning or public authorities, as appropriate.

"Indenture" shall mean the Indenture of Trust dated as of June 1, 1985 between the Authority and the Trustee, as previously amended and supplemented, and as further supplemented by the Forty-Third Supplemental Indenture.

"Interest Payment Date" shall mean any date upon which interest on Bonds is due and payable in accordance with their terms.

"Investment Securities" shall mean and include any of the following obligations, to the extent the same are at the time legal for investment of funds of the Authority under the Act, including amendments thereto hereafter made, or under other applicable law:

direct obligations of or obligations guaranteed by the United States of America;

any bond, debenture, note, participation certificate or other similar obligation issued by any of the following agencies: Government National Mortgage Association, Federal Land Bank, Federal Home Loan Banks, Federal Intermediate Credit Banks, Federal Farm Credit Banks Consolidated Statewide, Tennessee Valley Authority, United States Postal Service, Farmers Home Administration, Export-Import Bank and Federal National Mortgage Association;

any other obligation of the United States of America or any federal agency to the payment of the principal of and interest on which the full faith and credit of the United States of America is pledged which may then be purchased with Authority funds or which are legal investments for savings banks, savings associations, or savings and loan associations in the Commonwealth but only if such investments are rated "AA" or better by the Rating Agency, or, upon the discontinuance of such service, another nationally recognized rating service;

tax-exempt obligations of any state or any instrumentality, agency or political subdivision thereof which are fully secured as to principal and interest by direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, the United States of America, and which are rated in the highest rating category by the Rating Agency and which are not by their terms subject to redemption prior to the date on which they are needed for the purposes for which they have been deposited;

direct and general obligations of any state of the United States, to the payment of which the full faith and credit of such state are pledged, but only if such obligations are rated "AA" or better by the Rating Agency, or, upon the discontinuance of such service, another nationally recognized rating service;

deposits in interest-bearing time or demand deposits, or certificates of deposit, with an institution the unsecured deposits of which are rated "AA" or better by the Rating Agency at the time of purchase, or, upon discontinuance of such service, another nationally recognized rating service;

repurchase agreements with an institution rated "A+" or better by the Rating Agency, or, upon discontinuance of such service, another nationally recognized rating service;

commercial paper (except that of the Authority or an affiliate) or finance company paper rated "A-1" by Standard & Poor's Corporation;

investment agreements with an entity whose unsecured debt obligations are rated not less than "AA" by the Rating Agency;

interest bearing time deposits or certificates of deposit (such deposits or certificates of deposit may be in or issued by the Trustee), or other similar banking arrangements with the Trustee or a member bank or banks of the Federal Reserve System or a bank, the deposits of which are insured by the Federal Deposit Insurance Corporation or its successor, or a savings and loan association, the deposits of which are insured by the Federal Savings and Loan Insurance Corporation or its successor. Each such interest bearing time deposit or certificate shall be fully insured by the United States of America or the federal corporations enumerated above;

certificates of participation, lease and sublease obligations or other similar instruments evidencing the leasing or subleasing of capital assets to any state of the United States whose general obligation bonds are rated "AA" or better by the Rating Agency at the time of purchase, or, upon discontinuance of such service, another nationally recognized rating service; or

shares or certificates in any short-term investment fund, which short-term investment fund invests not less than 98% of its assets in obligations described in subparagraphs (1) through (11) above, including, without limitation, any mutual fund for which the Trustee or an affiliate of the Trustee serves as investment manager, administrator, shareholder servicing agent, and/or custodian or subcustodian, notwithstanding that (i) the Trustee or an affiliate of the Trustee receives fees from such funds for services rendered, (ii) the Trustee charges and collects fees for services rendered pursuant to the Indenture, which fees are separate from the fees received from such funds, and (iii) services performed for such funds and pursuant to the Indenture may at times duplicate those provided to such funds by the Trustee or its affiliates.

"Loan Agreement" shall mean the Loan and Security Agreement dated as of June 1, 1985, between the Authority, as lender, and the State System, as borrower, as previously amended and supplemented and as further supplemented by the Forty-Third Supplemental Loan Agreement.

"Outstanding" when used with reference to Bonds, shall mean, as of any date, all Bonds theretofore or thereupon being authenticated and delivered under the Indenture except:

any Bond canceled by the Trustee or the Authority at or prior to such date;

any Bond (or portion of a Bond) for the payment or redemption of which there shall be held in trust and set aside either:

(a) moneys in an amount sufficient to effect payment when due of the principal or the applicable Redemption Price thereof, together with all accrued interest, or

(b) Investment Securities as described in clauses (1), (2) and (4) of the definition of Investment Securities above in such principal amounts, of such maturities, bearing such interest, and otherwise having such terms and qualifications, as shall be necessary to provide moneys (whether as principal or interest) in an amount sufficient to effect payment when due of the principal or applicable Redemption Price thereof, together with all accrued interest, or

(c) any combination of (a) and (b) above,

and, if such Bond or portion of a Bond is to be redeemed, for which notice of redemption shall have been given or provision satisfactory to the Trustee shall have been made for the giving of such notice;

any Bond in lieu of or in substitution for which other Bonds shall have been authenticated and delivered pursuant to the Indenture; and

any Bond deemed to have been paid as provided in the Indenture.

"Pledged Revenues" shall mean all amounts payable by the State System to the Authority under the Loan Agreement (except those representing the Annual Administrative Fee and Administrative Expenses of the Authority).

"Project" shall mean each individual Educational Facility financed under the Indenture and shall include acquiring, holding, constructing, improvement, maintaining and operating by the State System or an institution thereof, of grounds, premises, buildings, and other property constituting "educational facilities" as defined in the Act and used or useful in providing construction, housing, recreation, or other services related to higher education and related activities, including the financing of the Costs thereof by the Authority and the refinancing by the Authority of the Cost of Educational Facilities previously financed. Project shall also include refunding or redeeming any Outstanding Bonds.

"Rating Agency" shall mean Standard & Poor's Corporation or Moody's Investors Service, Inc. or Fitch Ratings or any successor thereto.

"Record Date" shall mean, with respect to fixed rate issues, the close of business on the fifteenth day of the calendar month preceding an Interest Payment Date if the Interest Payment Date is on the first day of the month and the first day of the month when an Interest Payment Date is on the fifteenth day of a month, and shall mean with respect to variable rate issues, the close of business on the last Business Day preceding an Interest Payment Date, unless a Special Record Date is otherwise defined and provided for in any Supplemental Indenture.

"Redemption Date" shall mean the date upon which any Bond is to be called for redemption pursuant to the Indenture.

"Redemption Fund" shall mean the special fund so designated which is established and created pursuant to the Indenture.

"Redemption Price" shall mean, with respect to any Bond or portion thereof, the amount payable upon redemption thereof, not including interest, if any, accrued to the Redemption Date.

"Resolution" shall mean the resolution or resolutions of the Authority authorizing the issuance of Bonds and the execution and delivery of the Indenture.

