University System of New Hampshire

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October 31, 2018

His Excellency, Governor Christopher T. Sununu
and the Honorable Council
State House
Concord, New Hampshire 03301

Your Excellency and Members of the Council:

Pursuant to RSA 187-A:22, enclosed please find the Annual Report for the University System of New Hampshire for fiscal year ended June 30, 2018. On page 23 of the report you will find the Independent Auditor's Report reflecting the unmodified or "clean opinion" issued by KPMG, our external independent auditors. The report was presented to and accepted by the University System's Board of Trustees on October 26, 2018.

In addition, also attached pursuant to RSA 187-A:25-a is information provided to the USNH Audit Committee by KPMG, its external auditors.

Please feel free to contact me with any questions on the report.

Respectfully,

Catherine A. Provencher
Vice Chancellor for Financial Affairs and Treasurer

Enclosures

# 2018 ANNUAL REPORT

University System of New Hampshire

The Pipeline to New Hampshire's Future


# University System *of* New Hampshire

The University System of New Hampshire (USNH) includes the University of New Hampshire (UNH), with campuses in Durham, Manchester and Concord, Plymouth State University (PSU), Keene State College (KSC) and Granite State College (GSC). KSC, PSU and UNH Durham are the three residential campuses of USNH. The system enrolls 32,000 students and is committed to providing access to affordable, high-quality education and to creating a talented workforce to serve the state's businesses and communities. A 29-member board of trustees is responsible for overseeing the system. The chancellor is the chief executive and academic officer of USNH, and is responsible for developing, recommending and implementing the board's policies and decisions.

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## University System of New Hampshire

1. University of New Hampshire, Durham
2. University of New Hampshire, Manchester
3. University of New Hampshire School of Law, Concord
4. Plymouth State University
5. Keene State College
6. Granite State College, Concord
7. Granite State College, Conway
8. Granite State College, Manchester
9. Granite State College, Nashua (Colocation)
10. Granite State College, Portsmouth
11. Granite State College, Rochester


The 2018 Annual Report is a publication of the University System of New Hampshire. Prior year University System annual reports are available online at https://www.usnh.edu/about/publications. University System of New Hampshire, 5 Chenell Drive, Suite 301, Concord, NH 03301 603-862-1800.

# Chancellor's Letter

At this year's Business and Industry Association's Strategic Retreat, workforce needs were identified as one of New Hampshire's most pressing business imperatives, and that sentiment seems to be shared by every industry leader I meet with. Unemployment data suggests that the State's biggest workforce bottleneck is among those that are bachelor's educated and above. Unfortunately, demographic data suggests the imperative is only going to be stronger over the next several years to come.

Compounding New Hampshire's workforce challenge is the fact that every other state in New England is facing the same demographic landscape and thus the same workforce challenge. What that means is that our workforce pipeline is going to be increasingly dependent upon a strong pipeline of talent and keeping more New Hampshire students in New Hampshire will be key to achieving the necessary talent pipeline.

The University System of New Hampshire is the State's largest provider of a bachelor's educated workforce. Our institutions are particularly focused on State needs for educators, health care professionals, and STEM (science, technology, engineering and math) educated workers. The University System invested over $5 million into biological science labs in UNH's Manchester facility this year in support of New Hampshire's regenerative medicine industry, and our institutions are dedicated to working closely with industry partners in support of their needs.

Key to preparing New Hampshire's workforce is ensuring affordable access. Holding down costs by leveraging economies of scale across the System has long been a focus of the System and those efforts have been stepped up through strategic procurement and aggressive management of health care costs, among other cost containment efforts. The System also leverages State dollars to lower tuition for all New Hampshire residents. In addition, USNH institutions have raised millions for additional scholarships and all residential institutions are offering the Granite Guarantee that allows Pell eligible New Hampshire students to attend tuition free.

New Hampshire's public four-year institutions are critical to the State's talent pipeline and serve as one of New Hampshire's most critical economic engines. The University System works hard to maximize the return on investment for both the State and our students.

**Todd Leach**
Chancellor


## University of New Hampshire

Founded in 1866, UNH is the state's flagship public research university, with campuses in Durham and Manchester, and the UNH School of Law Concord. More than 16,000 students, representing 50 states and 71 countries, attend UNH, which offers 130 undergraduate and 70 graduate programs of study. UNH is awarded more than $100 million in competitive research funding each year, and was ranked among the top 50 public universities in the nation, from among 629 ranked by U.S. News and World Report for 2019. More than 5,000 New Hampshire businesses receive direct, one-on-one assistance from UNH every year. The university also holds the nation's largest undergraduate conference, featuring nearly 2,000 students who present their projects each spring. Through the Cooperative Extension, UNH provides research, expertise and outreach programming across the state, with more than 114,000 residents participating in workshops, volunteer trainings, one-on-one consultations and courses.

## Plymouth State University

Plymouth State University dates to 1871. With an enrollment of more than 6,000 undergraduate and graduate students, PSU's 170-acre campus features up-to-date facilities amid the White Mountains and Lakes Region. Students can choose from studies in the arts, business, education, humanities, and the natural and social sciences. A bachelor's program in Robotics was launched in 2018-19. PSU is on the cutting edge of change in higher education, working to graduate students ready to participate in the workforce, who understand the nuances of working with a variety of people, and who will make a positive difference in the state's economy. The university, regional businesses and nonprofits, school districts and towns are working collaboratively through PSU's unique Integrated Clusters learning model, helping to improve businesses and energizing towns while giving students the chance to work with real-world challenges.

## Keene State College

Wisdom to make a difference.

Keene State College is New Hampshire's public liberal arts college, offering more than 40 majors in the arts and sciences, professional programs and selected graduate degrees. For its 3,500 students, the college provides rigorous academic programs and a tradition of small classes, faculty-student collaborative research and service learning. Chief among the college's priorities are preparing students for global citizenship and meaningful work and catalyzing economic development through institutional partnerships across the region and state.

## Granite State College

With a focus on adult students, as well as other individuals who seek a flexible learning environment, GSC provides comprehensive access to higher education. This commitment to access is best illustrated through its statewide locations and 365/24/7 online presence. The ability for GSC to meet students where they are presents the opportunity to achieve an affordable college education while balancing life's other responsibilities such as work, family, and community obligations. With associate, bachelor's and master's degrees, post-baccalaureate programs for teachers, credit for prior learning and a variety of transfer opportunities , GSC emphasizes practical and relevant areas of study that are responsive to the workforce development needs of New Hampshire's economy.

## Alumni Legislator Breakfast

Always terrific to connect with our alumni lawmakers at our annual USNH alumni breakfast. This is a wonderful event where our alumni lawmakers hear first-hand from the presidents and recent graduates of our institutions and are recognized for their commitment to public service.

# USNH Gets Positive Marks for Fiscal Management

## Rating agencies cite strong fiscal management, affirm USNH bond ratings

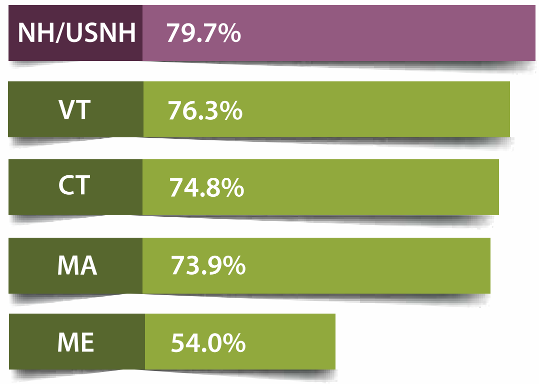
As the result of strong leadership and sound fiscal management, two of the world's key credit rating firms, Standard & Poor's (S&P) and Moody's, have issued a stable outlook for the University System of New Hampshire. Both agencies cited strong fiscal stewardship and continued positive operations, including relatively stable enrollments, despite minimal state support.

Moody's Investor Service affirmed its USNH "Aa3" rating, adding that "the outlook is stable." Noting USNH's fiscal responsibility, the report stated, "We expect the system's strong leadership team will carefully navigate a challenging state funding environment and focus on stabilizing enrollment to produce ongoing positive operating margins."

S&P Global Ratings affirmed its "AA-" long-term rating for USNH. In its report, S&P noted, "We assessed USNH's financial profile as very strong with excellent financial management policies, ample financial performance with recurring positive (full-accrual based) operating margins, superior financial resources, and low to moderate debt and contingent liabilities for the rating category."

## Degree Completion

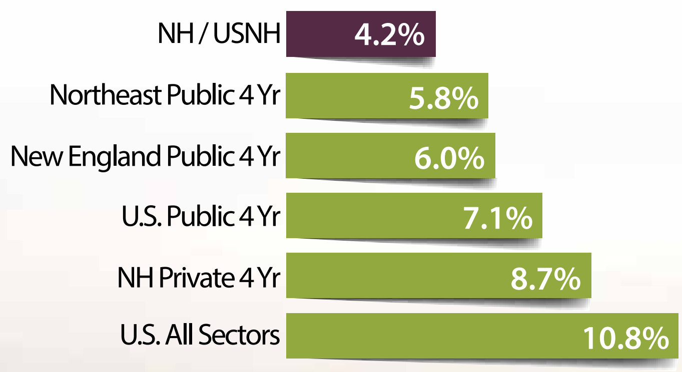
USNH ranks 1st in New England (and the Northeast) and 3rd in the U.S. among public systems for high bachelor's degree completion




Source: National Student Clearinghouse. RI omitted for technical reasons.

## Student Loan Default

USNH consistently ranks among the top systems in the U.S. with the lowest average loan default.




Source: National Student Loan Data System

## USNH Hosts Northern New England Higher Education Summit

In a collective effort to reduce the costs of higher education, educational leaders across northern New England met to explore areas for collaboration to improve the student experience and bend the cost curve of higher education. The University System of New Hampshire hosted the summit with leaders from the University System of Maine and the Vermont State Colleges System.

The summit was designed to look at ways to address the challenges higher education faces and to identify the resources to develop solutions. Conversations centered around the benefit of shared services and procurement, which could potentially save each system millions of dollars.

The summit ended with a commitment of the three university systems to work together, to share information and best practices, to benchmark data and to advance accreditation policies.

## The Granite Guarantee Expands to More USNH Institutions

### The successful program launched at UNH will now help even more New Hampshire students obtain their degrees.

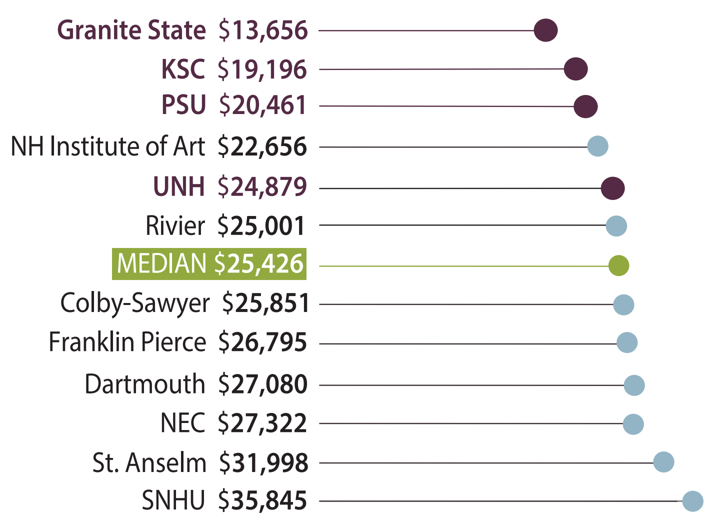
This past year, USNH expanded the successful Granite Guarantee program to all of its residential campuses. Students who qualify for need-based federal Pell grants have the opportunity to achieve their educational dreams in New Hampshire.

*"To be able to expand this program to help even more New Hampshire residents is gratifying, and it advances the critical role of public higher education in building the state's future workforce. We are working hard to ensure our institutions are accessible and affordable to in-state students and their families. This is one solution that our institutions have committed to that helps need-based students afford the cost of their education. The Granite Guarantee is a significant achievement toward our goal of making a USNH education attainable to every student."*

-Chancellor Leach


### Average In-State Cost of Attendance for NH 4-Year Colleges and Universities

Average undergraduate net price after all grant and scholarship aid. Price includes tuition, mandatory fees, books and supplies, room and board and other expenses as calculated for financial aid.




## GSC Again Named Best College for Adult Learners and Best Online Bachelor's Programs

In 2018, GSC was once again featured as a Best Four-Year College for Adult Learners (Washington Monthly) and a top online bachelor's program (U.S. News & World Report). GSC is the #1 college in NH on each of these distinctive lists.

# Building NH’s New Biotech Industry: UNH Manchester Selected as Leading Partner

UNH Manchester is the lead education and training partner for an innovative, $300 million project that is developing a new biotech industry in New Hampshire that will create hundreds of jobs for highly skilled workers. Located in Manchester’s Millyard, the Advanced Regenerative Manufacturing Institute (ARMI), was created by inventor Dean Kamen, founder of DEKA and the FIRST Robotics competition, and is supported by an $80 million grant from the U.S. Department of Defense.

ARMI aims to harness large-scale manufacturing and commercialization techniques in order to grow human tissues, including skin and some organs. As ARMI grows, breakthroughs in manufacturing techniques, cell biology, biofabrication and materials science will make its technology available first to soldiers injured in service and then to hospitals to help the general public. USNH is proud to support this exciting new industry.

## Electromechanical Technology and Robotics

New Hampshire's first bachelor's degree program in Robotics was launched in 2018-19 at PSU. The systems-level program builds on PSU's strength in programming, allowing students to guide microcontrollers, actuators and sensors. New courses include Microprocessors and Digital Systems and three dedicated Robotics courses. The planned Open Laboratory will facilitate experimentation, assembly and collaboration with business and regional partners. Graduates of PSU's new Robotics program will be qualified for in-demand jobs such as robot software engineer, robot systems engineer and other highly rewarding positions.

## USNH Robotics Scholarship

This year, USNH joined Governor Chris Sununu to support New Hampshire's best and brightest students by providing a tuition-free semester at any USNH institution for the winners of the new statewide Governor's Cup Robotics Championship. USNH is very pleased to be part of this effort to encourage these students to stay in New Hampshire, attend one of our great USNH institutions and ultimately keep their talent right here in the Granite State.

### USNH Leads New Hampshire in STEM Education

**58%**

USNH schools award 58% of NH's engineering and science degrees

**52%**

USNH awards more than half of NH's K-12 STEM teacher degrees

# At Lonza Biologics, UNH Interns Build High-Tech Skills – and Careers

## Nearly 80 percent of UNH students complete at least one internship before they graduate – that's 19 percent higher than the national average!

Many UNH students get great hands-on experience with cutting-edge technology through internships with Lonza Biologics, a global pharmaceutical supplier with facilities in Portsmouth. Interns work on laboratory studies, technology transfer, manufacturing and administration, getting a feel for the full range of Lonza operations. Students often find these opportunities at one of UNH's career fairs, which attract 4,000 students and hundreds of employers each year.

"If I hadn't had the chance to take a bio-manufacturing class and go to the career fair at UNH, I never would have had this opportunity with Lonza," says Sidney Snelling '19, a Lonza intern and medical microbiology major. "And if I hadn't gone to UNH, I never would have gotten a chance to have this great internship."

## First-in-the-Nation Construction Safety Sciences Program

Keene State's new Construction Safety Sciences Program is the first in the nation. The program prepares students for a variety of occupational safety and health program management positions in the private and public sectors. Emphasis is placed on critical thinking, hazard identification and prioritization, problem solving, cost effectiveness, professional skills in programmatic management and safety and environmental regulatory compliance.

## Applied Optics Program

Keene State invited representatives from local industries to campus on August 17 to explore the creation of an 'Optics' or 'Applied Optics' program at the college. The group included BAE Systems, Corning, Omega Optical, Chroma, and Stingray Optics. Keene State shared details of current courses that could be built into an optics program, brainstormed skills and outcomes of an optics curriculum, and discussed creation of a program that meets the hiring needs of those companies. Moving forward, KSC is forming a faculty advisory committee to outline courses for a four-year major in optics, as well as certificate and minor options. BAE has volunteered to identify instrumentation and machinery that may be donated or loaned to Keene State, and representatives of the company have discussed the potential of sponsoring a course or program. In addition, BAE is one of eight represented companies that will participate in the college's Career Speaker Series. BAE Systems made its first hires from Keene State in May – Brittany Jennings '18 was hired as a process engineer and Julia Przekaza '19 was an intern.

## 10,000 Businesses Started – and Counting!

### UNH Entrepreneurship Center Trains Innovators

UNH alumni have started, or helped to start, more than 10,000 businesses. Better yet, you can expect the pace of entrepreneurship to pick up in coming years, as UNH's Peter T. Paul Entrepreneurship Center (ECenter) sends more talented graduates into the marketplace. Since opening in 2016, the ECenter has become UNH's heart of ideas, innovation and entrepreneurship; and it is creating the next generation of business leader.

The ECenter brings together students, faculty, and alumni with the resources to bring their innovative ideas to market, often in partnership with privates businesses.

Within two years of opening, the ECenter was recognized as the top emerging entrepreneurship center by the Global Consortium of Entrepreneurship Centers, which represents 250 member institutions in 15 countries.

## UNH Advanced Manufacturing Center Designed to Meet NH Workforce Needs

In June 2018, UNH opened the John Olson Advanced Manufacturing Center, designed to provide highly skilled employees for New Hampshire's — and the nation's — manufacturing sector in high-precision machining, light materials, flexible electronics and Industry 4.0.

Whelen Engineering Co., a 1,900-employee firm based in Charlestown, NH, contributed $5.3 million to start the project and worked closely with the UNH College of Engineering and Physical Sciences to create training that will help to answer New Hampshire's workforce needs.

Taylor Caswell, commissioner of the NH Department of Business and Economic Affairs, praised Olson, president of Whelan Engineering, for his years of speaking out about the importance of advancing educational opportunities in manufacturing. "UNH was listening," Caswell said, adding, "Companies are coming to New Hampshire for this high-quality workforce."

## GSC Creates Customized Training for Top Employers

As New Hampshire faces challenges in building and retaining talent, GSC is offering its expertise in educating and training adult learners through customized professional development programs. Partners include Easterseals and Novacure, an oncology company developing innovative cancer treatments. GSC works closely with each employer to develop programs specifically designed to meet their emerging needs.

## Colocation

River Valley Community College (RVCC), Keene State College (KSC) and Nashua Community College (NCC) will be sharing labs, classrooms and administrative space to deliver programs more efficiently and effectively to area students. Beyond student access and affordability, this partnership will reinforce efforts with regional employers and entrepreneurs as a hub for workforce development activities. Two of the program areas most positively impacted initially will be nursing and manufacturing. The collaboration will position the community colleges to broaden associate degree and certificate offerings in Keene in a variety of fields and will provide seamless movement for students seeking four-year or advanced degrees at Keene State.

Additionally, GSC has been working closely with the Community College System to build strong bridges of opportunity for New Hampshire's students. These bridges take many forms including GSC courses offered on site at Nashua Community College, a GSC Advising Office located at River Valley Community College's Lebanon Academic Center, the RN to BSN Pathway Program, and two accelerated bachelor's degree completion programs offered to CCSNH students for Psychology and Business Management.

## Standardized Patients Program

PSU's physical therapy, counseling, and nursing programs have partnered with their theatre colleagues to create a university-centered Standardized Patients program. Theatre students are carefully trained to act like real patients to simulate a set of symptoms or problems, which require appropriate responses from students in the health sciences. The result is a rich learning experience for all. PSU's program is unique in that it is utilizing individuals from its own student body for this training, providing theatre students with valuable acting opportunities and additional marketable skills. Potential offshoots of the program could go beyond the medical program, for example, a student actor could pose as an employer interviewing a student or a business person evaluating a proposal.

## Enriching Professional Development Opportunities Across Grafton County

In Grafton County, the two top employers—Dartmouth-Hitchcock Medical Center and Hypertherm—have each partnered with Granite State College to help to grow their workforce from within. In 2018, Hypertherm named GSC as the partner of choice for their tuition reimbursement program. Qualified employees can pursue flexible, online associate, bachelor's and master's degrees completed online while continuing to work full time. With strong internal training programs to help entry-level workers advance to more sophisticated health care careers, Dartmouth-Hitchcock works with GSC to assess their training for college credit. Each participant who completes the organization's vigorous surgical technologist training program now earns significant credits towards a bachelor's degree at GSC.