"Responsible Officer" shall mean (i) when used with respect to the Authority, the President, any Vice President, the Secretary, any Assistant Secretary, the Treasurer, any Assistant Treasurer, the Controller, the Assistant Controller, the Executive Director or any Assistant Executive Director, (ii) when used with respect to the State System, the Chancellor, Vice Chancellor, President, Chairperson, Vice Chairperson or any person designated as an Administrative Officer by Certificate of the State System, and (iii) when used with respect to either the State System or the Authority, as the case may be, any other person designated by certified resolution of the Board of the Authority or the State System to act for any of the foregoing, either generally or with respect to the execution of any particular document or other specific matter, a certified copy of which resolution shall be on file with the Trustee.

"Revenues" shall mean all unrestricted receipts, revenues, income, gains and all other moneys received by the State System from any source, including without limitation, tuition and fee revenues, Commonwealth appropriations and other operating and non-operating revenues required to be recorded as revenue under Generally Accepted Accounting Principles, exclusive of net assets released from restriction, gifts, grants, bequests and donations which are designated by the donor at the time of making as being for specific purposes.

"Revenue Fund" shall mean the special fund so designated which is established and created pursuant to the Indenture.

"Series AG Bonds" shall mean the Authority's Refunding Revenue Bonds, State System of Higher Education, Series AG, issued under the Indenture.

"Series AH Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AH, issued under the Indenture.

"Series AI Bonds" shall mean the Authority's Refunding Revenue Bonds, State System of Higher Education, Series AI, issued under the Indenture.

"Series AJ Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AJ, issued under the Indenture.

"Series AK Bonds" shall mean the Authority's Refunding Revenue Bonds, State System of Higher Education, Series AK, issued under the Indenture.

"Series AL Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AL, issued under the Indenture.

"Series AM Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AM, issued under the Indenture.

"Series AN Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AN, issued under the Indenture.

"Series AO Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AO, issued under the Indenture.

"Series AP Bonds" shall mean the Authority's Refunding Revenue Bonds, State System of Higher Education, Series AP, issued under the Indenture.

"Series AQ Bonds" shall mean the Authority's Refunding Revenue Bonds, State System of Higher Education, Series AQ, issued under the Indenture.

"Series AR Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AR, issued under the Indenture.

"Series AS Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AS, issued under the Indenture.

"Series AT Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AT, issued under the Indenture.

"Series AT Insurer" shall mean Assured Guaranty Municipal Corp.

"Series AU Bonds" shall mean the Authority's Revenue Bonds, State System of Higher Education, Series AU, issued under the Indenture.

"Series AU Project" shall mean the issuance of the Authority's Series AU Bonds and the application of the proceeds to the costs included in the "Project" as defined in and for purposes of the forepart of this Official Statement.

"Sinking Fund Payment" shall mean, as of any particular date of calculation, the amount required to be paid in all events on a single future date for the retirement of Outstanding Bonds which mature after said future date, but does not include any amount payable by reason of the maturity of a Bond.

"State System of Higher Education" or "State System" or "System" shall mean the State System of Higher Education, a body corporate and politic constituting a public corporation and governmental instrumentality consisting of institutions of higher education recognized by the Board of Education of the Commonwealth.

"Supplemental Indenture" shall mean any indenture supplemental to or amendatory of the Indenture, executed and delivered by the Authority and effective in accordance with the Indenture.

"Trustee" shall mean The Bank of New York Mellon Trust Company, N.A., or its successor or successors, as successor trustee under the Indenture.

"Trust Estate" shall mean the security for the Bonds granted to the Trustee by the Authority in the granting clauses under the Indenture.

SUMMARY OF LEGAL DOCUMENTS

The following are summaries of certain provisions of the Loan Agreement and the Indenture. The summaries should not be regarded as full statements of the documents themselves or of the portions summarized. For complete statements of the provisions thereof, reference is made to the documents in their entireties, copies of which will be available for inspection at the principal corporate trust office of the Trustee.

THE LOAN AGREEMENT

The Loan Agreement, as previously supplemented and as further supplemented by the Forty-Third Supplemental Loan Agreement, was entered into between the Authority, as lender, and the State System, as borrower.

(i) The Projects

The State System shall use the proceeds of the Bonds in accordance with the Loan Agreement to undertake the Projects, including the Series AU Project, from time to time authorized thereunder and under the Indenture.

(ii) Agreement to Lend; Use of Bond Proceeds

Under the Loan Agreement, the Authority agrees to make, solely from the proceeds of Bonds, and the State System agrees to accept, the loans of Bond proceeds to finance the Costs of Projects. The State System agrees to accept disbursement of the proceeds of such loans to be used in the manner provided in the Indenture, including the construction and/or renovation, improvement and installation of the Projects and the making of all payments required by the Loan Agreement as and when the same shall become due.

(iii) Loan Repayments and Additional Sums

The Loan Agreement is a general obligation of the State System and the full faith and credit of the State System is pledged to the payment of all sums due thereunder. The State System shall pay to the Trustee, as assignee of the Authority, for deposit in the Revenue Fund created under the Indenture, the following amounts in immediately available funds: (a) with respect to fixed rate issues, fifteen days prior to an Interest Payment Date, and with respect to variable rate issues, no later than one day prior to an

Interest Payment Date, an amount which is sufficient to pay interest on the Bonds to be paid on the next Interest Payment Date (taking into account as a credit against such installments, any amounts representing accrued and capitalized interest on deposit in any account of the Bond Proceeds Fund and moneys on deposit in the Revenue Fund for such purpose) and (b) principal of the Bonds due (at stated maturity or through sinking fund redemption) and (c) in each year, the State System shall pay directly to the Authority its Annual Administrative Fees and, when due, the Authority's Administrative Expenses incurred from time to time in connection with the Projects, as provided in the Indenture.

In lieu of the portion of the loan repayments payable with respect to principal of the Bonds becoming due (at stated maturity or through sinking fund redemption) on the next following principal or sinking fund payment date, the State System, or at its direction, the Authority, may purchase on the open market Bonds of the maturity becoming due and present such Bonds to the Trustee for cancellation. The Bonds so presented to the Trustee shall be credited to the principal amount of the next payment due thereunder at 100% of the principal amount of such Bonds.

The State System may make advance payments as required or permitted by the Loan Agreement. So long as any of the Bonds remain Outstanding, the obligation of the State System to pay sums due under the Loan Agreement shall be absolute and unconditional and shall not be suspended, abated, reduced, abrogated, waived, diminished or otherwise modified in any manner or to any extent whatsoever, regardless of any rights of setoff, recoupment or counterclaim that the State System might otherwise have against the Authority or the Trustee or any other party or parties and regardless of any contingency, act of God, event or cause whatsoever and notwithstanding any circumstances or occurrence that may arise or take place after the date of the Loan Agreement.

(iv) Concerning the Projects

The State System will undertake and proceed to complete any Projects financed by the Authority under the Loan Agreement with all reasonable dispatch and will use its best efforts to complete or cause the completion of such component parts to take place on or before the dates specified in the Indenture or as soon thereafter as may be practicable, except for delays incident to strikes, riots, acts of God or the public enemy or any delay beyond the reasonable control of the State System; but if for any reason the State System's undertakings with respect to any Project shall not be completed by such dates there shall be no resulting diminution in or postponement of the loan repayments required to be made by the State System under the Loan Agreement.