## Growing the Nursing Workforce through Smart Partnerships

According to a report from Medicare Health Plans, New Hampshire's nurses rank #10 among the most overworked nationwide. To support growth among the nursing workforce, Granite State College has developed key partnerships across the state. Now in its fifth year, the Community College System of New Hampshire (CCSNH) and GSC offer an RN to BSN pathway that guides NH students from the associate-level to a bachelor's degree with a competitive, low tuition rate. This flexible option allows students to work in a health care facility and gain experience, while finishing their degree.

## Two New Master's Programs: Addressing NH's Health Care Needs

With roughly half of its employees nearing retirement age, the health care industry in New Hampshire is positioned for a generational turnover of workers, which will create a significant shortage of talent across the field. Two new graduate programs at GSC, the Master of Science in Nursing and the M.S. in Health Care Management, will help to address this gap by preparing emerging leaders in the health care workforce for top positions in nursing and management. These programs are designed for professionals who are already serving the workforce and can be completed 100% online, allowing students to balance their graduate program with their career and home life.

## Strength and Conditioning Open Laboratory

Plymouth State University's comprehensive renovation of the Physical Education Center includes a new Strength and Conditioning Open Laboratory, which will support the Health and Human Enrichment Cluster of disciplines. Students enrolled in athletic training, physical education, adventure education, physical therapy, exercise and sports physiology and other allied health fields will use top-notch equipment and work in state-of-the-art facilities. This academic hub will integrate knowledge gained in the classroom with hands-on expertise refined in the Open Laboratory, which will serve as a nexus for shared projects with industry. The renovation is taking place courtesy of $3 million in initial Capital Improvement Project (CIP) funding approved by Governor Sununu and the New Hampshire Legislature.


## Nursing Externships

### Nursing Student Gains Experience Working in Intensive Care Jimmy Halkiotis '19

Keene State nursing student, Jimmy Halkiotis '19, is participating in the gold-standard of externships this summer at Dartmouth-Hitchcock Lebanon's intensive care unit. Halkiotis, from Hampstead, NH, is gaining skills under two intensive care nurses at New Hampshire's largest hospital. During his time there, he is getting hands-on experience with what being a critical care nurse entails and requires.

**5,268**
Extension volunteers

**114,206**
Residents assisted

**100+**
Lakes protected

**85,490**
Acres improved

# UNH Cooperative Extension

## In 2017, for every $1 a county spent, UNH provided $1.99 in statewide resources.

UNH Cooperative Extension brings information and education into the communities of the Granite State help to make New Hampshire's citizens, businesses and communities more successful and its natural resources healthy and productive. For 100 years, Extension specialists and its network of dedicated volunteers have been tailoring contemporary, practical education to regional needs, helping to create a well-informed citizenry, to strengthen the economy and to support our first-in-the-nation quality of life.

The Extension's statewide outreach programs and experts meet Granite Staters where they are by using effective technologies, online learning platforms and face-to-face interactions that match the ways people learn and engage, while continuing to provide customized, in-person programming and assistance.



# Furthering the Open Education Initiative in New Hampshire

Open Education is a movement that recognizes the benefit for students to have free access to the tools and knowledge necessary to obtain a college education. By adopting Open Education in its classrooms, USNH acknowledges the demand for 21st-century, student-driven learning that emphasizes community and collaboration. USNH is one of the first university systems in the United States to adopt a system-wide Open Education initiative.

"We are encouraged by the work that has taken place and proud to be a national leader in the Open Education initiative," stated USNH Chancellor Todd Leach. "We are always striving to improve the student experience. Providing students with the tools to further their studies in a cost-effective manner aligns with our mission of accessibility to a quality education. This is a great example of how we are harnessing technology to foster innovation and drive costs down."


## Portsmouth, UNH Team Up with Local Employers

Seacoast area businesses learned how they can hire a UNH student or graduate in early summer 2018 when the City of Portsmouth's economic development office hosted a "How to Hire a Wildcat" workshop with the UNH Cooperative Extension and UNH Career and Professional Success (CaPS).

The event was developed in response to an Extension survey of 71 Portsmouth businesses, which outlined the challenges local employers face in finding qualified, well-trained employees.

## UNH School of Law 5th in U.S. for Jobs on the Open Market

The UNH School of Law ranked No. 1 among the 14 law schools in New England for employment on the open market (excluding law school funded jobs) – and No. 5 in the U.S. – with 95 percent of the 2017 JD class employed within 10 months of graduation. UNH Law was also No. 2 in New England in graduates employed in bar-passage-required jobs at 85.2 percent, while 91.8 percent obtained jobs that required bar passage or a law degree.

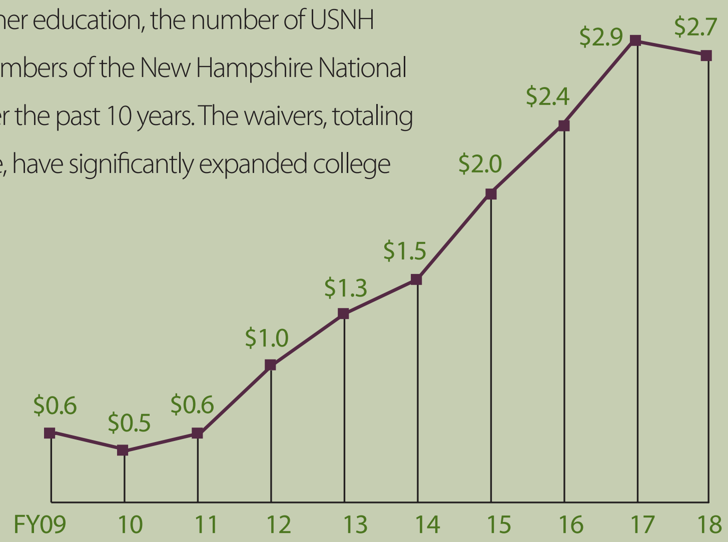
UNH Law's strong employment outcomes were bolstered by an impressive bar passage rate in 2017, as graduates achieved a first-time bar-passage rate of 93.3 percent, 15th among law schools nationwide.

## First-Year Seminar, "Wicked Problems"

The current generation is facing some large, seemingly intractable problems: world hunger, gender inequity, technology's increasing influence, inequities in education and more. Daunting issues, but also precisely the kind that lend themselves to Plymouth State University's cross-disciplinary Integrated Clusters approach, which is why PSU students are tackling these "Wicked Problems"—and many more—in their First-Year Seminars. Each of this year's approximately 1,200 first-year students chose one of 35 Wicked Problems to work on. They then partnered with peers from other majors, and with faculty, regional partners, businesses and nonprofit organizations, gaining real-world, résumé-boosting experience.


## USNH supports New Hampshire's National Guard

Recognizing the value of higher education, the number of USNH tuition waivers sought by members of the New Hampshire National Guard have nearly tripled over the past 10 years. The waivers, totaling $15.5 million over the decade, have significantly expanded college access for NH Guardsmen.



KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

# Independent Auditors' Report

The Governor and
Legislative Fiscal Committee
State of New Hampshire; and
The Board of Trustees
University System of New Hampshire:

## Report on the Financial Statements

We have audited the accompanying statements of net position of the University System of New Hampshire (the System), a component unit of the State of New Hampshire, as of and for the years ended June 30, 2018 and 2017, the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the System's basic financial statements for the years then ended.

### *Management's Responsibility for the Financial Statements*

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

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. 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 opinion.

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of the University System of New Hampshire as of June 30, 2018 and 2017, and the changes in its net position and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

***Emphasis of Matter***

As discussed in Note 1 to the financial statements, in 2018 the System adopted Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

***Other Matter - Required Supplementary Information***

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 25 - 33 and the required supplemental information on page 50 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 audits 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.

KPMG LLP

October 26, 2018

## I. Introduction

The following Management's Discussion and Analysis summarizes the financial condition and results of activities of the University System of New Hampshire (USNH) for the fiscal years ended June 30, 2018 and 2017. This analysis provides a comparison of significant amounts and measures to prior periods and, where appropriate, presents management's outlook for the future.

USNH is a Section 501(c)(3) corporation organized under the laws of the State of New Hampshire to serve the people of the state as the key provider of public higher education for Bachelor's and advanced degree students. USNH accomplishes its mission by operating four educational institutions that collectively offer a broad array of education, research and public service options for the state. These institutions include the University of New Hampshire (UNH), Plymouth State University (PSU), Keene State College (KSC) and Granite State College (GSC). While select programs are active in other regions as well as abroad, most of USNH's activities take place at the three residential campuses (UNHD, PSU and KSC), UNH's urban campuses (UNHM and UNHL), the six regional sites of GSC, and the UNH Cooperative Extension and Small Business Development Centers located throughout the state. The accompanying financial statements also include the activities and balances of the University of New Hampshire Foundation, Inc. (UNHF) and the Keene Endowment Association (KEA), two legally separate but affiliated entities. (See Note 1 to the Financial Statements for additional information on affiliated entities.)

## II. Economic Outlook

The US Census Bureau projects that through 2030 the number of New Hampshire residents between ages 15 and 19 will drop 6.6% (approximately 5,600 students) from the current level of 85,385. The dip will then be partially recovered over the following ten years to approximately 83,300 in 2040. This is one near-term trend impacting USNH campuses. However, it is mitigated by other trends including increased demand for fifth year programs culminating in graduate degrees, as well as local industry needs for higher education levels of new hires. At 2.7% as of July 2018, New Hampshire has the fourth lowest unemployment rate in the country behind only Hawaii, Iowa and North Dakota. This compares to the national average of 4.0%, and will ease the pathway for our graduates as they transition into the state's workforce. Over the past year USNH institutions have increased partnerships with the State and businesses to offer and expand programs in areas of expected economic growth including nursing and associated medical needs, as well as robotics and other new technologies. In short, our campuses continue to evolve to meet local and national demands for quality education. The remainder of this report describes the results of financial operations for the year ended June 30, 2018 with comparisons to prior years.

## III. Financial Highlights

### A. Revenues

Chart 1 to the right shows USNH's operating revenue streams including state appropriations, which totaled approximately $1 billion in both fiscal years 2018 and 2017. Given our tri-fold mission of instruction, research and public service, the vast majority of USNH revenues are used for education, student support, and the delivery of related auxiliary services. Even our research projects increase the knowledge base. As shown in Chart 2, institutional financial aid expenditures significantly exceeded the level of student loans issued. This resource commitment is made in support of the state's workforce needs to ensure qualified students can attend our institutions, without being burdened by excessive debt.

**Chart 1: 2018 Gross Revenues by Source**
**Total = $1+ Billion**
*($ in millions)*

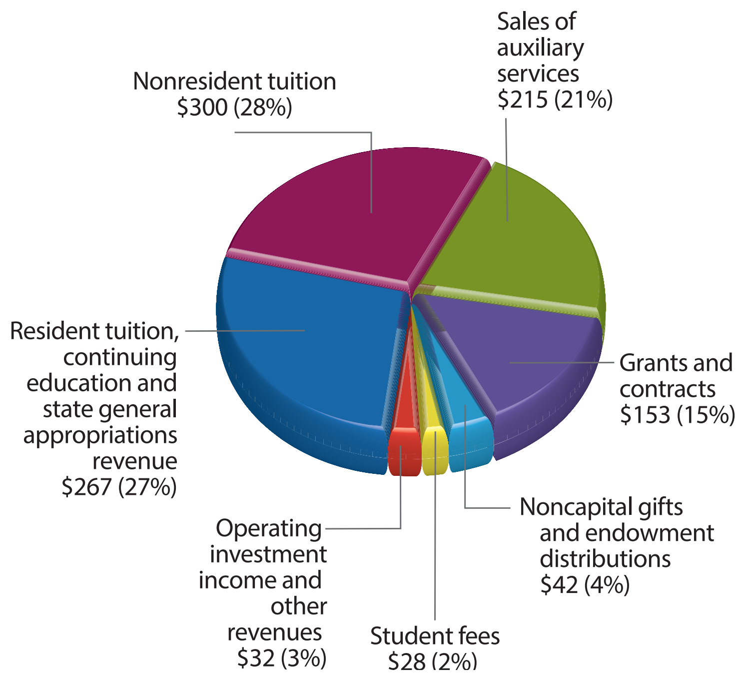
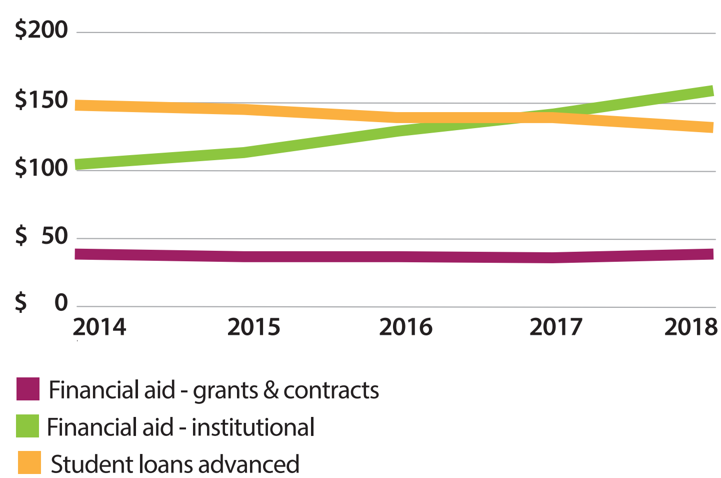



**Chart 2: Student Aid Trends**
*($ in millions)*



As seen in Table 1 below, enrollment at the flagship campus has remained stable over the past five years at an average of approximately 15,500 FTE students for all UNH locations combined. UNH's Durham campus had large increases in freshmen applications over the past five years as shown in Table 2. Their enrollment strategy remains focused on attracting exemplary students. Approximately 41% of new UNHD students in the fall of 2017 ranked in the top 20% of their high school class reflecting the continued quality of the population. PSU also launched an innovative new learning clusters program in 2017. The clusters group students in related majors to share resources with the goal of providing a holistic educational experience so that students are able to provide value to their future employers on their first day of work. The sharing of resources is also designed to drive down administrative costs as well as streamline financial transaction processing. KSC is also grouping its academic programs into two new Schools to gain administrative efficiencies and share resources. Beginning in the fall of 2018 the School of Arts, Education and Culture will house programs including education, journalism, communications, philosophy, Holocaust studies and a number of other majors. In addition, the School of Sciences, Sustainability and Health will include architecture, chemistry, political science, nursing, human performance, and environmental studies as well as technology and other related programs.

## Table 1: Full-Time Equivalent Credit Enrollment

*For the Fall of Each Fiscal Year*

| | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|
| UNH (all campuses) | 15,272 | 15,406 | 15,657 | 15,473 | 15,669 |
| PSU | 4,670 | 4,346 | 4,674 | 4,641 | 4,694 |
| KSC | 4,705 | 4,751 | 4,250 | 4,160 | 3,758 |
| GSC | 1,551 | 1,685 | 1,658 | 1,584 | 1,446 |
| **Total USNH FTEs** | 26,198 | 26,188 | 26,239 | 25,858 | 25,567 |
| NH Resident | 14,797 | 14,308 | 13,742 | 13,240 | 12,940 |
| Nonresident | 11,401 | 11,880 | 12,497 | 12,618 | 12,627 |
| **Total USNH FTEs** | 26,198 | 26,188 | 26,239 | 25,858 | 25,567 |

During 2018 nonresident tuition increased 3.8% ($11.0 million) over the prior year. Over the past five years the mix of USNH students has changed from 57% to 51% New Hampshire residents when calculated on a full-time equivalency basis. This is due, in part, to expansion of international recruiting as well as online course offerings available at nearly any location. USNH is working to ensure New Hampshire students are also well-represented and prepared to meet the needs of the State's workforce. Institutional financial aid grew nearly 10% ($13.8 million) from 2017 to 2018, and grant aid grew by 6.5% ($2.0 million). USNH has also made significant changes in the way it awards financial aid. During 2018, UNH launched the Granite Guarantee program which covers the cost of tuition for all federal Pell-grant eligible New Hampshire students. The sister USNH campuses were quick to follow suit. The State is also partnering in this area by renewing its Governor's Scholarship Fund for New Hampshire resident students as well.

## Table 2: Freshman Applications, Acceptances and Enrollees at UNH Durham*

*For the Fall of Each Fiscal Year*

| | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|
| Freshmen applications received | 17,938 | 18,420 | 19,255 | 20,203 | 19,966 |
| Acceptances as % of applications | 78% | 80% | 71% | 76% | 77% |
| Enrolled as % of acceptances | 16% | 18% | 24% | 19% | 20% |

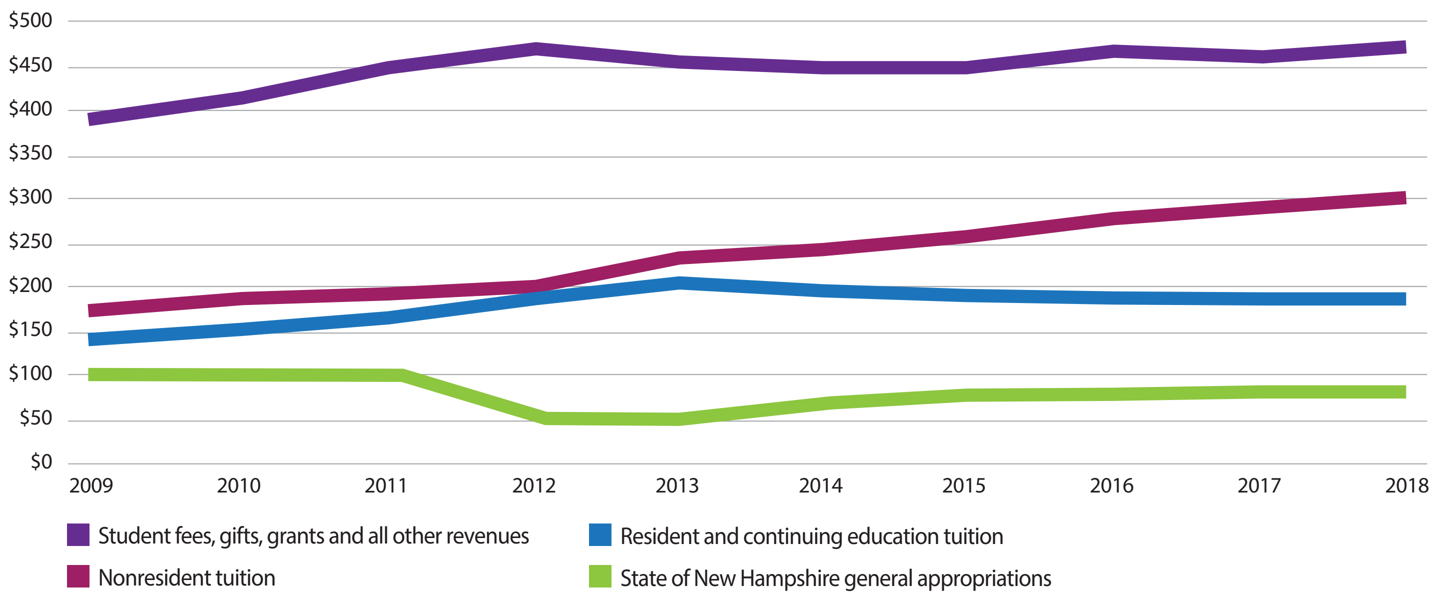
** Comparable data for other campuses is available upon request.*

Other areas of growth included noncapital and endowment gifts which were both up 23% over the prior year ($2.7 million and $3.1 million, respectively). These increases are attributable to the final year of UNH's highly successful fundraising campaign. Offsetting those contributions, plant gifts were at normal levels during 2018, compared to the significant gifts received for the Holocaust Studies Library addition at KSC ($4 million) and the Ocean Engineering Program at UNH ($2 million) in 2017. Chart 3 below shows USNH's major revenue stream trends for the past ten years. As seen in the graph, state appropriation revenues were cut by 50% in 2012, which resulted in a significant increase in resident tuition rates for fiscal years 2012 and 2013. USNH then held resident tuition rates flat through 2015 as the appropriation was partially restored. Inflationary increases in the resident tuition rates were added for 2016 through 2018. As evidenced by the financial aid growth shown in Chart 2, on page 25, USNH is committed to working with the State to ensure that New Hampshire's students have access to a quality education at an affordable price.