The State System shall enforce any construction contracts and purchase orders relating to a Project and will cause the State System's undertakings with respect to such Project to be completed substantially in accordance with any plans and specifications which may have been prepared therefor.

The State System agrees to obtain, or cause to be obtained, in connection with the construction of any Project, a surety bond or bonds covering performance of contracts and payment for labor and materials. Such bonds shall be executed by responsible surety companies and shall be in amounts aggregating not less than 100% of the contract price. The State System shall have the exclusive right to receive the proceeds of such bonds.

The State System will not do or refrain from doing any act whereby any surety on any bond may be released in whole or in part from any obligations assumed by it or from any agreement to be performed by it under any surety bond and the State System will comply with all present and future laws, acts, rules, regulations, orders, and requirements lawfully made relating to any acquisition or construction undertaken in accordance with the Loan Agreement.

The State System may amend the plans and specifications, if any, at any time prior to the completion date thereof, including amendments which change the proposed allocation of moneys in the account established for the State System in the Bond Proceeds Fund among components of such Project or which delete components of its undertakings under the Loan Agreement with respect to the Project. No such changes shall be made, and no amendment shall be made to the plans and specifications, if any, which shall so modify the State System's undertakings with respect to a Project that they fail to qualify as Educational Facilities eligible for assistance by the Authority under the Act.

The State System is also required to maintain builder's risk insurance (or equivalent coverage) upon work done or materials furnished (except excavations, foundations and other structures not customarily covered), worker's compensation insurance, employer's liability insurance and public liability, comprehensive automobile liability insurance and property insurance with respect to construction of new facilities.

(v) Costs of Projects

The State System shall direct to the Trustee requisitions for payment of proper Costs with respect to the Projects in accordance with the procedures established in the Indenture; provided, however, that the State System shall not submit any requisition which, if paid, would result in the proceeds of the Bonds being used other than to pay the Costs of the State System's undertakings with respect to a Project.

(vi) Completion of Projects

Under the Loan Agreement, the State System is obligated to complete its undertakings with respect to Projects at its own expense regardless of the adequacy of the moneys allocated to the State System in any particular account established in the Bond Proceeds Fund under the Indenture or the adequacy of other moneys made available to the State System by the Authority. The Authority makes no warranty, either express or implied, that the amounts to be deposited pursuant to the Indenture in any account established for the State System in the Bond Proceeds Fund will be sufficient to complete payment of the Costs of any Projects. The State System agrees that if, after exhaustion of the moneys allocated to the State System in the account established for the State System in the Bond Proceeds Fund and any other moneys made available by the Authority, the State System should pay any portion of the Costs of a Project, it shall not be entitled to any reimbursement therefor from the Authority, the Trustee or the owners of any of the Bonds, nor shall it be entitled to any diminution in or postponement of the amounts payable under the Loan Agreement.

(vii) Additional Projects

In the event that the State System should wish to undertake an additional Project with unused balances in the account established for the State System in the Bond Proceeds Fund (whether because of the deletion of a component of the State System's undertakings with respect to the Project or otherwise), the State System may provide for the payment of the Costs of such additional Project from the unused balances in such account in the Bond Proceeds Fund, provided that it shall comply with the foregoing requirements with respect to changes in a Project, and provided further that both an Officer's Certificate of the Authority to the effect that the additional Project is duly authorized under the Act and applicable Authority resolutions shall have been delivered.

(viii) Assignment to Trustee

The Authority shall assign the Loan Agreement and all sums payable under the Loan Agreement (other than amounts representing payments of the Authority's Annual Administrative Fees and Administrative Expenses and amounts representing the Authority's rights to indemnification pursuant to the Loan Agreement), to the Trustee, in trust, to be held and applied pursuant to the provisions of the Indenture. The State System (1) consents to the assignment to the Trustee and accepts notice thereof; (2) agrees to pay directly to the Trustee all such sums without any defense, set-off or counterclaim arising out of any default on the part of the Authority under the Loan Agreement or any transaction between the State System and the Authority; and (3) agrees that the Trustee may exercise all rights granted the Authority thereunder.

(ix) Additional Authority Financing

If the State System shall deem it necessary or advisable that additional Projects be undertaken, or if it is deemed necessary by the State System to refund Outstanding Bonds or obtain additional financing for the completion of a Project, the State System may request the Authority to provide a loan for all or part of Costs thereof. Upon receipt of a request of the State System, the Authority shall use its best efforts to provide such money from available sources under the Indenture or through the issuance of Additional Bonds or other evidences of indebtedness of the Authority.

(x) Certain Additional Covenants of the State System

The State System represents and covenants in the Loan Agreement that it is (i) a body corporate and politic constituting a public corporation and governmental instrumentality; (ii) organized and operated exclusively for educational purposes; and (iii) not for pecuniary profit. The State System agrees that it shall not perform any act nor enter into any agreement which shall change such status.

The State System covenants that it will preserve and maintain its existence as a public corporation under the laws of the Commonwealth, and to the extent permitted by law at any given time, remain free from Federal, state and local income, property, franchise and other taxes, and preserve and maintain its authority to operate the Projects.

The State System covenants that it will maintain the necessary accreditation to enable it to maintain its authority to operate its constituent educational institutions as institutions of higher education in the Commonwealth within the meaning of the Act.

The State System covenants that throughout the term of the Loan Agreement:

(A) it will take whatever actions are necessary to continue to be organized and operated in a manner which will preserve and maintain the exemption from federal income taxation of the State System; and

(B) it will not perform any acts nor enter into any agreements which shall cause any revocation or adverse modification of such federal income tax status of the State System; and

(C) it will not carry on or permit to be carried on in any Project (or with Bond proceeds or the proceeds of any loan refinanced with Bond proceeds) any trade or business the conduct of which would cause the interest paid by the Authority on the Bonds to be subject to Federal income tax in the hands of the owners thereof; and

(D) it will not take any action or permit any action to be taken on its behalf, or cause or permit any circumstances within its control to arise or continue, if such action or circumstances would cause the interest paid by the Authority on the Bonds to be subject to Federal income tax in the hands of the owners thereof; and

(E) neither it nor any person related to it within the meaning of the Code, pursuant to an arrangement, formal or informal, will purchase the Bonds in an amount related to the total amount payable under and secured by the Loan Agreement.

The State System covenants that it shall not pledge more than twenty percent (20%) of its Revenues to secure any indebtedness it may incur or guaranties it may undertake without simultaneously granting such a lien for the benefit of the Bonds.

The State System further covenants that:

(1) during the term of the Loan Agreement it will not initiate any proceedings or take any action whatsoever to dissolve or liquidate or to terminate its existence as a public corporation or otherwise dispose of all or substantially all of its assets, or the Projects, either in a single transaction or in a series of related transactions, except as provided in the Loan Agreement.

(2) it shall pay or cause to be paid to the public officers charged with the collection thereof, promptly as the same become due, all taxes (or contributions or payments in lieu thereof).

(3) it will, at its own expense, keep and maintain or cause to be kept and maintained the Projects in good order, repair and operating condition.

(4) all actions taken by the State System to acquire and carry out the Projects, including the making of contracts or the entering into of purchase orders, have been and will be in full compliance with all pertinent laws, ordinances, rules, regulations and orders applicable to the State System.

(5) it will keep accurate records and books of account with respect to the revenues and expenses of the State System in accordance with generally accepted accounting principles and, within 150 days after the end of each Fiscal Year during the term of the Loan Agreement, provide a statement of revenue and expenses to the Authority and the Trustee.

(6) the Authority, by its duly authorized representatives, at reasonable times, and for purposes of determining compliance with the Loan Agreement and confirming the progress and completion of a Project, may inspect any part of a Project.

(xi) Events of Default and Remedies

"Events of Default" as defined in the Loan Agreement include the State System's failure:

(1) to make payments required under Section 4.01 thereof relating to payment of the principal of and interest on Bonds when the same shall become due and payable;

(2) to make any other payment required thereunder and such failure continues for 10 days after the Authority or the Trustee gives notice that such other payment is due and unpaid; or

(3) to perform any of its other covenants or to perform any of its obligations under the Loan Agreement and such failure continues for 60 days after the Authority gives the State System notice thereof; provided, however, that if such performance requires work to be done, actions to be taken, or conditions

remedied, which by their nature cannot reasonably be done, taken or remedied, as the case may be, within such 60-day period, no Event of Default shall be deemed to have occurred or to exist if, and so long as, the State System shall commence such performance within such 60-day period and shall diligently and continuously prosecute the same to completion.

An "Event of Default" also occurs if the State System shall become insolvent or unable to pay its debts as they mature, or shall file a voluntary petition seeking reorganization or to effect a plan or other arrangement with creditors, or shall file an answer admitting the jurisdiction of the court and the material allegations of an involuntary petition, pursuant to any act relating to bankruptcy or to any act purporting to be amendatory thereof, or shall be adjudicated bankrupt or insolvent, or shall make an assignment for the benefit of creditors or to an agent authorized to liquidate any substantial amount of its assets, or shall apply for or consent to or suffer the appointment of any receiver or trustee for it or a substantial part of its property or assets; or a proceeding shall be instituted, without the application, approval or consent of the State System pursuant to any act relating to bankruptcy or to any act purporting to be amendatory thereof, seeking (i) adjudication of the State System as bankrupt or insolvent, (ii) reorganization of, or an order appointing any receiver or trustee for a substantial part of the property or assets of the State System, or (iii) issuance of a writ of attachment or any similar process against a substantial part of the property or assets of the State System and any such proceeding shall result in the entry of an order for relief or any such adjudication or appointment shall continue undismissed, or pending and unstayed, for any period of 30 consecutive days.

If any of the foregoing Events of Default shall happen, then and at any time thereafter while such Event of Default is continuing, the Authority may, in addition to its other remedies at law or equity or provided for in the Loan Agreement, if the Trustee shall have declared the principal of any Bonds then Outstanding to be immediately due and payable pursuant to the Indenture, with the prior written consent of the Trustee, declare amounts payable under the Loan Agreement to be immediately due and payable; then there shall become due and payable under the Loan Agreement as then current damages an amount equal to the principal of all Bonds so declared to be immediately due and payable plus accrued interest to the date of payment of such Bonds and all other amounts then due and payable under the Loan Agreement to the Authority. Until said amounts are paid by the State System, the Authority shall continue to have all of the rights, powers and remedies herein set forth, and the State System's obligations thereunder shall continue in full force and effect.

(xii) Amendment of Loan Agreement

The Authority and the State System may execute an appropriate supplement or amendment to the Loan Agreement in connection with the issuance of Additional Bonds as contemplated by the Indenture. In addition, the Authority and the State System may enter into any written amendments to the Loan Agreement as shall not adversely affect the rights of or the security of the owners of the Bonds, only for the following purposes:

(1) to cure any ambiguity, defect, or inconsistency or omission in the Loan Agreement or any amendment thereto;

(2) to grant to or confer upon the Authority any additional rights, remedies, powers, authority or security that lawfully may be granted to or conferred upon it;

(3) to reflect a change in applicable law; or

(4) to provide terms not inconsistent with the Indenture or the Loan Agreement; provided, however, that the Loan Agreement as so amended or supplemented shall provide at least the same security for owners of Bonds issued under the Indenture as the Loan Agreement prior to such amendment.

All other amendments to the Loan Agreement must be approved by the Trustee and, if the Indenture must be amended with the Bondowners' consent, by the Bondowners also, in the same manner and to the same extent as is set forth in the Indenture.

THE INDENTURE

The Series AU Bonds are being issued under and subject to the provisions of the Indenture to which reference must be made for complete details of the terms of the Series AU Bonds as well as the Series AG Bonds, the Series AH Bonds, the Series AI Bonds, the Series AJ Bonds, the Series AK Bonds, the Series AL Bonds, the Series AM Bonds, the Series AN Bonds, the Series AO Bonds, the Series AP Bonds, the Series AQ Bonds, the Series AR Bonds, the Series AS Bonds, the Series AT Bonds, the Series AU Bonds and any other Additional Bonds which may be issued under the Indenture.

(i) Pledge and Assignment

The Bonds are limited obligations of the Authority payable under the Indenture solely from the Trust Estate. Under the Indenture, the Pledged Revenues payable to the Authority from the State System under the Loan Agreement and all income and receipts earned on funds held by the Trustee under the Indenture have been pledged to the Trustee for the equal and ratable benefit (except as set forth in the Indenture) of the registered owners of all Bonds Outstanding under the Indenture. The rights of the Authority under the Loan Agreement (other than the rights to receive payment of its Annual Administrative Fees and Administrative Expenses and the Authority's right to receive indemnification pursuant to the Loan Agreement) have been assigned to the Trustee to secure the payment of the Bonds and the performance and observance of the covenants in the Indenture.

(ii) Disposition of the Proceeds of the Sale of the Series AU Bonds

Upon the issuance and delivery of the Series AU Bonds, the Authority shall forthwith transfer the proceeds to the Trustee and the Trustee shall deposit the same in the Settlement Account of the Bond Proceeds Fund established under the Indenture and the Forty-Third Supplemental Indenture to be transferred and applied upon the order of the Authority and approved by the State System. From the proceeds of the Series AU Bonds, the Trustee shall make the following transfers or expenditures from the Settlement Account: (1) amounts representing accrued interest on the Series AU Bonds shall be transferred to an account established in the Revenue Fund and applied to the payment of interest on the Series AU Bonds on the first Interest Payment Date following issuance thereof, (2) payment of the costs of issuance of the Series AU Bonds shall be paid, and (3) the balance remaining shall be transferred to the Series AU Account of the Revenue Fund for application to the payment of the Series AU Project in accordance with the procedures established in the Indenture.

(iii) Additional Bonds

Under the Indenture, the Authority is authorized to issue, at the request of the State System under the Loan Agreement, Additional Bonds for the purpose of undertaking any additional Projects on behalf of the State System or to refund any prior series of Bonds outstanding under the Indenture. Such Additional Bonds, if issued, will be equally and ratably secured under the Indenture with the Series AG Bonds, the Series AH Bonds, the Series AI Bonds, the Series AJ Bonds, the Series AK Bonds, the Series AL Bonds, the Series AM Bonds, the Series AN Bonds, the Series AO Bonds, the Series AP Bonds, the Series AQ Bonds, the Series AR Bonds, the Series AS Bonds, the Series AT Bonds and the Series AU Bonds except to the extent expressly limited under the Indenture.