## Chart 3: Ten Year Revenue History

*Before Application of Student Financial Aid*

*($ in millions)*




## B. Operating and Capital Expenditures

USNH's operating expenses (including interest) increased $12.7 million or 1.5% over the 2017 level; and 2017 expenses increased only $650,000 or 0.1% over 2016. This compares to an increase of $26 million (3.2%) from 2015 to 2016; and an increase of $30 million (3.9%) from 2014 to 2015. There have been significant efforts to organize USNH employee groups over the past few years. This has resulted in new unions for certain faculty and staff at the residential and urban campuses. Nongrant compensation expenditures were up $9.6 million (2.1%) in 2018 after being down $8.9 million (1.9%) in 2017. The costs of employee separation offerings, medical and other benefits continue to be reviewed, along with supplies and services costs. In addition, depreciation charges are also increasing as efforts are made to modernize our buildings and infrastructure.

During 2017 USNH restructured its Procurement activities to have all campus purchasing personnel report centrally. This new model of local delivery with central oversight is designed to contain costs in future years by combining our purchasing volumes across the state. As part of this initiative USNH contracted for a system-wide online purchasing system during 2018. This new system is expected to be live for calendar year 2019 and will add another layer of cost control, as well as continuous monitoring and oversight of the purchasing function.

Other ongoing system-wide activities being regularly monitored by the Financial Affairs Committee of the USNH Board of Trustees include the implementation of an Enterprise Performance Management System, and implementation of the latest version of our Enterprise Resources and Planning System. Both of these systems are cloud-based and expected to go live in 2019. Accordingly, the Financial Affairs Committee is also monitoring a system-wide cyber security assessment as well.

## Chart 4: Expenses by Functional Classifications

*($ in millions)*

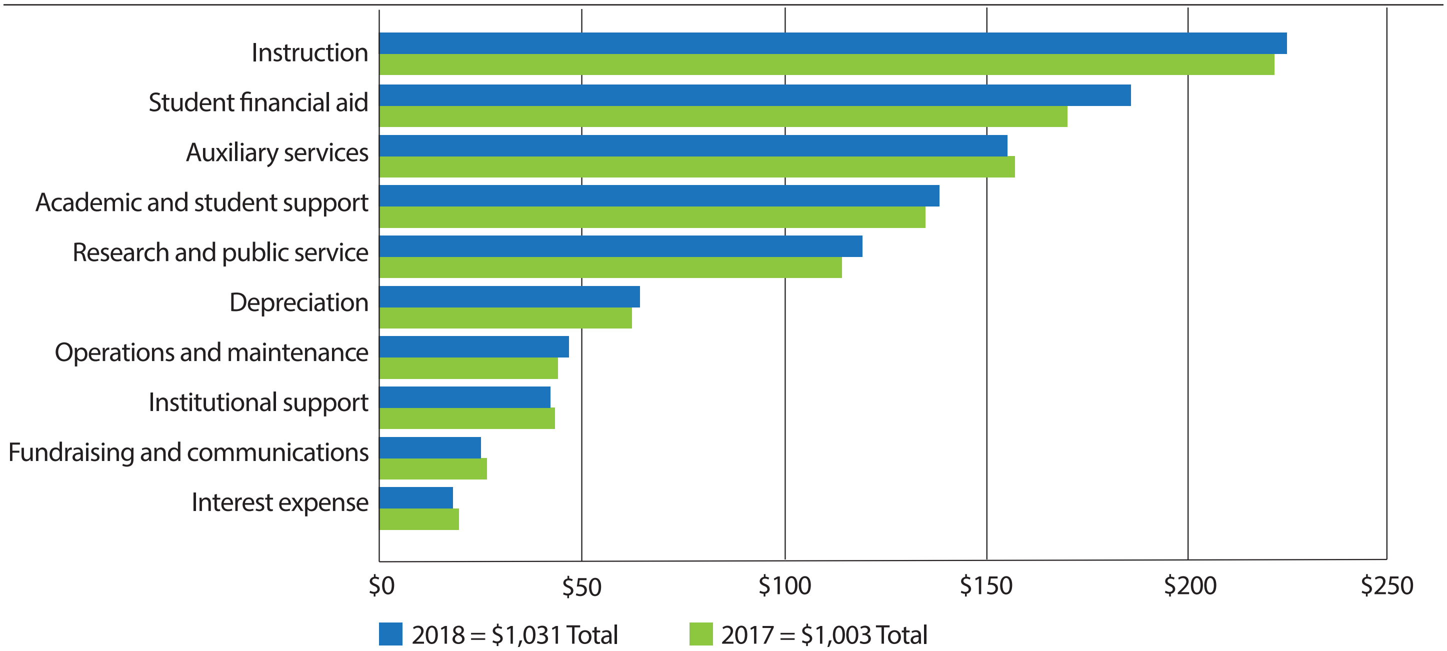



Chart 4 displays USNH's operating expenses for the past two years by functional, rather than natural, classification. The 2018 increases in financial aid discussed above are clearly depicted in the graph. That is the only cost category with such significant growth. (Additional detail on operating expenses by function can be found in Note 13 to the Financial Statements.)

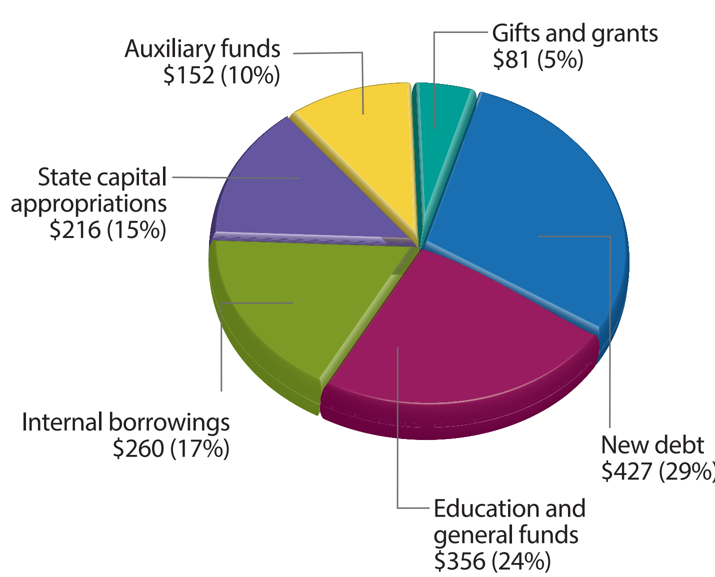
The campuses also have several major capital projects currently underway. These include KSC's Mason Library expansion for Holocaust study materials funded primarily with gift proceeds ($5 million); UNH's water treatment plant shared with the town of Durham ($20 million) funded with internal resources; PSU's physical education center ($10 million) funded with proceeds from bonds issued by USNH as well as internal resources; and PSU's Geneva Smith residence hall ($9 million) funded with internal resources.

Chart 5 to the right shows the funding sources for USNH's capital spending over the past fifteen years. USNH spent over $1 billion during this time to construct and renovate buildings and infrastructure at all campuses. One of the largest sources of funding for the related projects was debt issuances of $427 million. USNH is authorized to issue debt only for self-supporting, auxiliary projects. The majority of the related debt service is funded by student fees for each type of auxiliary service (housing, dining or recreation).

From 2002 to 2013, USNH received significant state capital appropriations to renovate specific science buildings on each campus. During the past ten years operating funds and internal borrowings totaling $616 million were used to supplement the state appropriations. However, there are still several buildings in need of improvement at each campus to ensure USNH is able to meet the education and experiential needs of the state's future workforce. In 2017 USNH engaged third-party consultants to complete a detailed Facilities Condition Assessment and prioritization of deferred maintenance needs at each campus. Because state capital funding has been significantly reduced over the past 5 years, USNH campuses must strategically prioritize the available limited funding for capital assets, while at the same time not allowing deferred maintenance needs to escalate. Plant depreciation expenses of $580 million were recorded during the same 15 year period. (See Notes 5 and 8 to the Financial Statements for additional information on property and equipment, and debt balances.)

## Chart 5: Capital Funding Sources, 2004-2018 Total $1.5 Billion

*($ in millions)*



### C. Investing Activities

Cash and short-term investment balances totaled approximately $206 million on June 30, 2018. This compares to $213 million on June 30, 2017. The reduction is primarily due to purposeful spending of internal resources for the capital projects noted above. Advisory services of cash and short-term investment balances were outsourced in 2015 to improve short-term returns while ensuring sufficient liquidity for near-term obligations. (See Note 2 to the Financial Statements for additional information on cash, cash equivalents and short-term investments.)

USNH's long-term investments are primarily derived from endowment gifts intended to be invested in perpetuity. With Board approval USNH also invests select large, current-use gifts, and unrestricted balances held centrally, as quasi-endowment funds. These amounts are invested in one of three venues depending on whether the donor contributed to a campus, the UNH Foundation (UNHF), or the Keene Endowment Association (KEA). The investment pools are managed to provide the highest rate of return over the long term given an acceptable level of risk as determined by the responsible fiduciaries. The USNH Consolidated Endowment Pool holds funds for the benefit of all campuses. The UNHF endowment pool holds funds for the benefit of UNH only, and the KEA pool holds funds for the benefit of KSC only. The USNH Board of Trustees has fiduciary responsibility for the USNH Pool, whereas the separate boards of UNHF and KEA have their own investment policies and are responsible for those investments. Below is a summary of USNH's endowment and similar investment values for the past three years.

**Table 3: Endowment and Similar Investments Market Value Summary**

*($ in millions)*

| | As of June 30, | | |
|---|---|---|---|
| | **2018** | **2017** | **2016** |
| USNH Pool | $527 | $498 | $444 |
| UNHF Pool | 225 | 204 | 185 |
| KEA Pool | 9 | 8 | 7 |
| Funds held in trust | 16 | 16 | 15 |
| Life Income/Annuity Funds | 4 | 4 | 4 |
| | $781 | $730 | $655 |

While the two larger pools are primarily invested in funds, the KEA pool primarily holds individual stock and bond investments. As shown in Table 4 to the right, the KEA pool net gains over the past five years averaged 10.0% and the USNH and UNHF pools averaged 7.5% and 7.4%, respectively.

Distributions from the pools totaled approximately $28 million in 2018, approximately $1 million higher than the prior year. Distributions of approximately $17 million were made from the USNH pool and trusts, along with $11 million from the UNHF pool and $400,000 from the KEA pool. Distributions represent a smaller percentage of the USNH pool because USNH holds several quasi-endowment funds for future, rather than current, use. Recent volatility in returns has resulted in a limited number of endowment funds having market values less than the original gift value ("underwater" funds). The 2017 and 2018 gains have mitigated this in most cases. Of the 1,472 endowment funds maintained in the various endowment pools, only 42 remained underwater at June 30, 2018. This compares to 46 underwater funds at June 30, 2017. The balances underwater at June 30, 2018 totaled $440,000, compared to $817,000 at June 30, 2017. (See Notes 4 and 12 for further information on endowment and similar investments.)

**Table 4: Pooled Endowment Returns**

| | Year - Ended June 30, 2018 | 2017 | Five Year Average |
|---|---|---|---|
| **USNH Pool** | | | |
| **Gross return** | 8.4% | 13.4% | 7.9% |
| *Investment management fees* | (0.4%) | (0.4%) | (0.4%) |
| **Net return** | 8.0% | 13.0% | 7.5% |
| *Distributions* | (3.2%) | (3.5%) | (3.4%) |
| **Net reinvested** | 4.8% | 9.5% | 4.1% |
| **UNHF Pool** | | | |
| **Gross return** | 8.6% | 14.1% | 8.0% |
| *Investment management fees* | (0.7%) | (0.6%) | (0.6%) |
| **Net return** | 7.9% | 13.5% | 7.4% |
| *Distributions* | (5.3%) | (5.7%) | (5.3%) |
| **Net reinvested** | 2.6% | 7.8% | 2.1% |
| **KEA Pool** | | | |
| **Gross return** | 14.7% | 11.3% | 10.7% |
| *Investment management fees* | (0.7%) | (0.7%) | (0.7%) |
| **Net return** | 14.0% | 10.6% | 10.0% |
| *Distributions* | (3.7%) | (5.7%) | (4.2%) |
| **Net reinvested** | 10.3% | 4.9% | 5.8% |

## IV. Using the Financial Statements

### A. Statements of Net Position

The Statements of Net Position on the following two pages depict all USNH assets, deferred inflows/outflows of resources, and liabilities on June 30th each year, along with the resulting net financial position. An increase in net position over time is a primary indicator of an institution's financial health. Factors contributing to future financial health as reported on the Statements of Net Position include the value and liquidity of financial and capital investments, and balances of related obligations.

Table 5 below shows condensed information from the Statements of Net Position at June 30 for the past five years. Note that we have also included certain condensed information as of June 30, 2018 by campus herein as required by recent regional accreditation standard changes.

## Table 5: Condensed Information from the Statements of Net Position as of June 30,

*($ in millions)*

| | 2014 | 2015 | 2016 | 2017 | 2018* |
|---|---|---|---|---|---|
| Cash and short-term investments | $ 235 | $ 237 | $ 228 | $ 213 | $ 206 |
| Endowment and similar investments | 667 | 679 | 655 | 730 | 781 |
| Property and equipment, net | 982 | 1,010 | 1,077 | 1,120 | 1,122 |
| Other assets and deferred outflows of resources | 96 | 168 | 162 | 106 | 95 |
| **Total Assets and Deferred Outflows of Resources** | 1,980 | 2,094 | 2,122 | 2,169 | 2,204 |
| Derivative instruments - interest rate swaps | 30 | 30 | 37 | 26 | 18 |
| Postretirement medical benefits | 51 | 54 | 56 | 56 | 90 |
| Long-term debt | 431 | 500 | 519 | 501 | 488 |
| Other liabilities and deferred inflows of resources | 150 | 160 | 169 | 152 | 160 |
| **Total Liabilities and Deferred Inflows of Resources** | 662 | 744 | 781 | 735 | 756 |
| Net investment in capital assets | 574 | 598 | 630 | 651 | 665 |
| Restricted financial resources | 397 | 413 | 405 | 454 | 481 |
| Unrestricted financial resources | 347 | 339 | 306 | 329 | 302 |
| **Total Net Position** | $1,318 | $1,350 | $1,341 | $1,434 | $1,448 |

**Beginning net position restated to reflect the adoption of GASB 75 related to postretirement medical obligations.*

As shown above, cash and short-term investment balances have decreased over the past four years. The spending also increased the value of the related property assets. In 2017 endowment returns rebounded after net losses in the prior two years. The 2018 endowment gains were more moderate. This increased the restricted net position, as well as the investment asset balances. The other assets balances above include investments of $69 million, $57 million, $11 million and $4 million, held by our bond trustee related to our Series 2015 and 2016 bond issuances for 2015 through 2018, respectively. In 2017 USNH also transferred assets related to our Operating Staff Retirement Program into a trust, and applied the provisions of GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*. The actuarial reviews completed for the plan in 2017 and 2018 resulted in the recording of a net pension asset of approximately $1 million, which is also included in other assets. Accordingly, no related pension liabilities are recorded for the plan beginning in 2017.

Deferred inflows and outflows of resources include changes in the fair value of USNH's interest rate swap derivatives, as well as accounting gains and losses incurred when refinancing certain bonds outstanding. Because the interest-rate swaps are deemed to be effective hedge instruments, the fair value of the derivatives is recorded to offset the fair value of the interest rate swap liability in its entirety. The accounting gains and losses on debt refinancing are amortized and charged to interest expense annually over the term of the new obligations. The impacts of changes in actuarial assumptions, differences between projected and actual earnings, and benefit payments made after the measurement dates of USNH benefit plans are also included in deferred inflows and outflows beginning in 2017 and 2018 depending on the type of plan.

The reduction in other assets and deferred outflows of resources in 2018 is due to a $7 million reduction in the fair value of interest rate swap obligations, offset by an increase of $2 million in accounting losses on debt refinancing, and postretirement medical plan benefit payments of $3 million which were made after the actuarial review measurement date in 2018. Approximately $11 million of bond proceeds was also unspent at June 30, 2017, then used in 2018 for the fall 2017 occupancy. (See Notes 8 and 9 to the Financial Statements for further discussion of outstanding debt and related interest rate swaps in place.)

In 2017 USNH adopted the provisions of GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement No. 68*, with respect to the accounting for our Additional Retirement Contributions (ARC) plan. In 2018 USNH adopted the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*, for our postretirement medical obligations. The actuarial review completed for the ARC plan in June 2017 resulted in the recording of deferred inflows for the related obligations of approximately $693,000 in 2017 and $629,000 in 2018. The actuarial review completed for the Postretirement Medical Plan in 2018 resulted in recording deferred outflows of approximately $3 million, as well as deferred inflows of approximately $6 million.

The UNH Foundation also adopted the provisions of GASB Statement No.81, Irrevocable Split-Interest Agreements, which resulted in recording deferred inflows of approximately $1 million and $2 million in 2017 and 2018, respectively.

USNH has large liabilities related to long-term debt and postretirement medical benefits. Bond and capital lease principal payments of approximately $16 million and $19 million reduced the related liabilities in 2017 and 2018, respectively. The postretirement obligations represent the actuarially-determined value of medical benefits provided to certain current and former employees for various periods, including the remaining life of the participants in some cases. (See Notes 7 and 8 to the Financial Statements for additional information in this regard.)

Net position is reported in three categories. The net invested in capital assets amount represents the historical cost of property and equipment reduced by total accumulated depreciation and the balance of related debt outstanding for certain auxiliary buildings. Restricted financial resources include balances of current and prior year gifts for specified purposes such as scholarships or academic programs, as well as the majority of campus endowment balances which were requested to be invested in perpetuity by the original donors ($264 million and $270 million at June 30, 2017 and 2018, respectively). Unrestricted financial resources represent net assets that are available for any future use without restriction. (See Note 14 to the Financial Statements for further details on the components of net position.) A breakdown of asset, liability and net position balances by campus as of June 30, 2018 is shown below.

## Table 5A: Condensed Information from the Statement of Net Position as of June 30, 2018 Presented by Campus

*($ in millions)*

| | University of New Hampshire Campuses & Foundation | Plymouth State University | Keene State College & Endowment Association | Granite State College | Chancellor's Office | Total University System of New Hampshire |
|---|---|---|---|---|---|---|
| Cash and short-term investments | $ 251 | $ 44 | $ 58 | $ 20 | $(167) | $ 206 |
| Endowment and similar investments | 391 | 27 | 37 | 7 | 319 | 781 |
| Property and equipment, net | 747 | 189 | 177 | 8 | 1 | 1,122 |
| Other assets and deferred outflows of resources | (32) | (8) | (2) | (1) | 138 | 95 |
| Total Assets and Deferred Outflows of Resources | 1,357 | 252 | 270 | 34 | 291 | 2,204 |
| Derivative instruments - interest rate swaps | | | | | 18 | 18 |
| Postretirement medical benefits | 70 | 12 | 12 | 2 | (6) | 90 |
| Long-term debt | 197 | 104 | 103 | – | 84 | 488 |
| Other liabilities and deferred inflows of resources | 84 | 14 | 7 | 2 | 53 | 160 |
| Total Liabilities and Deferred Inflows of Resources | 351 | 130 | 122 | 4 | 149 | 756 |
| Net investment in capital assets | 474 | 72 | 71 | 5 | 43 | 665 |
| Restricted financial resources | 404 | 25 | 43 | 9 | – | 481 |
| Unrestricted financial resources | 128 | 25 | 34 | 16 | 99 | 302 |
| Total Net Position | $1,006 | $122 | $148 | $30 | $142 | $1,448 |

*Beginning net position restated to reflect the impact of adoption of GASB 75 related to postretirement medical obligations.*

## B. Statements of Revenues, Expenses and Changes in Net Position

Operating revenues are generally earned in exchange for providing goods and services. However, GASB reporting standards require that some of USNH's recurring revenues be shown as nonoperating. This includes state general appropriations, federal Pell grants, noncapital gifts, operating investment income, and the portion of endowment returns used to fund the related programs. These revenue streams are important sources of funds used to supplement tuition and fees revenue. Accordingly, we have grouped the operating and nonoperating revenues together in the condensed statement below to allow readers to better understand which revenues support operating expense streams.

Table 6 shows condensed information from the Statements of Revenues, Expenses and Changes in Net Position for the five years ended June 30, 2018.

The net tuition and other revenue values on these statements reflect the size and type of student enrollments, financial need, and growth of supporting revenue streams. Total operating and nonoperating revenues were up $6 million in 2018, primarily due to increases in grant and noncapital gifts revenues. Expenses were up approximately $12 million in 2018, after being held flat in 2017. Compensation, utilities and depreciation cost increases were offset by a decrease in supplies and services costs.

The increase in net position from recurring activities reflects USNH's operating margin each year. USNH's margin for 2018 was half the level of 2017. This reflects the increased investment in institutional financial aid provided as discussed previously. USNH is implementing a cloud-based ERP upgrade and a new EPM system to help improve forecasting and control costs. The USNH Board of Trustees is monitoring these initiatives, particularly our move to more electronic procurement, as work continues to lower administrative cost structures.

## Table 6: Condensed Information from the Statements of Revenues, Expenses and Changes in Net Position for the Years Ended June 30,

*($ in millions)*

| | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|
| Tuition and fees | $465 | $472 | $491 | $501 | $514 |
| Less: student financial aid | (144) | (149) | (162) | (172) | (188) |
| Net tuition and fees | 321 | 323 | 329 | 329 | 326 |
| Sales of auxiliary services | 203 | 206 | 211 | 216 | 215 |
| Grants and contracts | 152 | 149 | 149 | 146 | 153 |
| State general appropriations | 69 | 81 | 81 | 81 | 81 |
| Noncapital gifts, investment income and other revenues | 65 | 66 | 79 | 71 | 74 |
| Total Operating and Nonoperating Revenues | 810 | 825 | 849 | 843 | 849 |
| Employee compensation | 481 | 503 | 529 | 521 | 533 |
| Supplies and services | 195 | 203 | 203 | 210 | 208 |
| Utilities, depreciation and interest | 98 | 98 | 99 | 100 | 102 |
| Total Operating and Nonoperating Expenses | 774 | 804 | 831 | 831 | 843 |
| Increase in Net Position from Recurring Activities | 36 | 21 | 18 | 12 | 6 |
| Endowment gifts and returns, net | 83 | 6 | (30) | 70 | 45 |
| State capital appropriations and other changes | 10 | 5 | 3 | 11 | 5 |
| Total Other Changes in Net Position | 93 | 11 | (27) | 81 | 50 |
| Cumulative effect of adoption of GASB 75 related to accounting for postretirement medical obligations | – | – | – | – | (42) |
| Total Increase (Decrease) in Net Position | $129 | $ 32 | $ (9) | $ 93 | $ 14 |

Endowment gifts totaled $16 million in 2018, and $13 million in 2017. Most of these gifts were due to UNH's recent capital campaign which ended in 2018. The investment return after distributions totaled $29 million in 2018 compared to $56 million in 2017. The volatility of endowment returns is a significant driver of the change in total net position each year.

Table 6A below provides condensed information from the Statement of Revenues, Expenses and Changes in Net Position presented by campus for the year ended June 30, 2018.

## Table 6A: Condensed Information from the Statement of Revenues, Expenses and Changes in Net Position for the Year Ended June 30, 2018, Presented by Campus *($ in millions)*

| | University of New Hampshire Campuses & Foundation | Plymouth State University | Keene State College & Endowment Association | Granite State College | Chancellor's Office | Total University System of New Hampshire |
|---|---|---|---|---|---|---|
| Tuition and fees | $361 | $ 73 | $ 65 | $ 15 | $ – | $514 |
| Less: student financial aid | (133) | (26) | (23) | (6) | – | (188) |
| Net tuition and fees | 228 | 47 | 42 | 9 | – | 326 |
| Sales and auxiliary services | 150 | 31 | 34 | – | – | 215 |
| Grants and contracts | 132 | 8 | 8 | 5 | – | 153 |
| State general appropriations | 55 | 12 | 11 | 3 | – | 81 |
| Noncapital gifts, investment income and other revenues | 60 | 5 | 6 | 2 | 1 | 74 |
| Total Operating and Nonoperating Revenues | 625 | 103 | 101 | 19 | 1 | 849 |
| Employee compensation | 393 | 59 | 61 | 13 | 7 | 533 |
| Supplies and services | 154 | 26 | 28 | 4 | (4) | 208 |
| Utilities, depreciation and interest | 65 | 17 | 16 | 1 | 3 | 102 |
| Total Operating and Nonoperating Expenses | 612 | 102 | 105 | 18 | 6 | 843 |
| Change in Net Position from Recurring Activities | 13 | 1 | (4) | 1 | (5) | 6 |
| Endowment gifts and returns, net | 23 | 3 | 3 | 1 | 15 | 45 |
| State capital appropriations and other changes, net* | (27) | (3) | (6) | (2) | 1 | (37) |
| Total Other Changes in Net Position | (4) | – | (3) | (1) | 16 | 8 |
| Total Increase (Decrease) in Net Position | $ 9 | $ 1 | $ (7) | $ – | $ 11 | $ 14 |

** Includes impact of adoption of GASB Statement 75 related to postretirement medical obligations.*

## C. Statements of Cash Flows

The Statements of Cash Flows summarize transactions affecting cash and cash equivalents during the fiscal period. Table 7 below shows summary information from the Statements of Cash Flows for the five years ended June 30, 2018.

### Table 7: Condensed Information from the Statements of Cash Flows for the Years Ended June 30,

*($ in millions)*

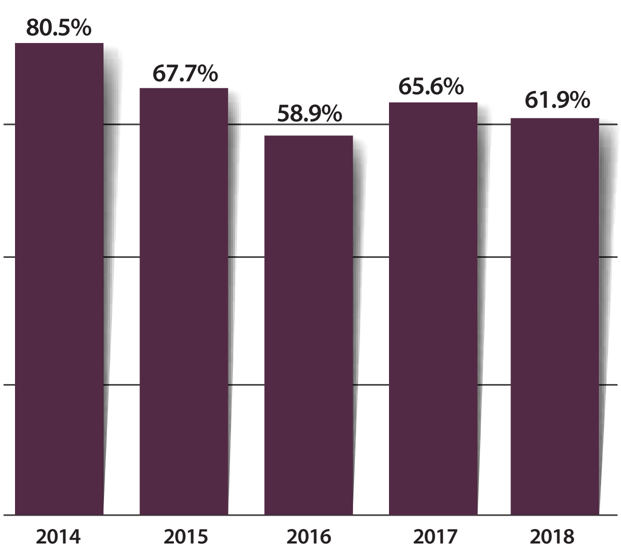
| | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|
| **Cash flows from:** | | | | | |
| Receipts from tuition and fees, net | $321 | $324 | $331 | $332 | $328 |
| Receipts from sales of auxiliary services | 204 | 206 | 208 | 217 | 214 |
| Receipt of state general appropriations | 69 | 81 | 81 | 81 | 81 |
| Noncapital gifts, grants and other receipts | 192 | 190 | 193 | 188 | 203 |
| Payments to and on behalf of employees | (478) | (499) | (518) | (543) | (537) |
| Payments for supplies, services and utilities | (223) | (224) | (222) | (227) | (227) |
| **Net Cash Provided by Operating and Noncapital Financing Activities** | 85 | 78 | 73 | 48 | 62 |
| **Net Cash Used in Capital Financing Activities** | (75) | (5) | (110) | (120) | (83) |
| **Net Cash (Used in)/Provided by Investing Activities** | (10) | (73) | 26 | 69 | 10 |
| **Increase/(Decrease) in Cash and Cash Equivalents** | $ – | $ – | $ (11) | $ (3) | $(11) |

These statements provide information about cash collections and cash payments made by USNH each year to help readers assess our ability to generate the future cash flows necessary to meet current and future obligations. Cash flows from operating activities will always be different than the operating results on the Statements of Revenues, Expenses and Changes in Net Position because of the inclusion of noncash items, such as depreciation expense, and because the latter statement is prepared on the accrual basis of accounting, meaning that it shows revenues when earned and expenses as incurred. The increase in cash flows from operating and noncapital financing activities is primarily related to the increase in grant revenues during 2018. The net cash used in capital financing activities for 2018 is lower since most of the prior year investments generated by USNH's recent bond issuances had already been liquidated in prior years. The lower level of available bond proceeds also reduced the net cash provided by investing activities in 2018.

## D. Financial Health

USNH's primary indicator of its financial health is the level of unrestricted financial resources to external debt outstanding. This ratio uses the unrestricted net position balance as the numerator and the total long-term debt balance outstanding as the denominator. USNH's targeted unrestricted financial resources to debt ratio is 50% or above. The average of this ratio over the past five years was 67% reflecting sufficient available support of ongoing initiatives. (See Notes 8 and 14 to the Financial Statements for additional information in this regard).

### Chart 6: Unrestricted Financial Resources to Total Debt



## University System of New Hampshire
### Statements of Net Position

*($ in thousands)*

| | Balance at June 30, | |
|---|---|---|
| | **2018** | **2017** |
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and cash equivalents | $ 55,128 | $ 66,069 |
| Short-term investments | 151,150 | 146,588 |
| Accounts receivable, net | 20,628 | 21,729 |
| Pledges receivable, net - current portion | 3,299 | 3,187 |
| Notes receivable, net - current portion | 2,711 | 3,293 |
| Prepaid expenses and other current assets | 7,590 | 7,811 |
| Total Current Assets | 240,506 | 248,677 |
| **Noncurrent Assets** | | |
| Debt proceeds held by bond trustee for construction purposes | 4,239 | 10,718 |
| Endowment and similar investments - campuses | 543,365 | 514,162 |
| Endowment and similar investments - affiliated entities | 237,917 | 216,346 |
| Pledges receivable, net of current portion | 5,501 | 7,106 |
| Notes receivable, net of current portion | 18,070 | 18,094 |
| Pension assets | 724 | 993 |
| Property and equipment, net | 1,122,011 | 1,119,628 |
| Total Noncurrent Assets | 1,931,827 | 1,887,047 |
| **TOTAL ASSETS** | **2,172,333** | **2,135,724** |
| | | |
| **DEFERRED OUTFLOWS OF RESOURCES** | **31,436** | **33,067** |
| | | |
| **LIABILITIES** | | |
| **Current Liabilities** | | |
| Accounts payable and accrued expenses | 59,924 | 57,238 |
| Deposits and unearned revenues | 39,864 | 37,682 |
| Accrued employee benefits - current portion | 6,917 | 7,407 |
| Postretirement medical benefits - current portion | 5,837 | 6,018 |
| Long-term debt - current portion | 22,968 | 20,064 |
| Total Current Liabilities | 135,510 | 128,409 |
| **Noncurrent Liabilities** | | |
| Obligations under life income agreements | 2,000 | 2,126 |
| Refundable government advances | 16,679 | 16,643 |
| Accrued employee benefits, net of current portion | 25,736 | 27,178 |
| Postretirement medical benefits, net of current portion | 83,975 | 50,251 |
| Derivative instruments - interest rate swaps | 18,294 | 25,759 |
| Long-term debt, net of current portion | 465,219 | 481,401 |
| Total Noncurrent Liabilities | 611,903 | 603,358 |
| **TOTAL LIABILITIES** | **747,413** | **731,767** |
| | | |
| **DEFERRED INFLOWS OF RESOURCES** | **8,700** | **3,508** |
| | | |
| **NET POSITION** (see Note 14) | | |
| Net investment in capital assets | 665,194 | 650,968 |
| Restricted | | |
| Nonexpendable | 263,969 | 270,089 |
| Expendable | 216,339 | 183,540 |
| Unrestricted | 302,154 | 328,919 |
| **TOTAL NET POSITION** | **$1,447,656** | **$1,433,516** |

*See accompanying notes to the financial statements.*

## University System of New Hampshire
### Statements of Revenues, Expenses and Changes in Net Position
*($ in thousands)*

| | For the year ended June 30, | |
|---|---|---|
| | **2018** | **2017** |
| **OPERATING REVENUES** | | |
| Resident tuition | $ 165,325 | $ 164,406 |
| Nonresident tuition | 299,663 | 288,702 |
| Continuing education tuition | 20,749 | 21,110 |
| Student fees revenue | 28,072 | 26,901 |
| Total tuition and fees | 513,809 | 501,119 |
| Less: student financial aid - grants and contracts | (33,591) | (31,533) |
| Less: student financial aid - all other | (153,890) | (140,069) |
| Net tuition and fees | 326,328 | 329,517 |
| Grants and contracts - direct revenues | 105,735 | 101,033 |
| Grants and contracts - facilities & administrative recovery | 21,160 | 20,060 |
| Sales of auxiliary services | 214,784 | 215,554 |
| Other operating revenues | 29,677 | 29,800 |
| **TOTAL OPERATING REVENUES** | **697,684** | **695,964** |
| **OPERATING EXPENSES** | | |
| Employee compensation - grants and contracts | 61,714 | 59,324 |
| Employee compensation - all other | 471,004 | 461,372 |
| Supplies and services - grants and contracts | 32,416 | 31,342 |
| Supplies and services - all other | 175,883 | 178,511 |
| Utilities | 19,065 | 17,949 |
| Depreciation | 65,096 | 62,942 |
| **TOTAL OPERATING EXPENSES** | **825,178** | **811,440** |
| Operating loss | (127,494) | (115,476) |
| **NONOPERATING REVENUES (EXPENSES)** | | |
| State of New Hampshire general appropriations | 81,000 | 81,000 |
| Federal Pell grants | 26,408 | 24,603 |
| Noncapital gifts | 14,101 | 11,424 |
| Endowment and investment income | 29,667 | 29,970 |
| Interest expense, net | (18,440) | (19,521) |
| Other nonoperating revenue | 349 | 241 |
| **TOTAL NONOPERATING REVENUES (EXPENSES)** | **133,085** | **127,717** |
| **INCREASE IN NET POSITION BEFORE OTHER CHANGES** | **5,591** | **12,241** |
| **OTHER CHANGES IN NET POSITION** | | |
| State of New Hampshire capital appropriations | 3,000 | 3,611 |
| Plant gifts, grants and other changes, net | 1,862 | 7,828 |
| Endowment and similar gifts | 16,494 | 13,395 |
| Endowment return, net of amount used for operations | 28,985 | 56,296 |
| **TOTAL OTHER CHANGES IN NET POSITION** | **50,341** | **81,130** |
| **INCREASE IN NET POSITION** | **55,932** | **93,371** |
| Net Position at Beginning of Year | 1,433,516 | 1,340,145 |
| Effect of adoption of new accounting standard related to postemployment benefits other than pensions | (41,792) | – |
| **NET POSITION AT END OF YEAR** | **$1,447,656** | **$1,433,516** |

*See accompanying notes to the financial statements.*

# University System of New Hampshire
## Statements of Cash Flows
*($ in thousands)*

| | For the year ended June 30, | |
|---|---|---|
| | 2018 | 2017 |
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Receipts from tuition and fees, net of student financial aid | $ 327,532 | $ 331,935 |
| Receipts from sales of auxiliary services | 214,353 | 216,831 |
| Receipts from grants, contracts and other operating revenues | 160,598 | 150,932 |
| Payments to employees | (404,062) | (402,840) |
| Payments for employee benefits | (133,283) | (139,960) |
| Payments for supplies, services and utilities | (226,678) | (226,957) |
| **NET CASH USED IN OPERATING ACTIVITIES** | **(61,540)** | **(70,059)** |
| **CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES** | | |
| State general appropriations | 81,000 | 81,000 |
| Federal Pell and other nonoperating grants | 26,757 | 24,844 |
| Noncapital gifts | 15,599 | 12,516 |
| **NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES** | **123,356** | **118,360** |
| **CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES** | | |
| State appropriations for plant projects | 1,762 | 3,973 |
| Plant gifts and grants | 6,307 | 10,614 |
| Endowment gifts | 17,002 | 13,429 |
| Proceeds from issuance of debt and sale of property | 109,736 | 66 |
| Purchases and construction of property | (72,427) | (112,843) |
| Retirement of debt through defeasance | (106,572) | 16 |
| Debt principal payments | (18,632) | (16,089) |
| Interest payments | (19,994) | (19,874) |
| **NET CASH USED IN CAPITAL FINANCING ACTIVITIES** | **(82,818)** | **(120,708)** |
| **CASH FLOWS FROM INVESTING ACTIVITIES** | | |
| Proceeds from sale of investments | 718,539 | 507,248 |
| Purchase of investments | (717,912) | (445,502) |
| Investment income | 9,434 | 7,576 |
| **NET CASH PROVIDED BY INVESTING ACTIVITIES** | **10,061** | **69,322** |
| Decrease in cash and cash equivalents | $ (10,941) | $ (3,085) |
| Beginning cash and cash equivalents | 66,069 | 69,154 |
| **ENDING CASH AND CASH EQUIVALENTS** | **$ 55,128** | **$ 66,069** |
| **RECONCILIATION OF OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES** | | |
| Operating loss | $(127,494) | $ (115,476) |
| Adjustments to reconcile operating loss to net cash used in operating activities: | | |
| Depreciation | 65,096 | 62,942 |
| Changes in current assets and liabilities: | | |
| Accounts receivable, net | 2,339 | (1,803) |
| Notes receivable | 642 | 695 |
| Prepaid expenses and other current assets | 221 | 947 |
| Accounts payable and accrued expenses | 3,446 | (8,103) |
| Deposits and unearned revenues | 2,135 | 4,970 |
| Accrued employee benefits | (7,925) | (14,231) |
| **NET CASH USED IN OPERATING ACTIVITIES** | **$(61,540)** | **$(70,059)** |
| **SIGNIFICANT NONCASH TRANSACTIONS** | | |
| Endowment return, net of amount used for operations | $ 28,985 | $ 56,296 |
| Loss on disposal of capital assets | (4,403) | (1,978) |
| Construction services payable balance | 10,373 | 10,642 |

*See accompanying notes to the financial statements.*

## 1. Summary of significant accounting policies and presentation

The University System of New Hampshire (USNH) is a not-for-profit institution of higher education created in 1963 as a body politic and corporate under the laws of the State of New Hampshire (the State) and is generally exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. USNH is considered a component unit of the State for financial reporting purposes. The accompanying financial statements include the accounts of the University of New Hampshire (UNH), Plymouth State University (PSU), Keene State College (KSC), and Granite State College (GSC) as well as certain affiliated entities discussed below. UNH, PSU, KSC and GSC are collectively referred to in the accompanying financial statements as "campuses."

### Affiliated entities and related parties

Governmental accounting standards require that all potential component units be evaluated for inclusion in the financial statements of the primary government of the reporting entity. USNH's policy on 'Foundations Established for the Benefit of USNH or its Component Institutions' states that the USNH Board of Trustees retains control over the activities of any affiliated foundation. The USNH policy further states that USNH has the legal authority to terminate the existence of any affiliated foundation, at which time ownership of the related assets would revert to USNH. Two legally separate affiliated foundations are impacted by this policy and, accordingly, are considered blended component units of USNH. The University of New Hampshire Foundation, Inc. (UNHF) and the Keene Endowment Association (KEA) are collectively referred to in the accompanying financial statements as "affiliated entities." The associated revenues, expenses, assets, liabilities, deferred inflows, deferred outflows and net position of UNHF and KEA are fully consolidated with those of the campuses in the accompanying financial statements, and all associated inter-entity activity has been eliminated.

UNHF, Inc. was incorporated in 1989 as a not-for-profit, tax-exempt organization. Its purpose is to solicit, collect, invest and disburse funds for the sole benefit of the University of New Hampshire. The University of New Hampshire funds a portion of the operating expenses of UNHF. UNHF is governed by its own Board of Directors, the membership of which includes the President of the University of New Hampshire and up to three other members of the USNH Board of Trustees. UNHF has a separate financial statement audit each year. Condensed financial information for UNHF is included in Note 16. The KEA was organized in 1957 as a separate charitable entity to provide financial assistance to deserving students at Keene State College. Income is distributed at the discretion of the Trustees of KEA.

### Basis of accounting

The accompanying financial statements have been prepared in accordance with US generally accepted accounting principles (GAAP) prescribed by the Governmental Accounting Standards Board (GASB) using the economic resources measurement focus and the accrual basis of accounting.

USNH follows the requirements of the "business-type activities" (BTA) model as defined by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis for Public Colleges and Universities*. BTAs are defined as those that are financed in whole or in part by fees charged to external parties for goods or services. The Statement requires that resources be classified into the following net position categories, as more fully detailed in Note 14:

**Net investment in capital assets:** Property and equipment at historical cost or fair value on date of acquisition, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition or construction of those assets.

**Restricted Nonexpendable:** Resources subject to externally imposed stipulations that they be maintained permanently by USNH. These funds include the historical gift value of restricted true endowment funds.