(iv) Establishment of Funds

The "Bond Proceeds Fund" established under the Indenture shall contain funds deposited therein pursuant to the Indenture and shall be expended only (i) to pay the cost of financing a Project, (ii) to pay Costs of issuance, and (iii) to pay accrued and capitalized interest on Bonds. Under the Indenture, the Trustee is directed to establish separate accounts in which to deposit proceeds of the various series of Bonds. Amounts in the Bond Proceeds Fund or any account established therein shall be held for the benefit of all Bonds Outstanding under the Indenture (other than with respect to any capitalized interest account created for a specific series of Bonds which shall be held and applied solely for the particular specified Bonds).

Payments shall be made from any account of the Bond Proceeds Fund to pay Costs of each Project, but only upon receipt by the Trustee of the requisitions and certifications required by the Indenture. Upon the completion of each Project, evidenced in the manner provided in the Indenture, amounts in the applicable account of the Bond Proceeds Fund may, at the option of the Authority upon the direction of the State System, be transferred to the Revenue Fund to be applied to the payment of Debt Service on the applicable series of Bonds or to the redemption of Bonds or to any other account of the Bond Proceeds Fund to be used to pay costs of additional Projects.

The "Revenue Fund" established under the Indenture shall contain Pledged Revenues of the Authority received by the Trustee under the Loan Agreement. Under the Indenture, the Trustee is directed to establish separate accounts within the Revenue Fund in connection with each series of Bonds. Moneys in the Revenue Fund are pledged for the equal and ratable benefit of all Bonds Outstanding under the Indenture, except as expressly limited by the Indenture.

The Trustee shall pay out of the Revenue Fund the following amounts in the following order, on the dates specified, for the following purposes (i) on each Interest Payment Date, the amounts required, taking into consideration the amounts otherwise available, for the payment of principal, Sinking Fund Payments, Redemption Price, if any, and interest due on the Outstanding Bonds on such date; (ii) on the Redemption Date or date of purchase of Bonds the amounts required for the payment of accrued interest on Bonds redeemed or purchased for retirement, unless the payment of such accrued interest shall be otherwise provided for; (iii) upon the written direction of the Authority on each Interest Payment Date to the payment of certain fees and expenses of the Trustee, including costs of redemption of Bonds; and (iv) all remaining amounts shall be transferred to the Redemption Fund upon the written direction of the Authority at the request of the State System.

The "Redemption Fund" shall contain amounts which are required to be deposited therein pursuant to the Indenture and any other amounts available therefor and determined by the State System pursuant to the Loan Agreement to be deposited therein subject to the provisions of the Indenture, and the Trustee shall apply all amounts so deposited to the redemption of Bonds. At any time prior to the date upon which notice is given that Bonds are to be redeemed from such amounts, the Trustee shall apply any amounts in the Redemption Fund to the purchase of any of the Bonds which may be redeemed by application of such amounts upon the direction of the Authority at the written direction of the State System. The Trustee shall purchase Bonds at such times, for such prices, in such amounts and in such manner as the Authority upon written direction of the State System shall from time to time direct.

(v) Deposits

In order to permit any amount to be available for use at the time when needed, amounts held under the Indenture by the Trustee or any Depositary, as such, may if and as directed by the State System, be deposited in the commercial banking department of the Trustee or Depositary which may honor checks and drafts on such deposit with the same force and effect as if it were not such Trustee or Depositary. The Trustee or Depositary shall allow and credit on such amounts at least such interest, if any, as it customarily allows upon similar funds of similar size and under similar conditions or as required by law.

All amounts deposited by the Trustee or Depositary shall be continuously and fully secured (a) by lodging with the Trustee, as custodian, as collateral security, Investment Securities having a market value (exclusive of accrued interest) not less than the amount of such deposit, and (b) in such manner as may then be required by applicable federal or state laws and regulations regarding security for the deposit of public funds provided that in no event shall such security be in an amount less than such deposit. It shall not be necessary, unless required by applicable law, for the Trustee to give security for the deposit of any amounts to the extent that such deposit is insured by the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation, or their respective successors, or which are held in trust and set aside by them for the payment of the principal or Redemption Price of or interest on any Bonds, or for the Trustee or any Depositary to give security for any moneys which shall be represented by obligations or certificates of deposit purchased as an investment of such moneys.

All amounts so deposited by the Trustee or Depositary shall be credited to the particular Fund from which such amounts were derived.

(vi) Investment of Funds

Moneys in any Fund shall be continuously invested and reinvested and/or deposited and redeposited by the Trustee, as permitted in the Indenture, as the State System shall direct the Trustee in writing. The State System shall consult with the Trustee from time to time as to the investment of amounts in the Funds and Accounts established or confirmed by the Indenture. Except as otherwise provided herein, the State System shall give written directions to the Trustee to invest and reinvest the moneys in said Funds and Accounts in Investment Securities so that the maturity date or date of redemption at the option of the holder thereof shall coincide as nearly as practicable with the times at which moneys are needed by the Authority to be so expended. The Investment Securities purchased shall be held by the Trustee and shall be deemed at all times to be part of such Fund or Account, and the Trustee shall keep the Authority and the State System advised as to the details of all such investments.

Except as otherwise provided therein, Investment Securities purchased as an investment of moneys in any Fund held by the Trustee under the provisions of the Indenture shall be deemed at all times to be a part of such Fund, but the income or interest earned and gains realized in excess of losses suffered by a Fund due to the investment thereof may be deposited in the Bond Proceeds Fund during the construction period of any Project and thereafter shall be deposited in the Revenue Fund as Pledged Revenues or shall be credited to the Revenue Fund from time to time as Pledged Revenues and reinvested.

Except as otherwise provided herein, the Trustee shall sell at the best price obtainable with reasonable diligence, or present for redemption or exchange, any Investment Security purchased by it pursuant to the Indenture whenever it shall be necessary in order to provide moneys to meet any payment or transfer from the fund for which such investment was made. The Trustee shall advise the Authority and the State System in writing, on or before the twentieth day of each calendar month, or as soon as practicable thereafter of all investments held for the credit of each Fund in its custody under the provisions of the Indenture as of the last business day of the preceding month.

(vii) Valuation of Funds

In computing the amount in any Fund, obligations purchased as an investment of moneys therein shall be valued at the lower of cost or fair market value.

(viii) Covenants of the Authority

The Authority shall, among other things, promptly pay solely from the Trust Estate the principal or Redemption Price, if any, of every Bond and all interest thereon. The Authority shall preserve and protect the pledge of the Trust Estate, Pledged Revenues and other assets and revenues.

The Authority shall at all times do and perform all acts and things necessary in order to assure that interest paid on the Bonds shall, for the purposes of federal income taxation, be and remain excludable from the gross income of the recipients thereof and be and remain exempt from such taxation.