**Restricted Expendable:** Resources whose use by USNH is subject to externally imposed stipulations. Such funds include the accumulated net gains on donor-restricted "true" endowment funds; the fair value of restricted funds functioning as endowment; restricted funds loaned to students; restricted gifts and endowment income; and other similarly restricted funds.

**Unrestricted:** Resources that are not subject to externally imposed stipulations. Substantially all unrestricted net position funds are designated to support academic, research, or auxiliary enterprises; invested to function as endowment; or committed to capital construction projects.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. The most significant areas that require management estimates relate to valuation of certain investments and derivative instruments, useful life and related depreciation of capital assets, and accruals for postretirement medical and other employee-related benefits.

Investments are maintained with established financial institutions whose credit is evaluated by management and the respective governing boards of USNH and its affiliated entities. Investments of operating cash in money market and other mutual funds are generally recorded as cash equivalents. These amounts are invested for purposes of satisfying current operating liabilities and generating investment income to support ongoing operations. Short-term investments represent highly liquid amounts held for other current liabilities.

Property and equipment are recorded at original cost for purchased assets or at fair value on the date of donation in the case of gifts. Equipment with a unit cost of $5,000 or more is capitalized. Building improvements with a cost of $50,000 or greater are also capitalized. Net interest costs incurred during the construction period for major, debt-funded capital projects are added to the cost of the underlying asset. The value of equipment acquired under capital leases is recorded at the present value of the minimum lease payments at the inception of the lease. Depreciation of property and equipment is calculated on a straight-line basis over the estimated useful lives of the respective assets. The cost of certain research buildings is componentized for the purpose of calculating depreciation. Buildings and improvements are depreciated over useful lives ranging from 10 to 50 years. Depreciable lives for equipment range from 3 to 30 years. (See Note 5 for additional information on depreciation.) USNH does not record donated works of art and historical treasures that are held for exhibition, education, research and public service. Library collections are recorded as an expense in the period purchased, with the exception of UNH School of Law library collections which are capitalized annually and depreciated over a ten year period on a straight-line basis.

Deposits and unearned revenue consist of amounts billed or received in advance of USNH providing goods or services. Advances from the US Government for Federal Perkins loans to students are reported as government advances refundable. Federal Direct Loan proceeds are posted to student accounts as approved and drawn weekly.

Operating revenues include tuition and fees, grants and contracts, sales of auxiliary services, and other operating revenues. Tuition and fee revenues are reported net of student financial aid discounts and allowances. Operating expenses include employee compensation and benefits, supplies and services, utilities, and depreciation. Operating expenses also include early retirement and other separation incentive stipends and benefits promised to certain employees in exchange for termination of employment. All such termination benefits are accrued as of the date the termination agreements are signed, and are presented at net present value at year end. Nonoperating revenues (expenses) include all other revenues and expenses except certain changes in long-term plant, endowment and other net position funds, which are reported as other changes in net position. Operating revenues are recognized when earned and expenses are recorded when incurred. Restricted grant revenue is recognized only to the extent of applicable expenses incurred or, in the case of fixed-price contracts, when the contract terms are met or completed.

Unconditional pledges of nonendowment gifts are presented net of estimated amounts deemed uncollectible after discounting to the present value of expected future cash flows. Because of uncertainties with regard to their realization and valuation, bequest intentions and other conditional promises are not recognized as assets until the specified conditions are met. In accordance with GASB requirements, endowment pledges expected to be received over the next ten years, totaling $8,166,000 and $8,227,000 at June 30, 2018 and 2017, respectively, have not been reported in the accompanying financial statements. USNH generally uses restricted funds first when an expense is incurred where both restricted and unrestricted funds are available.

Endowment return used for operations per application of the Board-approved endowment spending policy is reported as nonoperating revenue. Net realized and unrealized gains/losses and interest/dividend income earned on endowment and similar investments, together with the excess (deficiency) of these earnings over the return used for operations, are reported as other changes in net position.

The System's financial statements include comparative financial information. Certain prior year amounts have been reclassified to conform to the current year presentation.

**New reporting standards**
The System's financial statements and notes for fiscal 2018 as presented herein reflect the adoption of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, as of July 1, 2017. GASB 75 requires recording of the full actuarially determined postemployment benefits liability, modifies the presentation of certain postemployment benefits related assets and obligations, and requires new and enhanced disclosures related to these benefits plans. Note that the prior year data has not been restated as allowed under this standard. Additional information can be found in Notes 7 and 10, respectively. The System also adopted GASB Statement No. 81, *Irrevocable Split-Interest Agreements,* for both fiscal years 2017 and 2018. GASB 81 modifies the reporting and recognition of certain deferred giving instruments, collectively referred to as annuities. As a result of this adoption the opening net position as of July 1, 2016 was reduced by $1,055,000.

## 2. Cash, cash equivalents and short-term investments

Cash, cash equivalents, and short-term investments are recorded at fair value. USNH's investment policy and guidelines specify permitted instruments, durations, required ratings and insurance of USNH cash, cash equivalents and short-term investments. The investment policy and guidelines are intended to mitigate credit risk on investments individually and in the aggregate through restrictions on investment type, liquidity, custodian, dollar level, maturity, and rating category. Money market funds are placed with the largest national fund managers. These funds must be rated AA/Aa by Standard & Poor's and Moody's Investor Service and comply with Securities and Exchange Commission Rule 2A-7. Repurchase agreements must be fully collateralized at 102% of the face value by US Treasuries, or 103% of the face value by US Government- backed or guaranteed agencies or government sponsored enterprises. In addition, USNH investments may not exceed 5% of any institution's total deposits or 20% of any institution's net equity.

Cash equivalents represent amounts invested to satisfy current operating liabilities and include repurchase agreements, money market funds and other mutual funds. Repurchase agreements are limited to overnight investments only. Short-term investments are highly liquid amounts held to support specific current liabilities. Cash, cash equivalents and short-term investments are generally uninsured and uncollateralized against custodial credit risk, and the related mutual funds are not rated. Cash and cash equivalents totaled $55,128,000 and $66,069,000 at June 30, 2018 and 2017, respectively, and short-term investments totaled $151,150,000 and $146,588,000 at June 30, 2018 and 2017, respectively. See Note 4 for additional information on fair value classifications.

The components of cash, cash equivalents and short-term investments are summarized below *($ in thousands)*:

| | Balances and Terms as of June 30, 2018 | | | | Balances and Terms as of June 30, 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Total** | **Weighted Average Maturity** | **Level 1** | **Level 2** | **Total** | **Weighted Average Maturity** |
| Cash balance | $ 10,654 | $ – | $ 10,654 | Less than 1 year | $ 18,144 | $ – | $ 18,144 | Less than 1 year |
| Repurchase agreements | – | 7,018 | 7,018 | Less than 1 year | – | 11,134 | 11,134 | Less than 1 year |
| Money market funds | 37,456 | – | 37,456 | Less than 1 year | 36,791 | – | 36,791 | Less than 1 year |
| **Subtotal cash and cash equivalents** | 48,110 | 7,018 | 55,128 | | 54,935 | 11,134 | 66,069 | |
| Money market funds | 30,888 | – | 30,888 | Less than 1 year | 28,118 | – | 28,118 | Less than 1 year |
| Domestic equity | 298 | – | 298 | Less than 1 year | 276 | – | 276 | Less than 1 year |
| Mutual funds | 93,928 | – | 93,928 | 1-5 years | 91,947 | – | 91,947 | 1-5 years |
| Corporate bonds | – | 14,254 | 14,254 | 1-5 years | – | 16,404 | 16,404 | 1-5 years |
| US government and agencies | – | 9,972 | 9,972 | 1-5 years | – | 7,689 | 7,689 | 1-5 years |
| Municipal bonds | – | 1,797 | 1,797 | 1-5 years | – | 2,149 | 2,149 | 1-5 years |
| Convertible note | – | 13 | 13 | 1-5 years | – | 5 | 5 | 1-5 years |
| **Subtotal short-term investments** | 125,114 | 26,036 | 151,150 | | 120,341 | 26,247 | 146,588 | |
| **Total cash, cash equivalents and short-term investments** | $173,224 | $33,054 | $206,278 | | $175,276 | $37,381 | $212,657 | |

## 3. Accounts, pledges and notes receivable

Accounts receivable at June 30 consisted of the following *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| Grants and contracts | $16,296 | $18,847 |
| Student and general | 6,589 | 6,095 |
| State of NH capital projects | 1,238 | – |
| Allowance for doubtful accounts | (3,495) | (3,213) |
| **Total accounts receivable, net** | $20,628 | $21,729 |

Pledges receivable at June 30 consisted entirely of unconditional nonendowment promises to pay as follows *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| Pledges receivable | $12,119 | $13,884 |
| Discounts and allowance for doubtful pledges | (3,319) | (3,591) |
| **Total pledges receivable, net** | 8,800 | 10,293 |
| Less: noncurrent portion | (5,501) | (7,106) |
| **Current portion** | $ 3,299 | $ 3,187 |

Notes receivable at June 30 consisted primarily of student loan funds as follows *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| Perkins loans | $22,134 | $22,481 |
| Other loans, restricted and unrestricted | 748 | 874 |
| Allowance for doubtful loans | (2,101) | (1,968) |
| **Total notes receivable, net** | 20,781 | 21,387 |
| Less: noncurrent portion | (18,070) | (18,094) |
| **Current portion** | $ 2,711 | $ 3,293 |

## 4. Investments

USNH's investment policy and guidelines specify permitted instruments, duration and required ratings for pooled endowment funds. The policy and guidelines are intended to mitigate risk on investments individually and in the aggregate while maximizing total returns and supporting intergenerational equity of spending levels. Illiquid investments are limited to 20% of the USNH consolidated endowment pool. Credit risk is mitigated by due diligence in the selection and continuing review of investment managers as well as diversification of both investment managers and underlying investments. No more than 15% of total portfolio assets may be invested in any single fund and no more than 20% of the pool may be invested with any single bank, fund manager, or investment group unless approved by the USNH Board of Trustees' Finance Committee for Investments. Foreign currency risk is mitigated by limiting global equity investments in publicly traded international and emerging market funds to 25% of the endowment pool. Private global equity investments are limited to 15% of the endowment pool. No USNH endowment investments were denominated in foreign currencies as of June 30, 2018 or June 30, 2017.

GASB Statement No. 72, *Fair Value Measurement and Application*, requires that USNH categorize assets measured at fair value using a three-tiered hierarchy based on the valuation methodologies employed.

The hierarchy includes the following:

**Level 1** — Value based on quoted prices (unadjusted) in active markets for identical assets that are accessible at the measurement date

**Level 2** — Value based on inputs other than quoted prices that are observable for an asset either directly or indirectly; and

**Level 3** — Value based on unobservable inputs for an asset

In determining fair value of investment assets, USNH utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. As a practical expedient to estimate the fair value of USNH's interests, certain investments in commingled funds and limited partnerships are reported at the net asset value (NAV) determined by the respective fund managers, without adjustment when assessed as reasonable by USNH, unless it is probable that all or a portion of the investment will be sold for an amount different from NAV. Because these investments are not readily marketable, their estimated fair values may differ from the values that would have been assigned had a ready market for such investments existed, and such differences could be material. As of June 30, 2018, and 2017, USNH had no plans or intentions to sell such investments at amounts different from NAV. Investments reported at NAV as a practical expedient are not categorized in the fair value hierarchy.

The endowment and similar investment holdings of the campuses and affiliated entities as of June 30, 2018 and 2017, respectively, are summarized below *($ in thousands):*

| | Campuses | | Affiliated Entities | |
|---|---|---|---|---|
| | 2018 | 2017 | 2018 | 2017 |
| Pooled endowments: | | | | |
| Campuses | $527,063 | $ 497,885 | $ – | $ – |
| UNH Foundation | – | – | 224,648 | 204,468 |
| Keene Endowment Association | – | – | 8,869 | 7,820 |
| Life income and annuity funds | 87 | 85 | 4,400 | 4,058 |
| Funds held in trust | 16,215 | 16,192 | – | – |
| Total | $543,365 | $514,162 | $237,917 | $216,346 |

The majority of USNH's investments are units of institutional commingled funds and limited partnerships invested in equity, fixed income, hedge, natural resources, private equity, or real estate strategies. Hedge strategies involve funds whose managers have the authority to invest in various asset classes at their discretion, including the ability to invest long and short. Funds with hedge strategies generally hold securities or other financial instruments for which a ready market exists and may include stocks, bonds, put or call options, swaps, currency hedges and other instruments which are valued by the investment manager. To the extent quoted prices exist the manager would use those; when these are not available, other methodologies maximizing observable inputs would be used for the valuation, such as discounted cash flow analysis, capitalization of current or stabilized net operating income, replacement costs, or sales contracts and recent sales comparable in the market. Private equity funds employ buyout, growth and venture capital, and distressed security strategies. Real asset funds generally hold interests in private real estate. As of June 30, 2018 and 2017, fixed income securities had maturities up to 29 years and carried ratings ranging from AAA to A3. The mutual fund investments held in the endowment pools are not rated.

The following table summarizes the fair value of USNH's investments by type ordered by liquidity terms shown on the following page *($ in thousands)*:

| | Balances as of June 30, 2018 | | | | Balances as of June 30, 2017 | | | |
|---|---|---|---|---|---|---|---|---|
| | Investments Classified in Fair Value Hierarchy | | Investments Measured | | Investments Classified in Fair Value Hierarchy | | Investments Measured | |
| | Level 1 | Level 2 | at NAV | Total | Level 1 | Level 2 | at NAV | Total |
| **Endowment and similar investments – campuses** | | | | | | | | |
| Money market | $ 14,671 | $ – | $ – | $ 14,671 | $ 13,694 | $ – | $ – | $ 13,694 |
| Global fixed income | 17,554 | 36,511 | – | 54,065 | 17,865 | 29,214 | – | 47,079 |
| Inflation hedging assets | – | 8,213 | 10,222 | 18,435 | – | 8,041 | 9,593 | 17,634 |
| International equity | 31,617 | – | 58,979 | 90,596 | 53,145 | – | 42,996 | 96,141 |
| Domestic equity | 106,777 | – | 57,801 | 164,578 | 106,689 | – | 50,323 | 157,012 |
| Hedge funds: | | | | | | | | |
| Equity Hedge | – | – | 73,076 | 73,076 | – | – | 44,479 | 44,479 |
| Event-Driven | – | – | 33,192 | 33,192 | – | – | 29,775 | 29,775 |
| Fund of Funds | – | – | 36,391 | 36,391 | – | – | 56,640 | 56,640 |
| Distressed/Restructuring | – | – | 15,347 | 15,347 | – | – | 12,236 | 12,236 |
| Private equity & non-marketable real assets | – | – | 26,799 | 26,799 | – | – | 23,280 | 23,280 |
| Funds held in trust | – | 16,215 | – | 16,215 | – | 16,192 | – | 16,192 |
| Total endowment and similar investments – campuses | $170,619 | $60,939 | $311,807 | $543,365 | $191,393 | $53,447 | $269,322 | $514,162 |
| **Endowment and similar investments – affiliated entities** | | | | | | | | |
| Money market | $ 9,408 | $ – | $ – | $ 9,408 | $ 3,303 | $ – | $ – | $ 3,303 |
| Global fixed income | 21,359 | – | 4,718 | 26,077 | 12,795 | 720 | 1,342 | 14,857 |
| Inflation hedging assets | 4,006 | 9,300 | 453 | 13,759 | 2,785 | 3,799 | 3,352 | 9,936 |
| Domestic equity | 24,193 | – | 33,573 | 57,766 | 37,240 | – | 34,635 | 71,875 |
| International equity | 12,865 | – | 39,699 | 52,564 | 15,788 | – | 29,918 | 45,706 |
| Hedge funds: | | | | | | | | |
| Diversified | – | – | 16,437 | 16,437 | – | – | 9,797 | 9,797 |
| Distressed/Restructuring | – | – | 31,089 | 31,089 | – | – | 26,075 | 26,075 |
| Equity Hedge | – | – | 15,029 | 15,029 | – | – | 21,216 | 21,216 |
| Private equity & non-marketable real assets | – | – | 15,788 | 15,788 | – | – | 13,581 | 13,581 |
| Total endowment and similar investments – affiliated entities | $ 71,831 | $ 9,300 | $156,786 | $237,917 | $ 71,911 | $ 4,519 | $139,916 | $216,346 |
| **Total endowment and similar investments** | $242,450 | $70,239 | $468,593 | $781,282 | $263,304 | $57,966 | $409,238 | $730,508 |

As of June 30, 2018, USNH had two equity hedge funds in a lock-up period set to expire in 7 months. As of June 30, 2018, UNHF had one distressed hedge fund with a lock-up period set to expire in 10 months. Hedge funds, private equity and real estate funds classified as illiquid have no ability to be redeemed. For USNH, of the 30 funds classified as illiquid, ten are currently in liquidation; two are expected to start liquidation within the next year; nine are expected to start liquidation in 2 to 15 years, and nine currently have no expected liquidation dates. For UNHF, fourteen funds are classified as illiquid and are expected to be liquidated over the next one to 13 years. One of the funds classified as illiquid can be redeemed in 3 years.

Investment liquidity for the past two years is aggregated below and on the following page based on redemption terms or availability *($ in thousands):*

| Liquidity Terms as of June 30, 2018 | Daily | Monthly | Quarterly | Semi-Annual | Annual | illiquid | Total | Redemption Notice Period |
|---|---|---|---|---|---|---|---|---|
| **Endowment and similar investments – campuses** | | | | | | | | |
| Money market | $ 14,671 | $ – | $ – | $ – | $ – | $ – | $ 14,671 | Same day |
| Global fixed income | 54,065 | – | – | – | – | – | 54,065 | Same day |
| Inflation hedging assets | 8,213 | 10,222 | – | – | – | – | 18,435 | 1-30 days |
| International equity | 45,296 | 45,300 | – | – | – | – | 90,596 | 1-30 days |
| Domestic equity | 106,777 | – | 57,801 | – | – | – | 164,578 | 1- 60 days |
| Hedge funds: | | | | | | | | |
| Equity Hedge | 24,595 | – | 23,721 | 326 | 24,434 | | 73,076 | 1-60 days, illiquid |
| Event-Driven | – | – | 18,985 | 14,146 | – | 61 | 33,192 | 60-65 days, illiquid |
| Fund of Funds | – | – | – | – | 35,930 | 461 | 36,391 | 65-91 days, illiquid |
| Distressed/Restructuring | – | – | – | – | 15,347 | – | 15,347 | 90 days |
| Private equity & non-marketable real assets | – | – | – | – | – | 26,799 | 26,799 | illiquid |
| Funds held in trust | – | – | – | – | – | 16,215 | 16,215 | illiquid |
| Total endowment and similar investments – campuses | $253,617 | $55,522 | $100,507 | $14,472 | $75,711 | $43,536 | $ 543,365 | |
| **Endowment and similar investments – affiliated entities** | | | | | | | | |
| Money market | $ 9,408 | $ – | $ – | $ – | $ – | $ – | $ 9,408 | Same day |
| Global fixed income | 22,971 | – | – | – | 1,069 | 2,037 | 26,077 | Same day, illiquid |
| Inflation hedging assets | 13,759 | – | – | – | – | – | 13,759 | 1-35 days |
| Domestic equity | 25,407 | – | 32,359 | – | – | – | 57,766 | 1-60 days |
| International equity | 13,782 | 31,282 | 7,500 | – | – | – | 52,564 | 1-90 days |
| Hedge funds: | | | | | | | | |
| Diversified | – | – | 7,786 | 3,537 | 5,114 | – | 16,437 | 45-60 days |
| Distressed/Restructuring | – | – | 19,589 | – | 11,500 | – | 31,089 | 45-90 days |
| Equity Hedge | – | – | 9,374 | 5,655 | – | – | 15,029 | 60-90 days |
| Private equity & non-marketable real assets | – | – | – | – | – | 15,788 | 15,788 | illiquid |
| Total endowment and similar investments - affiliated entities | $ 85,327 | $31,282 | $ 76,608 | $ 9,192 | $17,683 | $17,825 | $ 237,917 | |
| **Total endowment and similar investments** | $338,944 | $86,804 | $ 177,115 | $23,664 | $93,394 | $61,361 | $781,282 | |

As of June 30, 2018, USNH has two outstanding investment liquidation requests which have been limited by the respective fund managers. Management of the fund in which USNH has the largest of these balances has approved a plan to fully liquidate all balances by early 2019 with the anticipated holdback distributed by the end of 2019. USNH's balance in that fund was $369,000 and $482,000 as of June 30, 2018 and 2017, respectively. Plans have not been communicated for the remaining fund. USNH's balance in the remaining fund totaled $92,000 as of June 30, 2018. USNH's balance of $233,000 as of June 30, 2017 includes one fund that was completely liquidated during fiscal year 2018. The estimated fair values based on June 30 of the two investments at June 30, 2018 and the three investments at June 30, 2017 are $461,000 and $714,000, respectively. It is uncertain when, or if, the funds will be fully collected at the NAV recorded.

Unfunded commitments with various private equity and similar alternative investment funds totaled $30,277,000 for USNH and $23,878,000 for UNHF at June 30, 2018. This compares to $15,351,000 and $17,421,000, respectively, at June 30, 2017.

**Liquidity Terms as of June 30, 2017**

| | Daily | Monthly | Quarterly | Semi-Annual | Annual | illiquid | Total | Redemption Notice Period |
|---|---|---|---|---|---|---|---|---|
| **Endowment and similar investments – campuses** | | | | | | | | |
| Money market | $ 13,694 | $ – | $ – | $ – | $ – | $ – | $ 13,694 | Same day |
| Global fixed income | 47,079 | – | – | – | – | – | 47,079 | Same day |
| Inflation hedging assets | 8,041 | 9,593 | – | – | – | – | 17,634 | 1-30 days |
| International equity | 53,145 | 42,996 | – | – | – | – | 96,141 | 1-30 days |
| Domestic equity | 106,689 | – | 50,323 | – | – | – | 157,012 | 1-60 days |
| Hedge funds: | | | | | | | | |
| Equity Hedge | 13,974 | – | – | 6,243 | 24,137 | 125 | 44,479 | 1-60 days, illiquid |
| Event-Driven | – | – | 16,460 | 13,254 | – | 61 | 29,775 | 60-65 days, illiquid |
| Fund of Funds | – | – | 21,278 | – | 34,772 | 590 | 56,640 | 65-91 days, illiquid |
| Distressed/Restructuring | – | – | – | – | 12,236 | – | 12,236 | 90 days |
| Private equity & non-marketable real assets | – | – | – | – | – | 23,280 | 23,280 | illiquid |
| Funds held in trust | – | – | – | – | – | 16,192 | 16,192 | illiquid |
| Total endowment and similar investments – campuses | $242,622 | $52,589 | $ 88,061 | $19,497 | $71,145 | $ 40,248 | $514,162 | |
| **Endowment and similar investments – affiliated entities** | | | | | | | | |
| Money market | $ 3,303 | $ – | $ – | $ – | $ – | $ – | $ 3,303 | Same day |
| Global fixed income | 13,515 | 1,342 | – | – | – | – | 14,857 | 1-10 days |
| Inflation hedging assets | 6,584 | 3,352 | – | – | – | – | 9,936 | 1-60 days |
| Domestic equity | 38,893 | – | 32,982 | – | – | – | 71,875 | 1-60 days |
| International equity | 16,278 | 29,428 | – | – | – | – | 45,706 | 1-35 days |
| Hedge funds: | | | | | | | | |
| Diversified | – | – | – | 4,747 | 5,050 | – | 9,797 | 65-95 days |
| Distressed/Restructuring | – | – | 16,379 | – | 9,696 | – | 26,075 | 45-90 days |
| Equity Hedge | – | – | 3,189 | 7,226 | 10,801 | – | 21,216 | 45-60 days |
| Private equity & non-marketable real assets | – | – | – | – | – | 13,581 | 13,581 | illiquid |
| Total endowment and similar investments - affiliated entities | $ 78,573 | $ 34,122 | $ 52,550 | $11,973 | $25,547 | $ 13,581 | $216,346 | |
| **Total endowment and similar investments** | $ 321,195 | $86,711 | $140,611 | $31,470 | $96,692 | $ 53,829 | $730,508 | |

## 5. Property and equipment

Property and equipment activity for the years ended June 30, 2018 and 2017 is summarized as follows *($ in thousands)*:

| | | 2017 | | | 2018 | | |
|---|---|---|---|---|---|---|---|
| | Balance June 30, 2016 | Additions | Retirements & Changes | Balance June 30, 2017 | Additions | Retirements & Changes | Balance June 30, 2018 |
| Land | $ 15,780 | $ 85 | $ – | $ 15,865 | $ – | $ (277) | $ 15,588 |
| Buildings and improvements | 1,593,091 | 96,333 | (8,763) | 1,680,661 | 134,977 | (14,531) | 1,801,107 |
| Equipment | 123,087 | 12,603 | (3,075) | 132,615 | 11,153 | (5,181) | 138,587 |
| Construction in progress, net | 118,357 | 94,894 | (96,418) | 116,833 | 61,006 | (134,977) | 42,862 |
| **Total property and equipment** | 1,850,315 | 203,915 | (108,256) | 1,945,974 | 207,136 | (154,966) | 1,998,144 |
| Less: accumulated depreciation | (773,264) | (62,942) | 9,860 | (826,346) | (65,096) | 15,309 | (876,133) |
| **Property and equipment, net** | $1,077,051 | $140,973 | $(98,396) | $1,119,628 | $142,040 | $(139,657) | $1,122,011 |

Contractual obligations for major construction projects totaled approximately $35,380,000 and $26,794,000 at June 30, 2018 and 2017, respectively.

## 6. Accrued employee benefits

Accrued employee benefit obligations at June 30 are summarized below *($ in thousands)*:

| | | 2017 | | | 2018 | | | |
|---|---|---|---|---|---|---|---|---|
| | Balance June 30, 2016 | Payments to/ on Behalf of Participants | Expenses & Other Changes | Balance June 30, 2017 | Payments to/ on Behalf of Participants | Expenses & Other Changes | Balance June 30, 2018 | Current Portion |
| Additional retirement program | $ 2,953 | $ (455) | $ (175) | $ 2,323 | $ (121) | $ 92 | $ 2,294 | $ 95 |
| Employee separation incentives | 12,348 | (8,977) | 923 | 4,294 | (1,660) | 535 | 3,169 | 2,222 |
| Long-term disability | 2,617 | (571) | 320 | 2,366 | (511) | 232 | 2,087 | 511 |
| Workers' compensation | 3,901 | (1,089) | 1,388 | 4,200 | (543) | (366) | 3,291 | 543 |
| Compensated absences | 20,236 | (2,689) | 3,219 | 20,766 | (2,095) | 2,176 | 20,847 | 2,759 |
| Other benefits | 475 | – | 161 | 636 | – | 329 | 965 | 787 |
| **Total accrued employee benefits** | $42,530 | $(13,781) | $5,836 | $34,585 | $(4,930) | $2,998 | $32,653 | $6,917 |

The **Additional Retirement Contribution** program is a single employer plan administered by USNH and offered to eligible employees hired between July 1, 1994 and June 30, 2011. Under this plan, staff meeting certain voluntary defined benefit plan contribution levels receive an additional 1% of their salary contributed to their defined contribution retirement plan (see below) by USNH in lieu of postretirement medical benefits. Employees meeting certain service guidelines prior to July 1, 1994 are also eligible for a guaranteed minimum employer retirement contribution of $10,000 plus an additional $1,000 for each year of service in excess of 20 less 1% of the participant's salary account. There were 358 and 386 active employees meeting the requirements for the guaranteed minimum employer contribution as of June 30, 2018 and 2017, respectively.

The calculations for the Additional Retirement Contribution program are based on the benefits provided by the program at the time of the last biennial actuarial valuation, December 31, 2017, and were developed using the Entry Age Normal Cost Method. The discount rate used in determining the actuarial accrued liabilities was 3.44% and 3.78% for 2018 and 2017, respectively, based on Bond Buyer 20-Bond General Obligation index rate as of the measurement date. Inflation rates of 2.5% and salary increase rates of 3% were used to determine the liability along with the RP-2014 Employee Mortality Table with Scale MP-2016. USNH accrued $2,294,000 and $2,323,000 at June 30, 2018 and 2017, respectively, for the related obligations. If the discount rate were to increase by 1%, the total liability at June 30, 2018 would be $2,216,000. Similarly, if the discount rate were to decrease by 1%, the total liability at June 30, 2018 would be $2,371,000. The Additional Retirement Contribution program expense was $21,000 and $81,000 for fiscal years 2018 and 2017, respectively.

USNH had designated cash assets to fully fund the Additional Retirement Contribution obligations at June 30, 2018 and 2017. These assets are not administrated through a trust. The Additional Retirement Contribution program is not available to employees hired after June 30, 2011. Eligible employees hired after June 30, 2011 may elect to participate in USNH's defined contribution retirement plans administered by others. Retirement contributions by USNH for employees enrolled in the defined contribution plans range from 4% to 10% of eligible salaries for enrolled participants. USNH additions to the defined contribution plans totaled $27,421,000 and $26,283,000 in 2018 and 2017, respectively. Retirement contributions by plan members totaled $26,724,000 and $28,771,000 in 2018 and 2017, respectively.

Early retirement and employee separation incentive programs were provided to various faculty and staff during 2018 and 2017. Such incentives include stipends, as well as medical, educational and other termination benefits. The future costs associated with these incentive options is accrued as of the date of acceptance into the program. The liability balances of $3,169,000 and $4,294,000 at June 30, 2018 and 2017 represent obligations for 117 and 94 participants, respectively, which will be remitted in fiscal years 2019 through 2024.

USNH sponsors other benefit programs for its employees, including long-term disability, workers' compensation, and compensated absences. Long-term disability payments are provided through an independent insurer. The associated medical benefits are accrued and paid by USNH until age 65, at which point the postretirement medical plan takes over, if applicable. Workers' compensation accruals include amounts for medical costs and annual stipends. A small number of chronic workers' compensation cases will require stipends and regular employee medical benefits for life. Coverage for such claims is provided through an independent insurer. USNH also accrues amounts for compensated absences as earned. These accrued balances at June 30 represent vacation and earned time amounts payable to employees upon termination of employment.

USNH is self-insured for a portion of certain risks, including workers' compensation, employee long-term disability, and certain student health insurance claims. Most employee and retiree medical and dental coverage provided by USNH is also self-insured. The costs of self-insured medical and dental claims and administrative fees totaled $66,507,000 and $56,649,000 for fiscal year 2018 and 2017, respectively. These amounts include $8,059,000 and $5,572,000 for estimated claims incurred but not reported as of June 30, 2018 and 2017, respectively. In conjunction with the primary medical plan offering for active employees, USNH purchases stop-loss coverage which limits the USNH cost of claims to $500,000 per participant in most cases. The liabilities recorded in the financial statements for all USNH self-insured programs are developed by third party claim administrators and based on historical claims data. Management reviewed the calculations for reasonableness and believes the liabilities are sufficient to cover the actual claims incurred.

In addition to the benefits accruals included above, USNH created and fully funded a trust to hold assets set aside for its **Operating Staff Retirement Plan** on June 29, 2017. The related asset and liability values are not included in the financial statements as required by the related accounting standards. The related investment balances as of June 30, 2018 and 2017 are summarized below *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| Cash and equivalents | $ 311 | $6,700 |
| Fixed income | 2,779 | – |
| Equities | 3,200 | – |
| Real assets | 86 | – |
| **Total including accrued income** | $6,376 | $6,700 |

The plan has been closed to new participants since 1987. At June 30, 2018 there were approximately 184 current annuitants and 32 participants with deferred benefits, all fully vested. This compares to 190 current annuitants and 35 participants with deferred benefits as of June 30, 2017. The determination of total pension liabilities for this program was based on actuarial calculations completed by the plan trustee as of June 30, 2018 and 2017.

The calculations were developed using the Entry Age Normal Cost Method and the RP-2014 employee mortality tables. The 2018 valuation used Scale MP-2017, and Scale MP-2016 was used for the 2017 calculation. The discount rate used was 5.5% in both years based on the long term expected rate of return on the related investments. The plan fiduciary net position was $6,376,000 as of June 30, 2018 and $6,700,000 as of June 30, 2017 which resulted in the recording of a net pension asset of $724,000 and $993,000 for fiscal years 2018 and 2017, respectively. The actuarially-determined liability for the program was $5,652,000 as of June 30, 2018 and $5,707,000 as of June 30, 2017. If the discount rate were to increase by 1%, the net pension asset at June 30, 2018 would be $1,114,000. Similarly, if the discount rate were to decrease by 1%, the net pension asset at June 30, 2018 would be $275,000. The plan expense was $37,000 and $317,000 for fiscal years 2018 and 2017, respectively.

## 7. Postretirement medical benefits

The primary defined benefit postretirement medical plan has two components. The first offering known as the Medicare Complementary Plan (MCP), was optional for full-time status employees hired before July 1, 1994 and not offered to new employees after that date. At January 1, 2018 and 2017, respectively, there were 777 and 798 former employees receiving benefits under this program along with their eligible dependents. As of January 1, 2018 and 2017 there were 179 and 202 active employees, respectively, who along with their dependents, may eventually be eligible to receive benefits under this program. The MCP provides limited medical coverage for the remaining life of the participants. There are no costs to participate in the plan, but retirees must pay a portion of the actual costs of services rendered.

Employees hired on July 1, 1994 or later are eligible for the current offering which provides bridge coverage only for retirees aged 62-65. Retired employees must have reached age 62, completed at least 10 years of benefits eligible service, participated in the active retirement plans during their last 10 years of benefits-eligible service, and participated in USNH's active medical plan at the time of retirement in order to be eligible for the plan. Retirees contribute to the plan at then-current employee medical rates during the bridge period. As of January 1, 2018 and 2017, respectively, there were 97 and 125 retirees receiving benefits under this program along with their dependents. As of January 1, 2018 and 2017, respectively, there were also 3,638 and 3,687 active employees who, along with their dependents, may eventually be eligible to receive benefits under this program. The primary postretirement medical plan holds no assets. Together, the above offerings constitute the primary postretirement medical plan. This is a single-employer plan and funded on a pay-as-you-go basis with benefits paid when due.

Third-party actuaries are used to determine the postretirement benefit obligation and annual expense amounts. Actuarial calculations reflect a long-term perspective. Such calculations involve estimates and, by definition, are subject to revision. The healthcare cost trend and discount rate assumptions have a significant effect on the amounts reported. For measurement purposes the 2017 initial rate of increase in the cost of healthcare services was assumed to be 7.0% for participants, decreasing 0.5% each year thereafter until reaching an ultimate rate of 4.5% per year. The initial increase in the cost of prescriptions was assumed to be 10.0% for 2017, decreasing by 0.5% each year thereafter to an ultimate rate of 4.5% per year. The discount rate used in determining the actuarial accrued liability was 2.5% for 2017 and the actuarially determined postretirement benefit expense for the plan was $7,516,000. The June 30, 2017 obligation was calculated using the Projected Unit Credit Cost Method and measured as of December 31, 2016. USNH accrued $56,166,000 for obligations of the plan as of June 30, 2017.

Total annual postretirement medical costs for the primary postretirement medical plan for the year ended June 30, 2017, and the liability as of June 30, 2017 included the following components ($ in thousands *($ in thousands):*

| **Other Post-Employment Benefits (OPEB)** | **2017** |
|---|---|
| Annual required contribution | $ 13,886 |
| Interest on net OPEB obligation | 1,383 |
| Adjustment on annual required contribution | (8,417) |
| **Annual OPEB cost** | 6,852 |
| Claims paid | (6,018) |
| **Increase in net OPEB obligation** | 834 |
| **Net OPEB obligation at beginning of year** | $ 55,332 |
| **Net OPEB obligation at end of year** | $ 56,166 |
| **Current Portion** | $ 6,018 |

USNH adopted GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* for its June 30, 2018 financial statements. Fiscal year 2017 balances and activities were not restated to reflect this adoption as allowed under the standard. For measurement purposes the 2018 initial rate of increase in the cost of healthcare services was assumed to be 6.5% for participants, decreasing 0.5% each year for four years thereafter until reaching an ultimate rate of 4.5% per year. The initial increase in the cost of prescriptions was assumed to be 9.5% for 2018, decreasing 0.5% each year for ten years thereafter until reaching an ultimate rate of 4.5% per year. Salary increases of 3% were included in the calculations for fiscal year 2018. The determination of the 2018 postemployment medical liability was based on the last biennial actuarial valuation calculation measured as of December 31, 2017. The calculation was developed using the Entry Age Normal Cost Method and the RP-2014 employee mortality tables with Scale MP-2016. As required under the new standard, a single discount rate of 3.44% was used based on the Bond Buyer 20-Bond General Obligation index rate on the measurement date. USNH accrued $89,710,000 for obligations of the plan as of June 30, 2018 that included the following components *($ in thousands)*:

| | **2018** |
|---|---|
| Service costs | $ 1,416 |
| Interest | 3 ,627 |
| Benefit payments | (6,923) |
| Differences between expected and actual experience | (1,511) |
| Changes in assumptions | (4,857) |
| **Net Change in Postretirement Medical Plan liability** | (8,248) |
| **Total Postretirement Medical Plan liability - beginning of year** | 97,958 |
| **Total Postretirement Medical Plan liability - end of year** | $89,710 |
| **Current portion** | $ 5,837 |

The actuarially determined postretirement medical expense for the plan for year ended June 30, 2018 included the following components *($ in thousands)*:

| | **2018** |
|---|---|
| Service costs | $1,416 |
| Interest | 3,627 |
| Plan changes | – |
| Recognized portion of difference between expected and actual experience | (160) |
| Recognized portion of assumption changes | (514) |
| **Total OPEB Expense** | $4,369 |

The following presents the sensitivity of the postretirement medical plan liability to changes in the discount rate and healthcare cost trend rates *($ in thousands)*:

| OPEB Liability as of December 31, 2017 | Sensitivity to change in discount rate | | | Sensitivity to change in health care costs | | |
|---|---|---|---|---|---|---|
| | 1% increase | Current rate | 1% decrease | 1% increase | Current rate | 1% decrease |
| | $82,053 | $89,710 | $98,649 | $98,193 | $89,710 | $82,302 |

USNH also accrued $102,000 as of June 30, 2018 and 2017, for potential obligations related to postretirement care of certain USNH police personnel. The USNH Board of Trustees holds the authority to change these benefit plans at any time. Further information on the Additional Retirement Contribution, Operating Staff Retirement Plan, and Postretirement Medical Plan can be found in the required supplemental information on page 50 of the publication.

## 8. Long-term debt

USNH long-term debt activity, exclusive of deferred losses or gains on refunding, for the years ended June 30, 2018 and 2017 is summarized below *($ in thousands)*:

| | | 2017 | | | 2018 | | | |
|---|---|---|---|---|---|---|---|---|
| | Balance June 30, 2016 | Additions & Other Changes | Retirements | Balance June 30, 2017 | Additions & Other Changes | Retirements | Balance June 30, 2018 | Current Portion |
| **NHHEFA bonds** | | | | | | | | |
| Series 2005A | $ 51,750 | $ – | $ (1,650) | $ 50,100 | $ – | $ (1,900) | $ 48,200 | $ 1,950 |
| Series 2005B | 77,700 | – | (4,295) | 73,405 | – | (4,450) | 68,955 | 4,595 |
| Series 2006B-2 | 1,500 | – | (1,500) | – | – | – | – | – |
| Series 2007 | 46,570 | – | – | 46,570 | – | (46,570) | – | – |
| Series 2009A | 59,045 | – | – | 59,045 | – | (59,045) | – | – |
| Series 2011A | 6,000 | – | – | 6,000 | – | – | 6,000 | – |
| Series 2011B | 36,030 | – | (1,830) | 34,200 | – | (1,925) | 32,275 | 2,015 |
| Series 2012 | 15,265 | – | (2,815) | 12,450 | – | (2,930) | 9,520 | 3,050 |
| Series 2014 | 19,805 | – | (2,030) | 17,775 | – | (2,070) | 15,705 | 2,110 |
| Series 2015 | 116,970 | – | (1,100) | 115,870 | – | (2,610) | 113,260 | 2,730 |
| Series 2016 | 53,890 | – | – | 53,890 | – | (1,675) | 52,215 | 2,390 |
| Series 2017A | – | – | – | – | 53,805 | – | 53,805 | – |
| Series 2017B | – | – | – | – | 49,020 | – | 49,020 | 1,100 |
| Unamortized discounts/premiums, net | 23,700 | – | (1,450) | 22,250 | 10,085 | (2,016) | 30,319 | 1,915 |
| **Capital leases** | 10,774 | 149 | (1,013) | 9,910 | 71 | (1,068) | 8,913 | 1,113 |
| **Total bonds and leases** | $518,999 | $149 | $(17,683) | $501,465 | $112,981 | $(126,259) | $488,187 | $22,968 |

**New Hampshire Health and Education Facilities Authority (NHHEFA) Bonds**

NHHEFA is a public body corporate and an agency of the State of New Hampshire whose primary purpose is to assist New Hampshire not-for-profit educational and health care institutions in the construction and financing (or refinancing) of related facilities. NHHEFA achieves this purpose primarily through the issuance of bonds. Since 1989 all USNH bonds have been issued through NHHEFA. None of USNH's NHHEFA bonds provide for a lien or mortgage on any property. USNH is obligated under the terms of the NHHEFA bonds to make payments from revenues received from certain housing, dining, student union, recreational, and other related revenue generating facilities financed by the bonds. The state is not liable for the payment of principal or interest on the NHHEFA bonds, nor is the state directly, indirectly or contingently obligated to levy or pledge any form of taxation whatsoever or to make any appropriation for their payment. Management believes USNH is in compliance with all covenants specified in the NHHEFA bond agreements, the most restrictive of which is maintenance of a debt-service coverage ratio, as defined, of at least 1.0 to 1.0.