The Authority shall not permit at any time or times any of the proceeds of the Bonds or any other funds of the Authority to be used directly or indirectly to acquire any securities or obligations the acquisition of which would cause any Bond to be an "arbitrage bond" as defined in the Code. The Authority shall not permit at any time or times any proceeds of any Bonds or any other funds of the Authority to be used, directly or indirectly, in a manner which would result in the exclusion of any Bond from the treatment afforded by subsection (a) of Section 103 of the Code; and has covenanted with respect to the Series AU Bonds, to comply with all applicable provisions of the Code as from time to time in effect so as to maintain the federal tax exempt status of the interest payable on the Series AU Bonds, including, without limiting the generality of the foregoing, the arbitrage rebate provisions of Section 148(f) of the Code to the extent applicable.

Notwithstanding any terms, provisions or covenants to the contrary contained in the Indenture, the Authority shall not be prohibited from issuing obligations not exempt from federal income taxation so long as the tax exempt status of any Bonds Outstanding immediately prior to the issuance of such taxable obligations shall not be adversely affected thereby.

(ix) Additional Obligations

The Authority shall not create or permit the creation of or issue any obligations or create any additional indebtedness which will be secured by a superior or equal charge and lien on the revenues and assets pledged under the Indenture, except that Additional Bonds may be issued from time to time pursuant to a Supplemental Indenture of the Authority subsequent to the issuance of the initial issue of Bonds under the Indenture on a parity with the Bonds of such initial issue of Bonds and secured by an equal charge and lien on the revenues and assets pledged under the Indenture and payable equally therefrom (except for certain funds held under the Indenture).

(x) Supplements and Amendments

For any one or more of the following purposes and at any time or from time to time, a Supplemental Indenture of the Authority may be executed and delivered which, upon the filing with the Trustee of a copy thereof certified by an Authorized Officer of the Authority, shall be fully effective in accordance with its terms:

to close the Indenture against, or to provide limitations and restrictions in addition to the limitations and restrictions contained in the Indenture on, the authentication and delivery of Bonds; or

to add to the covenants and agreements of the Authority in the Indenture other covenants and agreements to be observed by the Authority which are not contrary to or inconsistent with the Indenture as theretofore in effect; or

to add to the limitations and restrictions in the Indenture other limitations and restrictions to be observed by the Authority which are not contrary to or inconsistent with the Indenture as theretofore in effect; or

to surrender any right, power or privilege reserved to or conferred upon the Authority by the terms of the Indenture, but only if the surrender of such right, power or privilege is not contrary to or inconsistent with the covenants and agreements of the Authority contained in the Indenture; or

to confirm, as further assurance, any pledge under, and the subjection to any lien or pledge created or to be created by, the Indenture, of the Pledged Revenues or of any other revenues or assets; or

to modify any of the provisions of the Indenture in accordance therewith; or

to provide for the issuance of Additional Bonds pursuant to the Indenture.

For any one or more of the following purposes and at any time or from time to time, a Supplemental Indenture may be entered into, which, upon (i) the filing with the Trustee of a copy thereof certified by an Authorized Officer, and (ii) the filing with the Trustee and the Authority of an instrument in writing made by the Trustee consenting thereto, shall be fully effective in accordance with its terms:

to cure any ambiguity, supply any omission, or cure or correct any defect or inconsistent provision in the Indenture; or

to insert such provisions clarifying matters or questions arising under the Indenture as are necessary or desirable and are not contrary to or inconsistent with the Indenture as theretofore in effect; or

to provide for additional duties of the Trustee.

Any other modification of or amendment to the Indenture and of the rights and obligations of the Authority and of the owners of the Bonds may be made by a

Supplemental Indenture, but only with the written consent of the owners of at least two-thirds in principal amount of the Bonds Outstanding at the time such consent is given. In case the modification or amendment changes the terms of any Sinking Fund Payment, the written consent of owners of at least two-thirds in principal amount of each of the Bonds entitled to such Sinking Fund Payment is required. No such modification or amendment shall permit a change in the terms of redemption or maturity of the principal of any Outstanding Bond or of any installment of interest thereon or a reduction in the principal amount or the Redemption Price thereof or in the rate of interest thereon without the consent of the holder of such Bond, or shall reduce the percentages or otherwise affect the classes of Bonds the consent of the owners of which is required to effect any such modification or amendment, or shall change or modify any of the rights or obligations of any fiduciary without its written assent thereto.

Upon the written consent of the owners of all the Bonds then Outstanding, the terms and provisions of the Indenture and the rights and obligations of the Authority and the owners of the Bonds may be modified or amended in any respect. However, any provision of the Indenture expressly recognizing or granting rights in or to a bond insurer may not be amended in any manner which affects its rights under the Indenture without the insurer's prior written consent.

(xi) Defaults and Remedies

Events of Default, as defined in the Indenture, include, among other things, the following:

the Authority shall default in the payment of the principal of or Redemption Price, if any, on any Bond when and as the same shall become due, whether at maturity or upon call for redemption or otherwise; or

payment of any installment of interest on any of the Bonds shall not be made as the same shall become due; or

the Authority shall file a petition in bankruptcy or seek a composition of its indebtedness; or

an Event of Default (as defined in the Loan Agreement) under the Loan Agreement; or

the Authority shall fail or refuse to comply with the other provisions of the Indenture, or shall default in the performance or observance of any of the other covenants, agreements, or conditions on its part contained in the Indenture or the Bonds, and such failure, refusal or default shall continue for a period of forty-five days after written notice thereof by the Trustee or the owners of not less than twenty-five percent (25%) in principal amount of the Outstanding Bonds.

Upon the happening and continuance of any Event of Default specified in paragraphs (1) through (3) above, the Trustee shall proceed, or upon the happening and continuance of any Event of Default specified in paragraphs (4) and (5) above, the Trustee may proceed and, upon the written request of the owners of not less than twenty-five percent (25%) in principal amount of the Outstanding Bonds, shall proceed, in its own name to protect and enforce the rights of the Bond owners by such of the following remedies, as the Trustee, being advised by counsel, shall deem most effectual to protect and enforce such rights:

by mandamus or other suit, action or proceeding at law or in equity, to enforce all rights of the Bond owners, including the right to require the Authority to receive and collect revenues, including Pledged Revenues, adequate to carry out the covenants and agreements as to, and to require the Authority to carry out any other covenants or agreements with Bond owners and to perform its duties under the Act;

by bringing suit upon the Bonds;

by action or suit in equity, to require the Authority to account as if it were the trustee of an express trust for the owners of the Bonds;

by action or suit in equity, to enjoin any acts or things which may be unlawful or in violation of the rights of the owners of the Bonds; or

by declaring all Bonds due and payable and, if all defaults shall be cured, then with the written consent of the owners of not less than sixty-six and two-thirds percent (66-2/3%) in principal amount of the Outstanding Bonds, by annulling such declaration and its consequences.

Anything in the Indenture to the contrary notwithstanding, upon the happening and continuance of an Event of Default with respect to a particular series of Bonds, if such Bonds are insured by a municipal bond insurance policy, the insurer thereunder shall be entitled to control and direct the enforcement of all rights and remedies granted to the holders of the such series of Bonds or the Trustee for the benefit of the holders of such series of Bonds under the Indenture.