USNH's bond portfolio at June 30, 2018 consisted of fixed rate and variable rate issues. The variable rate demand bonds (Series 2005A, 2005B, 2011B) are fully hedged via interest rate swap agreements (see Note 9 below), with all three issues supported by standby bond purchase agreements as of June 30, 2018 and 2017. The variable interest rates for the Series 2005A and 2005B Bonds at June 30, 2018 and 2017 were 1.56% and 0.92%, respectively. The 2011B Bonds variable interest rates at June 30, 2018 and 2017 were 1.57% and 0.92%, respectively.

USNH issued two Series 2017 Bonds during the year ended June 30, 2018. The Series 2017A Bonds were issued in the amount of $53,805,000 to advance refund and defease the Series 2009A Bonds ($59,045,000), while the Series 2017B Bonds were issued in the amount of $49,020,000 as a current refund of the Series 2007 Bonds ($46,570,000).

Construction proceeds of $4,239,000 and $10,718,000 were unspent as of June 30, 2018 and June 30, 2017, respectively, and held in reserve in accordance with the related debt agreements. The related investments are classified in Level 1 of the GASB fair value hierarchy because the underlying securities held by the bond trustee are valued based on quoted market prices. The Series 2009A refunding proceeds of $62,019,000 were held in escrow in the principal payment investment account on June 30, 2018.

Maturity dates and interest terms of outstanding debt issues are summarized below:

| NHHEFA Bonds | Maturity Date | Interest Terms and Rates |
|---|---|---|
| Series 2005A | 7/1/2035 | Variable with daily pricing |
| Series 2005B | 7/1/2033 | Variable with daily pricing |
| Series 2011A | 7/1/2021 | Fixed at 5.0% |
| Series 2011B | 7/1/2033 | Variable with daily pricing |
| Series 2012 | 7/1/2020 | Fixed at 1.7% |
| Series 2014 | 7/1/2024 | Fixed at 2.0% |
| Series 2015 | 7/1/2045 | Fixed at 3.8% |
| Series 2016 | 7/1/2046 | Fixed at 2.7% |
| Series 2017A | 7/1/2037 | Fixed at 3.2% |
| Series 2017B | 7/1/2037 | Fixed at 3.4% |

**Capital leases**

On April 30, 2004, USNH entered into a capital lease agreement in the amount of $18,292,000 to finance a portion of the costs of equipment housed in UNH's utility cogeneration facility. The related lease payments are due quarterly through June 2025, including principal as well as interest at a fixed rate of 4.5%. The carrying value of the related equipment was $8,913,000 and $9,910,000 as of June 30, 2018 and 2017, respectively.

**State of NH general obligation bonds**

The state, through acts of its legislature, provides funding for certain major plant facilities on USNH campuses. The state obtains its funds for these construction projects from general obligation bonds, which it issues from time to time. Debt service is funded by the general fund of the state, which is in the custody of the State Treasurer. The state is responsible for all repayments of these bonds in accordance with bond indentures. USNH facilities are not pledged as collateral for these bonds and creditors have no recourse to USNH. Accordingly, the state's debt obligation attributable to USNH's educational and general facilities is not reported as debt of USNH. As construction expenditures are incurred by USNH on state-funded educational and general facilities, amounts are billed to the state and recorded as State of New Hampshire capital appropriations.

**Maturity of Long-term Debt Obligations**

USNH Long-term debt obligations are scheduled to mature as follows using the associated fixed, estimated synthetic fixed, and expected variable rates in effect as of June 30, 2018 over the remaining terms of the individual issuances *($ in thousands):*

| Fiscal Year | Principal | Interest | Total |
|---|---|---|---|
| 2019 | $ 21,053 | $ 16,581 | $ 37,634 |
| 2020 | 24,288 | 17,487 | 41,775 |
| 2021 | 25,400 | 16,772 | 42,172 |
| 2022 | 28,760 | 15,698 | 44,458 |
| 2023 | 23,902 | 14,737 | 38,639 |
| 2024-2028 | 106,690 | 60,144 | 166,834 |
| 2029-2033 | 100,250 | 40,396 | 140,646 |
| 2034-2038 | 83,695 | 19,640 | 103,335 |
| 2039-2043 | 24,550 | 7,592 | 32,142 |
| 2044-2047 | 19,280 | 1,816 | 21,096 |
| Plus: unamortized discounts/premiums, net | 30,319 | – | 30,319 |
| **Total** | $488,187 | $210,863 | $699,050 |

## 9. Derivative instruments – interest rate swaps

USNH uses hedging derivatives to artificially fix interest rates on variable rate bonds outstanding. The terms and fair market value of swap contracts in place as of June 30, 2018 and 2017 were as follows *($ in thousands):*

| | Effective Date | Termination Date | Payable Fixed Swap Rate | Receivable Variable Swap Rate | Notional Amount at June 30, 2018 | Notional Amount at June 30, 2017 | Swap Fair Value at June 30, 2018 | Swap Fair Value at June 30, 2017 |
|---|---|---|---|---|---|---|---|---|
| Series 2005A swap | October 29, 2008 | July 1, 2035 | 3.6% | 67% LIBOR | $ 48,200 | $ 50,100 | $ (7,165) | $ (9,775) |
| Series 2005B swap | August 1, 2005 | July 1, 2033 | 3.1% | 63% LIBOR+0.29% | 68,955 | 73,405 | (5,357) | (8,256) |
| Series 2011B swap | April 4, 2011 | July 1, 2033 | 4.5% | 67% LIBOR | 32,275 | 34,200 | (5,772) | (7,728) |
| | | | | **Total** | $149,430 | $157,705 | $ (18,294) | $(25,759) |

USNH utilizes interest rate swap agreements with counterparties to effectively convert its variable rate debt to fixed rates. The swaps' fair values and changes therein are recognized in USNH's financial statements. Differences between the fixed and variable rates in effect at each interest due date are settled net under each swap, increasing or decreasing interest expense. The fair value of the swap instruments considers the estimated benefit or cost to the USNH to cancel the agreements as of the reporting dates, and is based on option pricing models that consider interest rates and other market factors, as well as the credit risks of the parties to the agreements. Interest rate volatility, remaining outstanding principal, and time to maturity will affect the swaps' fair values at subsequent reporting dates. The values were estimated using the zero-coupon discounting method. This method calculates the future payments required by the swap, assuming that the current forward rates implied by the yield curve are the market's best estimate of future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for a hypothetical zero-coupon rate bond due on the date of each future net settlement payment. Because the swap fair values are based predominantly on observable inputs corroborated by market data, they are classified in Level 2 of the GASB fair value hierarchy. USNH intends to hold all swap contracts to maturity.

These derivative instruments meet the criteria established by GASB Statement No. 53 for effective hedges as of June 30, 2018 and 2017 and, therefore, their accumulated changes in fair value are reflected as deferrals on the Statements of Net Position (see Note 10). The notional amount of each swap is tied to the outstanding balance of the related bonds throughout the life of the swap. Under the terms of each swap, USNH makes fixed rate interest payments to the counterparty and receives a variable rate payment from the counterparty. USNH makes variable rate payments to bondholders on the related bonds. None of the derivatives require collateralization by USNH at any level of negative fair market value.

### Risk Disclosure

**Counterparty Risk** – This is the risk that the counterparty will fail to perform under the terms of the swap agreement. As of June 30, 2018, USNH was exposed to no counterparty credit risk relative to its swaps as all swap market values were negative. The swaps require collateralization of any positive fair value of the swap should the counterparty's credit rating fall below thresholds identified in the swap contracts. USNH mitigates counterparty risk by spreading the swap exposure among various counterparties, by monitoring bond ratings continuously, and by requiring collateralization in certain circumstances.

**Basis Risk** – This is the risk of a mismatch between the variable rate received from the swap counterparty and the variable rate paid by USNH to bondholders on the underlying variable rate debt. The effective rate on the debt will vary depending on the magnitude and duration of any basis risk shortfall or surplus. Based on current and historical experience, USNH's financial advisors expect payments received under the agreements to approximate the related bond payments over the life of the swaps. USNH manages basis risk by closely monitoring daily and monthly rates paid and received on each transaction, by diversifying bond remarketing agents, and by varying swap terms (e.g., 67% of LIBOR vs. 63% of LIBOR + 29 bps).

**Termination Risk** – This is the risk that the swaps could be terminated as a result of any of several events, which may include rating downgrades below specified levels for USNH or the swap counterparty; covenant violation; swap payment default or bankruptcy by either party; or default events under a bond resolution or trust indenture. Under the terms of each agreement, USNH has the option to terminate a swap at the fair market value at any time by providing notice to the counterparty, while the counterparty may only terminate the swap upon certain termination events. USNH manages termination risk by adhering to bond covenant requirements, employing strategic indicator targets to maintain financial strength, monitoring swap market values and counterparty credit ratings, and diversifying swap counterparties. Effective interest rates and other key terms of each derivative are described below:

| | Counterparty's Most Recent Credit Rating | Variable Interest Rates Paid and Received: Interest Rate Paid by USNH to Bondholders as of 6/30/2018 | Interest Rate Paid by USNH to Bondholders as of 6/30/2017 | Interest Rate Received by USNH from Swap Counterparties as of 6/30/2018 | Interest Rate Received by USNH from Swap Counterparties as of 6/30/2017 | Inception-To-Date: Effective Interest Rate Through 6/30/2018 | Effective Interest Rate Through 6/30/2017 | All-in Synthetically Fixed Interest Rate |
|---|---|---|---|---|---|---|---|---|
| Series 2005A swap | Aa2/AA- | 1.6% | 0.9% | 1.3% | 0.7% | 4.3% | 4.2% | 4.1% |
| Series 2005B swap | A1/A+ | 1.6% | 0.9% | 1.5% | 1.0% | 3.6% | 3.4% | 3.6% |
| Series 2011B swap | A3/BBB+ | 1.6% | 0.9% | 1.3% | 0.7% | 5.2% | 5.1% | 4.9% |

## Swap Cash Flows

Actual interest payments on the swaps vary as market rates vary. The table below shows estimated annual future cash flows of the derivative instruments if interest rates remain unchanged from June 30, 2018 through the end of each swap contract *($ in thousands)*:

| Fiscal Year | Notional Bonds Amortization | Estimated Interest Received | Estimated Interest and Fees Paid | Estimated Swap Net Outflows |
|---|---|---|---|---|
| 2019 | $ *8,560* | $ (2,009) | $ 5,028 | $ 3,019 |
| 2020 | *8,720* | (1,883) | 4,718 | 2,835 |
| 2021 | *9,215* | (1,750) | 4,390 | 2,640 |
| 2022 | *9,385* | (1,614) | 4,056 | 2,442 |
| 2023 | *9,975* | (1,471) | 3,701 | 2,230 |
| 2024-2028 | *43,275* | (5,374) | 13,591 | 8,217 |
| 2029-2033 | *43,415* | (2,449) | 6,254 | 3,805 |
| 2034-2036 | *16,885* | (144) | 388 | 244 |
| **Total** | *$149,430* | $(16,694) | $42,126 | $25,432 |

## 10. Deferred inflows and outflows of resources

The components of Deferred Inflows and Outflows of Resources as of June 30, 2018 and 2017 were as follows *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| **Deferred Outflows of Resources** | | |
| Accumulated decrease in fair value of hedging derivatives | $18,294 | $25,759 |
| Accounting loss on debt refinancing | 9,770 | 7,308 |
| Changes of assumptions: | | |
| Operating Staff Retirement Plan | 179 | – |
| Additional Retirement Contribution Program | 22 | – |
| Net difference between projected and actual earnings: | | |
| Operating Staff Retirement Plan | 74 | – |
| Benefit payments subsequent to the measurement date: | | |
| Postretirement Medical Plan | 3,097 | – |
| **Total Deferred Outflows of Resources** | $31,436 | $33,067 |
| **Deferred Inflows of Resources** | | |
| Accounting gain on debt financing | $ 616 | $ 1,508 |
| Annuities unconditional remainder interest | 1,753 | 1,302 |
| Changes of assumptions: | | |
| Postretirement Medical Plan | 4,343 | – |
| Additional Retirement Contribution Program | 4 | 5 |
| Difference between expected and actual experience: | | |
| Operating Staff Retirement Plan | 4 | – |
| Postretirement Medical Plan | 1,351 | – |
| Additional Retirement Contribution Program | 629 | 693 |
| **Total Deferred Inflows of Resources** | $ 8,700 | $ 3,508 |

The accumulated decrease in fair value of hedging derivatives is recorded to offset the value of USNH's interest-rate swap liabilities which qualify for treatment as an effective hedge based on historic interest flows. USNH does not currently expect to terminate any of the swap agreements. The accounting gain on debt refinancing relates to the Series 2005B, 2011B, and 2015 bond issuances while the accounting loss on debt refinancing relates to the Series 2009A, 2012 and 2016 bond issuances. These costs will be amortized as a component of interest expense over the remaining terms of the new debt.

Amounts reported as deferred outflows and inflows of resources which are related to retirement programs will be recognized as a component of pension and OPEB expense over the next nine years as summarized below *($ in thousands):*

| Fiscal Year | Operating Staff Retirement Plan | Additional Retirement Contribution Program | Post-retirement Medical Plan |
|---|---|---|---|
| 2019 | $ 78 | $ (150) | $ (674) |
| 2020 | 78 | (150) | (674) |
| 2021 | 76 | (150) | (674) |
| 2022 | 17 | (150) | (674) |
| 2023 | – | (11) | (674) |
| 2024 | – | – | (674) |
| 2025 | – | – | (674) |
| 2026 | – | – | (674) |
| 2027 | – | – | (302) |
| **Total** | **$ 249** | **$ (611)** | **$(5,694)** |

## 11. Pass-through grants

USNH distributed $173,918,000 and $176,765,000 of student loans through the US Department of Education Federal Direct Lending program during 2018 and 2017, respectively. These distributions and related funding sources are not included as expenses and revenues, or cash disbursements and cash receipts, in the accompanying financial statements. The Statements of Net Position include receivables of $260,000 and $192,000 as of June 30, 2018 and 2017, respectively, for direct loans disbursed in excess of US Department of Education receipts.

## 12. Endowment return used for operations

The objective of the annual spending formula for endowment return used for operations is to provide sustainable continued future support for ongoing programs at current levels assuming moderate inflation. To the extent that endowment yield is insufficient in any one year to meet the required spending distribution, accumulated net gains are utilized to fund the distribution. For the USNH pool, the distribution rate is established annually by the USNH Board of Trustees. The rate was 4.7% for 2018 and 2017 calculated as a percentage of the pool market value per unit as of December 31, 2016 and December 31, 2015. For the UNHF primary pool, the distribution rate was 5.2% for 2018 and 2017 calculated as a percentage of the average market value per unit for the previous twelve quarters. Starting in fiscal year 2019, the USNH pool will also calculate distribution as a percentage of the average market value per unit for the previous twelve quarters.

The components of endowment return used for operations for 2018 and 2017 are summarized below *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| Pooled endowment yield - campuses | $ 6,598 | $ 6,252 |
| Pooled endowment yield - affiliates | 1,861 | 983 |
| Trusts, life income and annuities yield, net of gains utilized | 1,148 | 625 |
| Gains utilized to fund distribution - pooled campuses | 9,070 | 9,182 |
| Gains utilized to fund distribution - pooled affiliates | 9,315 | 9,779 |
| **Endowment return used for operations** | $27,992 | $26,821 |

## 13. Operating expenses by function

The following tables summarize USNH's operating expenses by functional classification for the past two years *($ in thousands)*:

| | Compensation | Supplies & Services | Utilities | Internal Allocations | Depreciation | 2018 Total |
|---|---|---|---|---|---|---|
| **Campuses – current funds** | | | | | | |
| Instruction | $203,210 | $ 23,500 | $ 17 | $ – | $ – | $ 226,727 |
| Auxiliary services | 53,940 | 53,695 | 3,406 | 45,921 | – | 156,962 |
| Research and sponsored programs | 74,705 | 35,432 | 18 | – | – | 110,155 |
| Academic support | 69,334 | 21,075 | 40 | 245 | – | 90,694 |
| Student services | 34,337 | 14,634 | 10 | (95) | – | 48,886 |
| Institutional support | 47,826 | 17,221 | 76 | (22,217) | – | 42,906 |
| Operations and maintenance | 23,175 | 16,602 | 15,482 | (24,148) | – | 31,111 |
| Fundraising and communications | 12,285 | 6,925 | – | 2,257 | – | 21,467 |
| Public service | 8,730 | 1,854 | – | – | – | 10,584 |
| Subtotal – current funds | 527,542 | 190,938 | 19,049 | 1,963 | – | 739,492 |
| **Campuses - other funds** | 155 | 16,494 | 16 | – | 65,096 | 81,761 |
| **Affiliated entities** | 5,021 | 867 | – | (1,963) | – | 3,925 |
| **Total** | $532,718 | $208,299 | $19,065 | $ – | $65,096 | $825,178 |

| | Compensation | Supplies & Services | Utilities | Internal Allocations | Depreciation | 2017 Total |
|---|---|---|---|---|---|---|
| **Campuses – current funds** | | | | | | |
| Instruction | $199,519 | $ 24,157 | $ 7 | $ – | $ – | $ 223,683 |
| Auxiliary services | 53,716 | 54,499 | 3,029 | 47,234 | – | 158,478 |
| Research and sponsored programs | 71,605 | 34,865 | 137 | – | – | 106,607 |
| Academic support | 68,313 | 21,108 | 37 | 247 | – | 89,705 |
| Student services | 31,692 | 14,503 | 11 | (74) | – | 46,132 |
| Institutional support | 47,153 | 17,482 | 68 | (21,114) | – | 43,589 |
| Operations and maintenance | 23,939 | 17,664 | 14,499 | (26,247) | – | 29,855 |
| Fundraising and communications | 12,813 | 7,258 | – | 3,247 | – | 23,318 |
| Public service | 7,487 | 1,821 | – | – | – | 9,308 |
| Subtotal – current funds | 516,237 | 193,357 | 17,788 | 3,293 | – | 730,675 |
| **Campuses - other funds** | (484) | 15,567 | 161 | (450) | 62,942 | 77,736 |
| **Affiliated entities** | 4,943 | 929 | – | (2,843) | – | 3,029 |
| **Total** | $520,696 | $209,853 | $17,949 | $ – | $62,942 | $811,440 |

## 14. Net position

The table below details USNH's net position as of June 30, 2018 and 2017 *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| **Net investment in capital assets** | $ 665,194 | $ 650,968 |
| **Restricted financial resources** | | |
| **Nonexpendable** | | |
| Historic gift value of endowment - campuses | 118,298 | 114,876 |
| Historic gift value of endowment - affiliated entities(1) | 145,671 | 155,213 |
| **Total restricted nonexpendable resources** | 263,969 | 270,089 |
| | | |
| **Expendable** | | |
| Held by campuses: | | |
| Accumulated net gains on endowment | 54,375 | 50,919 |
| Fair value of restricted funds functioning as endowment | 14,761 | 14,060 |
| Gifts, grants and contracts | 44,467 | 43,213 |
| Life income and annuity funds | 12 | 8 |
| Loan funds | 5,158 | 6,868 |
| Held by affiliated entities: | | |
| Accumulated net gains on endowment | 42,424 | 35,507 |
| Fair value of restricted funds functioning as endowment(1) | 44,108 | 20,288 |
| Other | 11,034 | 12,677 |
| **Total restricted expendable resources** | 216,339 | 183,540 |
| | | |
| **Unrestricted financial resources** | | |
| Held by campuses: | | |
| Education and general reserves | 20,998 | 35,913 |
| Auxiliary enterprises | 42,838 | 42,320 |
| Internally designated reserves | 13,003 | 10,841 |
| Unrestricted loan funds | 1,513 | 1,495 |
| Unexpended plant funds | 127,776 | 127,057 |
| Fair value of unrestricted funds functioning as endowment | 184,148 | 163,253 |
| Other | 971 | 993 |
| Less: postretirement medical liability(2) | (92,307) | (56,166) |
| Held by affiliated entities: | | |
| Fair value of unrestricted funds functioning as endowment | 1,314 | 1,280 |
| Other | 1,900 | 1,933 |
| **Total unrestricted financial resources** | 302,154 | 328,919 |
| **Total Net Position** | $1,447,656 | $1,433,516 |

(1) *During 2018 a prominent donor requested that the UNH Foundation remove the restriction on funds previously endowed which totaled $16,797,000, and move them into a new restricted quasi-endowment fund held by UNHF.*

(2) *As discussed in Note 7, the 2018 postretirement medical liability is shown net of the related deferred inflows and outflows of resources. See Note 10 for additional information in this regard.*

## 15. Commitments and contingencies

USNH holds insurance for losses related to real property, as well as professional, environmental and general liability claims. Property coverage is limited to $500 million in the aggregate with varying deductible levels. Liability coverage and deductible levels are based on management's assessments of the risks of related losses. Settlements below the relevant deductible amounts are funded from unrestricted net position.