In the enforcement of any rights and remedies under the Indenture, the Trustee shall be entitled to sue for, enforce payment of and receive any and all amounts then or during any default becoming, and at any time remaining, due and unpaid from the Authority for principal, Redemption Price, interest or otherwise, under any provisions of the Indenture or a Supplemental Indenture or of the Bonds, with interest on overdue payments at the rate of interest specified in such Bonds, together with any and all costs and expenses of collection and of all proceedings thereunder and under such Bonds, without prejudice to any other right or remedy of the Trustee or of the Bond owners, and to recover and enforce a judgment or decree against the Authority for any portion of such amounts remaining unpaid, with interest, costs and expenses, and to collect from any moneys available for such purpose, in any manner provided by law, the moneys adjudged or decreed to be payable.

Upon the occurrence of any Event of Default and upon the filing of a suit or commencement of other judicial proceedings to enforce the rights of the Bond owners under the Indenture, the Trustee shall be entitled, as a matter of right, to the appointment of a receiver or receivers for the Authority, but only with respect to the

Trust Estate, pending such proceedings, with such powers as the court making such appointment shall confer.

(xii) Limitation on Actions by Bond Owners

Bond owners shall have no right to pursue any remedy under the Indenture unless (a) the Trustee shall have given written notice of an Event of Default, (b) the owners of at least 25% in principal amount of the Bonds then Outstanding shall have requested the Trustee, in writing, to exercise the powers granted under the Indenture or to pursue such remedy, and (c) the Trustee shall have been offered indemnity satisfactory to it against costs, expenses and liabilities.

(xiii) Removal of Trustee

The Trustee shall be removed by the Authority if at any time so requested by an instrument or concurrent instruments in writing, filed with the Trustee and the Authority and signed by the owners of a majority in principal amount of the Bonds then Outstanding or their attorney-in-fact duly authorized. The Authority may remove the Trustee at any time, except during the existence of an Event of Default under the Indenture, for such cause as shall be determined in the sole discretion of the Authority.

(xiv) Defeasance

If the Authority shall pay or cause to be paid to the owners of the Bonds, the principal or Redemption Price and interest to become due thereon and make all other payments under the Indenture then the pledge of any revenues and assets hereby pledged and all other rights granted thereby shall be discharged and satisfied. In such event, the Trustee shall, upon the request of the Authority, execute and deliver to the Authority all such instruments as may be desirable to evidence such discharge and satisfaction and the Trustee shall pay over and deliver to the Authority all moneys or securities held by it pursuant to the Indenture which are not required for the payment or redemption of Bonds not theretofore surrendered for such payment or redemption.

All Outstanding Bonds and all interest installments appertaining to such Bonds shall, prior to the maturity or Redemption Date thereof, be deemed to have been paid if (i) in case any of said Bonds are to be redeemed on any date prior to their maturity, the Authority shall have given to the Trustee in form satisfactory to it irrevocable instructions to publish notice or redemption on said date of such Bonds; (ii) there shall have been deposited with the Trustee either moneys in an amount which shall be sufficient, or Investment Securities the principal of and the interest on which when due will provide moneys which, together with the moneys, if any, deposited with the Trustee at the same time, shall be sufficient, to pay when due the principal or Redemption Price, if any, and interest due and to become due on said Bonds on and prior to the redemption Date or maturity date thereof, as the case may be, and (iii) in the event said Bonds are not by their terms subject to redemption within the next succeeding sixty days, the Authority shall have given the Trustee irrevocable instructions to mail notice to the owners of such Bonds that the deposit required by (ii) above has been made with the Trustee and that said Bonds are deemed to have been paid and stating such maturity or Redemption Date upon which moneys are to be available for the payment of the principal or Redemption Price, if any, on said Bonds. For purposes of defeasance, Investment Securities shall mean and only such obligations as are described in clauses (1), (2) and (4) of the definition of Investment Securities (to the extent such securities are guaranteed or otherwise secured by the United States of America), or deposits in interest-bearing time or demand deposits or certificates of deposit secured by obligations of the types described in paragraphs (1) and (2) of the definition of Investment Securities.

Notwithstanding anything to the contrary, in the event that the principal and/or interest due on an outstanding series of Bonds shall be paid pursuant to a municipal bond insurance policy, such series of Bonds shall remain Outstanding for all purposes, not be defeased or otherwise satisfied and not be considered paid by the Authority, and the assignment and pledge of the Trust Estate and all covenants, agreements and other obligations of the Authority to the registered owners shall continue to exist and shall run to the benefit of the insurer under such municipal bond insurance policy who shall also be subrogated to the rights of such registered owners.

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Appendix IV

Form of Opinion of Co-Bond Counsel

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APPENDIX IV

FORM OF CO-BOND COUNSEL OPINION

______, 2017

RE: $__________ Pennsylvania Higher Educational Facilities Authority
Revenue Bonds, State System of Higher Education, Series AU, consisting of
$__________ Series AU-1, Revenue Bonds
$__________ Series AU-2, Refunding Revenue Bonds and
$__________ Series AU-3 Federally Taxable Refunding Revenue Bonds

To the Purchasers of the Within-Described Bonds:

We have served as co-bond counsel in connection with the issuance by the Pennsylvania Higher Educational Facilities Authority ("Authority") of its Revenue Bonds, State System of Higher Education, Series AU, consisting of $__________ Series AU-1 Revenue Bonds ("Series AU-1 Bonds"), $__________ Series AU-2 Refunding Revenue Bonds ("Series AU-2 Bonds"), and $__________ Series AU-3 Federally Taxable Refunding Revenue Bonds ("Series AU-3 Bonds"; together with the Series AU-1 Bonds and the Series AU-2 Bonds, collectively, "Bonds"). The Bonds are issued by the Authority pursuant to the Pennsylvania Higher Education Facilities Act of 1967, as amended (Act No. 318, approved December 6, 1967, P.L. 678, as amended, hereinafter, "Act"), action of the Authority including a resolution adopted July 19, 2017 ("Resolution"), and an Indenture of Trust, dated as of June 1, 1985, as supplemented from time to time including, in particular, by a Forty-Third Supplemental Indenture of Trust, dated as of September 1, 2017 ("Forty-Third Supplemental Indenture"; collectively, "Indenture"), between the Authority and The Bank of New York Mellon Trust Company, N.A., as trustee ("Trustee").

The proceeds from the sale of the Bonds will be applied for the benefit of the State System of Higher Education ("System") to: (i) payment of the costs of construction and renovation of academic and athletic facilities at Indiana University of Pennsylvania and at Slippery Rock University and construction of a guaranteed energy saving project at Slippery Rock University as well as the construction of a parking structure at West Chester University of Pennsylvania; (ii) advance refunding of a portion of the Authority's outstanding State System of Higher Education Series AH Bonds maturing on and after June 15, 2018 ("Refunded Bonds"), and (iii) payment of the costs of issuance of the Bonds.

Pursuant to a Loan and Security Agreement dated as of June 1, 1985, as supplemented from time to time including, in particular, by a Forty-Third Supplemental Loan and Security Agreement, dated as of September 1, 2017 ("Forty-Third Supplemental Loan Agreement"; collectively, "Loan Agreement"), between the Authority and the System, the Authority has loaned the proceeds of the Bonds to the System and the System has agreed to make loan repayments at such times and in such amounts as calculated to enable full and timely payment of the principal and redemption price of and interest on the Bonds. Pursuant to an assignment dated as of September 1, 2017 ("Assignment"), the Authority has assigned its rights under the Loan Agreement (except for its rights to indemnification and to receive certain notices and give certain approvals) to the Trustee. A portion of the proceeds of the Bonds is being deposited and applied to the advance-refunding of the Refunded Bonds, pursuant to an Escrow Deposit Agreement, dated of September 1, 2017, between the Authority and the Trustee, as escrow agent ("Escrow Agreement").

In our capacity as co-bond counsel we have examined the Act, such matters of law and records of the Authority and the System and such other documents, certifications and instruments as we considered necessary to enable us to express the opinions set forth below including, in particular, but not by way of limitation: original counterparts or certified copies of the Resolution, Indenture, Loan Agreement, Assignment, Escrow Agreement and the other documents, certifications and instruments, listed in the Closing Agenda in respect of the Bonds filed with the Trustee, including the Joint Tax Certificate, executed and delivered by the Authority and the System pursuant to the applicable provisions of Sections 103 and 141-150 of the Internal Revenue Code of 1986, as amended, and the regulations applicable thereunder ("Tax Certificate"), the legal opinions of Chief Counsel to the System ("System Counsel Opinion") and of Barley Snyder, LLP, counsel to the Authority ("Authority Counsel Opinion"). We have also examined the fully executed and authenticated Bonds or true copies thereof.

In rendering the opinions set forth below we have relied on the authenticity, truthfulness and completeness of all documents, certifications and instruments examined including, without limiting the generality of the foregoing, the Tax Certificate, upon the Authority Counsel Opinion and the System Counsel Opinion as to matters set forth therein, principally related to the due authorization, execution and delivery by the Authority of the Bonds, and such other documentation as the Authority and the System were required to execute and deliver in connection with the issuance thereof. Except as set forth below in numbered paragraphs 6 and 7, the following opinions are given only with respect to the laws of the Commonwealth of Pennsylvania as enacted and construed on the date hereof.

Based upon and subject to the foregoing, we are of the opinion that:

1. The Authority is a body corporate and politic constituting a public corporation and a government instrumentality organized and existing under the Act, of the Commonwealth of Pennsylvania and has the power to enter into the transactions contemplated by the Indenture and the Loan Agreement and to carry out its obligations thereunder.

2. The Forty-Third Supplemental Indenture, the Forty-Third Supplemental Loan Agreement, the Assignment and the Escrow Agreement have been duly authorized, executed and delivered by the Authority and, assuming, where appropriate, the due authorization, execution and delivery by the other parties thereto, constitute the valid and binding obligations of the Authority enforceable against it in accordance with their respective terms except as may be affected by bankruptcy, insolvency, reorganization, moratorium, fraudulent transfer or other similar laws or legal or equitable principles affecting the enforcement or creditors' rights ("Creditors' Rights Limitations").

3. The Loan Agreement has been duly authorized, executed and delivered by the System and the obligations to make payments thereunder constitute valid and binding obligations of the System enforceable against it in accordance with its terms, except as may be affected by Creditors' Rights Limitations; all right, title and interest of the Authority in and to the loan

payments due under the Loan Agreement have been duly assigned to the Trustee (except for the fees and expenses payable to the Authority and the Authority's right to indemnification).

4. The Bonds have been duly and validly authorized, executed, issued and delivered by the Authority and constitute the valid and binding limited obligations of the Authority enforceable against it in accordance with their terms and are entitled to the benefit and security of the Indenture, except as may be affected by Creditors' Rights Limitations.

5. Under the laws of the Commonwealth of Pennsylvania as enacted and construed on the date hereof, interest on the Bonds is exempt from Pennsylvania personal income tax and corporate net income tax and the Bonds are exempt from personal property taxes in the Commonwealth of Pennsylvania.

6. Under existing statutes, regulations, rulings and court decisions, interest on the Series AU-1 Bonds and the Series AU-2 Bonds, including in the form of properly accrued original issue discount, is not includable from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, such interest is taken into account in determining adjusted current earnings for the purposes of computing the alternative minimum tax imposed on certain corporations.

7. *Interest on the Series AU-3 Bonds is not excludable from gross income of the holders thereof for federal income tax purposes.*

The opinion set forth above in numbered paragraph 6 regarding the exclusion of interest on the Series AU-1 Bonds and the Series AU-2 Bonds from gross income of the recipient is subject to continuing compliance by the Authority and the System with their respective covenants relating to the requirements of the Internal Revenue Code of 1986, as amended, including those set forth in the Tax Certificate. Failure to comply with such covenants could cause the interest on the Series AU-1 Bonds and the Series AU-2 Bonds to be included in gross income retroactive to the date of issue thereof. Although we are of the opinion that interest on the on the Series AU-1 Bonds and the Series AU-2 Bonds is excluded from gross income for federal tax purposes, the accrual or receipt of interest on the Bonds may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences will depend upon the recipient's particular tax status or other items of income or deduction. We express no opinion regarding any such consequences nor, other than as set forth in numbered paragraph 7, as to any federal tax consequences of ownership of the Series AU-3 Bonds, as to all of which recipients should consult their own tax advisors.

This opinion is rendered on the basis of federal law and the laws of the Commonwealth of Pennsylvania as enacted and construed on the date hereof. We undertake no obligation to update or supplement this opinion under any circumstance including if, after the date hereof, facts or events come to our attention or changes in law occur which could affect the matters addressed herein. We express no opinion herein as to any matter not set forth in the numbered sections above, including, without limitation, with respect to, and assume no responsibility for, the accuracy, adequacy or completeness of the preliminary or definitive official statements prepared in respect of the Bonds, including the appendices thereto, and make no representation that we have independently verified the contents thereof.

Attention is called to the facts that the Bonds are limited obligations of the Authority payable from only the revenues pledged and other moneys available under the Indenture and do not pledge the credit or taxing power of the Commonwealth of Pennsylvania or any political subdivision thereof, and that the Authority has no taxing power.

Very truly yours,

KUTAK ROCK LLP

TURNER LAW, PC

State System of Higher Education
Established July 1, 1983
Commonwealth of Pennsylvania

Bloomsburg
UNIVERSITY

KUTZTOWN
UNIVERSITY

CAL U

LOCK
HAVEN
UNIVERSITY
OF PENNSYLVANIA

CU
CHEYNEY UNIVERSITY
1837

MANSFIELD
UNIVERSITY

CLARION
UNIVERSITY

Millersville
University

PREPARE TO SERVE
ESU
EAST STROUDSBURG
UNIVERSITY
FOUNDED 1893

SHIPPENSBURG
UNIVERSITY

EU
1857
EDINBORO
UNIVERSITY

SlipperyRock
University

IUP

WEST CHESTER
UNIVERSITY