USNH makes expenditures in connection with restricted government grants and contracts, which are subject to final audit by government agencies. Management is of the opinion that the amount of disallowances, if any, sustained through such audits would not materially affect the financial position, results of operations, or cash flows of USNH.

USNH is a defendant in various legal actions arising out of the normal course of its operations. Although the final outcome of such actions cannot presently be determined, management is of the opinion that the eventual liability, if any, will not have a material effect on USNH's financial position, results of operations or cash flows.

## 16. Component units

Condensed information from the audited financial statements of the University of New Hampshire Foundation, Inc. (UNHF) is presented below *($ in millions)*:

| | 2018 | 2017 |
|---|---|---|
| **Condensed information from the Statements of Net Position as of June 30,** | | |
| Endowment investments | $229 | $208 |
| Other assets | 14 | 17 |
| **Total Assets** | 243 | 225 |
| Annuities payable | 2 | 2 |
| Other liabilities and deferred inflows of resources | 3 | 4 |
| **Total Liabilities and Deferred Inflows of Resources** | 5 | 6 |
| **Total Net Position** | $238 | $219 |

| | 2018 | 2017 |
|---|---|---|
| **Condensed information from the Statements of Revenues, Expenses and Changes in Net Position for the years ended June 30,** | | |
| Gifts and other support | $ 35 | $ 23 |
| Investment income | 16 | 25 |
| **Total Revenues** | 51 | 48 |
| Distributions to UNH | 25 | 22 |
| Administrative and other expenses | 7 | 8 |
| **Total Expenses** | 32 | 30 |
| **Increase in Net Position** | $ 19 | $ 18 |

| | 2018 | 2017 |
|---|---|---|
| **Condensed information from the Statements of Cash Flows for the years ended June 30,** | | |
| Receipts from gifts and other sources | $ 21 | $ 20 |
| Payments to UNH and suppliers | (34) | (27) |
| **Net Cash Used in Operating Activities** | (13) | (7) |
| Net Cash (Used in) Provided by Investing Activities | (4) | 5 |
| Net Cash Provided by Noncapital Financing Activities | 15 | 5 |
| **Change in Cash and Equivalents** | $ (2) | $ 3 |

A copy of the complete financial statements for UNHF can be obtained on their website at https://www.unh.edu/give/financial-reports or by contacting the Advancement Finance and Administration Office at (603) 862-1584.

## 17. Subsequent events

Management has evaluated the impact of subsequent events through the date that the financial statements were available for issuance, and concluded that no material events have occurred which would require recognition or disclosure.

## Additional Retirement Contribution (ARC) Program

Schedule of Changes in Total Liability for the year ended June 30, *($ in thousands)*:

| | 2018 | 2017 |
|---|---|---|
| Service costs | $ 41 | $ 103 |
| Interest | 88 | 118 |
| Benefit payments [1] | (95) | (518) |
| Differences between expected and actual experience | (89) | (328) |
| Changes in assumptions | 26 | (5) |
| **Net Change in ARC liability** | (29) | (630) |
| Total ARC liability at beginning of year | 2,323 | 2,953 |
| **Total ARC liability at end of year** | $ 2,294 | $ 2,323 |
| Current portion | $ 95 | $ 455 |
| Covered payroll | $26,646 | $29,409 |
| Total Liability as percentage of covered payroll | 8.6% | 7.9% |

## Postretirement Medical Plan

Schedule of Changes in Total Liability for the year ended June 30, *($ in thousands)*:

| | 2018 [2] |
|---|---|
| Service costs | $ 1,416 |
| Interest | 3,627 |
| Benefit payments | (6,923) |
| Differences between expected and actual experience | (1,511) |
| Change in assumptions | (4,857) |
| **Net Change in Postretirement Medical Plan liability** | (8,248) |
| Total Postretiremnet Medical Plan liability-beginning of year | 97,958 |
| **Total Postretirement Medical Plan liability-end of year** | $ 89,710 |
| Current portion | $ 5,837 |
| Covered payroll | $290,107 |
| Total liability as a percentage of covered payroll | 30.9% |

## Operating Staff Retirement Plan

Schedules of Changes in Total Pension Liability for the year ended June 30, *($ in thousands)*:

| | 2018 | 2017 [3] |
|---|---|---|
| **Plan Fiduciary Net Position** | | |
| **Beginning balance** | $6,700 | $ – |
| Employer contributions | – | 6,700 |
| Plan administrative costs | (13) | – |
| Net investment income | 274 | – |
| Benefit payments | (585) | – |
| Fiduciary net position | $ 6,376 | $ 6,700 |
| **Total Pension Liability** | (5,652) | (5,707) |
| **Net Pension Asset** | $ 724 | $ 993 |
| Plan Net Position as percentage of total pension liability | 112.8% | 117.4% |
| **Total Pension Liability** | | |
| Service costs | $ – | $ 20 |
| Interest, net of acturial gain/loss | 292 | 298 |
| Benefit payments [1] | (585) | (956) |
| Changes in assumptions | 238 | – |
| **Net Change in Total Pension Liability** | $ (55) | $ (638) |
| **Total Pension Liability at beginning of year** | 5,707 | 6,345 |
| **Total Pension Liability at end of year** | $5,652 | $5,707 |
| Covered payroll | $ 961 | $1,007 |
| Net Pension Asset as a percentage of covered payroll | 75.3% | 98.6% |

[1] Prior year benefit payments included separation costs resulting in larger amounts.

[2] Restated in accordance with GASB 75 - detail information regarding the change in total OPEB liability for FY17 is not available.

[3] Reflects payments and adjustments made before the establishment of the trust on June 29, 2017.

*See accompanying independent auditor's report.*

# University System of New Hampshire

As of September 1, 2018

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KPMG

# University System of New Hampshire

**Report to the audit committee**

**Results of our audit of the financial statements for the year ended June 30, 2018**

October 25, 2018



# Introduction

**To the Audit Committee of University System of New Hampshire:**

We are pleased to have the opportunity to meet with you on October 25, 2018 to discuss the results of our audit of the financial statements of the University System of New Hampshire (the System) as of and for the year ended June 30, 2018. Our audit was conducted in accordance with the terms established in the audit engagement letter dated April 19, 2018.

We are providing this document in advance of our meeting to enable you to consider our findings and hence enhance the quality of our discussions. This document should be read in conjunction with our audit plan, presented on April 19, 2018. We will be pleased to elaborate on the matters covered in this document when we meet.

Our audit is substantially complete. Subject to the Committee's approval, we expect to be in a position to sign our audit opinion on the System's financial statements.

We expect to issue an unmodified Auditors' Report.

We draw your attention to the following communications included in the appendix (starting on slide 17) to this report:

— Responsibilities

— Responsibilities for other information in documents containing audited financial statements

— Report on the financial statements

— Report in accordance with *Government Auditing Standards*

— Management representation letter – Draft

— Update on emerging industry audit and accounting matters

— KPMG thought leadership, *The board's contribution to and oversight of strategy by colleges and universities*

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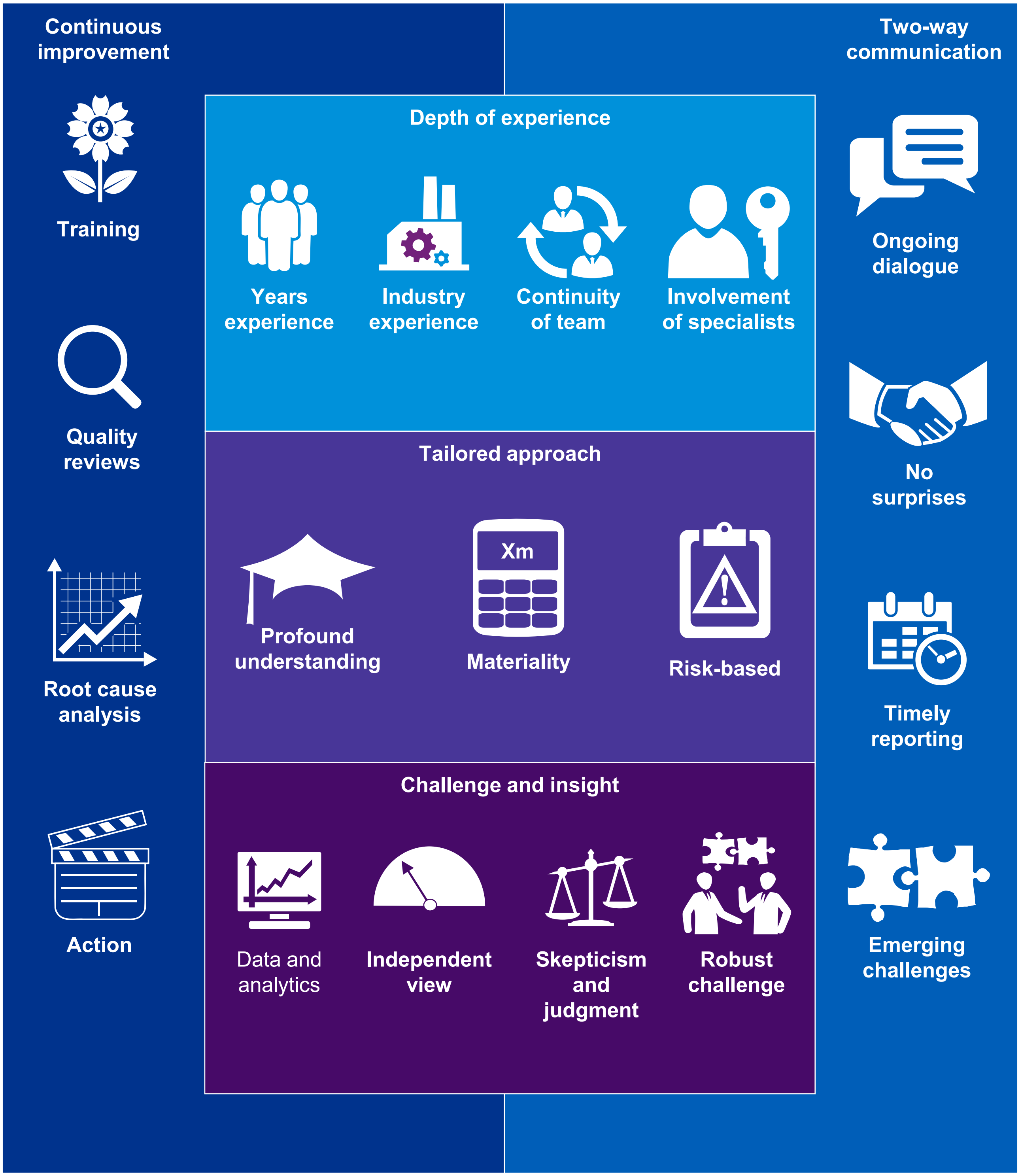
# How we delivered audit quality



# Audit summary

**Auditor's report**

Unmodified opinion on the financial statements

Emphasis of Matter paragraph regarding adoption of GASB 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*

Other Matter paragraph details KPMG's responsibility over the Required Supplementary Information

**Significant changes to our audit strategy or initial risk assessment**

There have been no significant changes to our audit strategy as compared to prior year. We did not have any changes to our initial risk assessment in the current year.

**Audit misstatements**

Corrected…………………………………………...None

Uncorrected……………………………………...None

Financial presentation and disclosure omissions…………………………....One

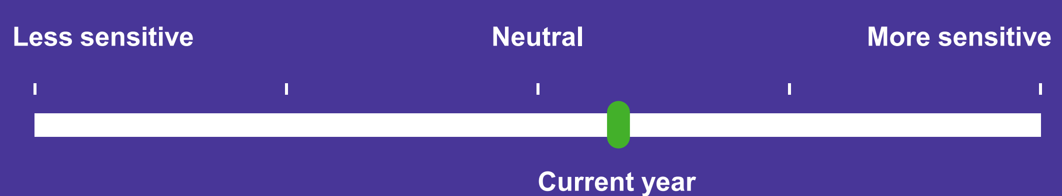
**Control deficiencies**

Material weaknesses………………………….None

Significant deficiencies………………………..None

Control deficiencies…………………………….One

**Accounting judgments related to estimates**




Our assessment of the risk associated with valuation estimates has not changed from the prior. Additional procedures were performed to audit management's implementation of GASB 75.

**Concerns regarding application of new accounting pronouncements**

— None noted

**Alternative accounting treatments**

— No matters to report

**Unusual transactions**

— No matters to report

# Audit results

## Findings at a glance

| | | Number of: | |
|---|---|---|---|
| | Uncorrected misstatements | Corrected misstatements | Control deficiencies |
| **Significant risks** | | | |
| 1 Management override of controls* | - | - | - |
| **Significant audit areas** | | | |
| 2 Cash and investments | - | - | - |
| 3 Contribution revenue, related receivables, and net assets | - | - | - |
| 4 Debt and related items | - | - | - |
| 5 Capital assets and related depreciation | - | - | - |
| 6 Tuition and fees and related receivables | - | - | - |
| 7 Grants and contracts revenue; sales of auxiliary services; and NH appropriations | - | - | - |
| 8 Compensation and benefits and related liabilities | - | - | 1 |
| 9 Commitments and contingencies | - | - | - |

*Management override of controls is an inherent significant risk in all entities
"–" indicates no findings

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 1 Management override of controls

### Significant risk of fraud

**The risk**

— Management is in a position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk nevertheless is present in all entities.

### Our response

***Internal controls***

— Assessed management's design and implementation of controls over journal entries and post-closing adjustments

— Assessed management's design and implementation of controls over recording of investment results

— Assessed management's design and implementation of controls over compliance with debt covenants

***Procedures***

— Assessed the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates.

— Performed risk assessment procedures to determine existence of any high-risk entries.

— Performed procedures over material manual post-closing adjustments to ensure accuracy and appropriateness of the entries.

— Performed procedures over the completeness, existence, accuracy, and valuation of the investment portfolio at the System, which includes benchmarking comparisons for alternative investments.

— Performed procedures to determine the System's compliance with debt covenants.

***Results***

Based on our procedures performed, no significant findings were noted.

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 2 Cash and investments

**Procedures performed**

- Gained an understanding of management's cash and investment processes
- Confirmed directly held cash and securities with financial institutions
- Tested bank reconciliations
- Reviewed audited fund financial statements, fund holdings, benchmarking of fund performance, communications with fund managers, and other monitoring documentation for alternative investments
- Price-tested directly held securities
- Reviewed accounting for year-end transactions (i.e., unsettled trades)
- Reviewed investment derivative activities and related valuation methodology
- Tested reasonableness of investment return components
- Reviewed classification of cash and cash equivalents and restricted balances
- Reviewed financial statement presentation and disclosures, including classifications within the fair value hierarchy in Levels 1, 2 and 3, as well as liquidity and related capital commitments to ensure compliance with GASB standards and U.S. GAAP
- Considered effects of subsequent events

***Significant accounting estimate(s):***

- Alternative Investments: Real estate, Hedge, Private Equity, and Collective

***Observations:***

- We spent significant collective effort on the presentation of gross purchases and sales of investments in the cash flows statement. Based on our analysis, we determined that transfers to and from the System's endowment cash account should be netted on the cash flows statement rather than grossed up because they qualify for net reporting under GASB Codification 2450.110.

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 3 Contribution revenue, related receivables, and net assets

**Procedures performed**

— Gained an understanding of management's processes surrounding gifts, pledges and distributions

— Tested a sample of new gifts to determine whether they are properly recognized and classified

— Tested roll-forward of endowment activities, including new endowments, reclassifications between net position categories, and transfers

— Reviewed required financial statement disclosures to ensure presentation was in compliance with GASB standards and U.S. GAAP

***Significant accounting estimate(s):***

— Pledges receivable, net

***Observations:***

— No significant matters noted

# Audit results (continued)

Skepticism D&A Specialists Challenge

4 **Debt and related items**

**Procedures performed**

— Gained an understanding of management's processes surrounding debt and related items
— Confirmed outstanding debt with financial institutions
— Tested new debt issuances and refundings
— Tested compliance with financial debt covenants
— Tested reasonableness of interest expense
— Reviewed required financial statement disclosures to ensure presentation was in compliance with GASB standards and U.S. GAAP

***Significant accounting estimate(s):***

— None

***Observations:***

— No significant matters noted

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 5 Capital assets and related depreciation

**Procedures performed**

— Gained an understanding of management's processes surrounding capital assets and related depreciation

— Tested fixed asset additions

— Reviewed construction-in-process accounts

— Tested reasonableness of depreciation

— Reviewed required financial statement disclosures to ensure presentation was in compliance with GASB standards and U.S. GAAP

***Significant accounting estimate(s):***

— Estimated useful lives of capital assets

***Observations:***

— No significant matters noted

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 6 Tuition and fees, and related receivables

**Procedures performed**

— Gained an understanding of management's processes surrounding tuition and fees

— Performed detailed procedures over tuition revenue, and analytical procedures over related student aid

— Tested significant receivable balances through subsequent cash receipts and adequacy of allowance for doubtful accounts

— Reviewed required financial statement disclosures to ensure presentation was in compliance with GASB standards and U.S. GAAP

***Significant accounting estimate(s):***

— None

***Observations:***

— No significant matters noted

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 7 Grants and contracts revenue; sales of auxiliary services; and NH appropriations

**Procedures performed**

— Gained an understanding of management's processes surrounding these revenue streams

— Tested propriety of allowable costs for payroll and non-payroll reimbursements under sponsored grants and contracts

— Performed analytical procedures over grants and contracts revenue

— Performed detailed procedures over sales of auxiliary services revenue

— Confirmed State of NH appropriations

— Reviewed required financial statement disclosures to ensure presentation was in compliance with GASB standards and U.S. GAAP

***Significant accounting estimate(s):***

— None

***Observations:***

— No significant matters noted

# Audit results (continued)

Skepticism D&A Specialists Challenge

## 8 Compensation and benefits and related liabilities

**Procedures performed**

- Gained an understanding of management's processes surrounding compensation and benefits and related liabilities
- Tested a sample of payroll expenses for proper recording and classification
- Performed analytical procedures over benefits expense and related accruals
- Reviewed appropriateness of OPEB actuarial calculations and related liabilities
- Reviewed GASB 75 implementation
- Reviewed required financial statement disclosures to ensure presentation was in compliance with GASB standards and U.S. GAAP

***Significant accounting estimate(s):***

- OPEB liability

***Observations:***

- As part of our test of details over payroll expenditures we reviewed the assigned functional classification for appropriateness. During this procedure we identified a coding error where an employee was charged to the incorrect function. Upon further analysis by management, they determined additional coding errors that resulted in a change to the functional expense footnote as shown below:

**Excerpt of footnote 13, operating expenses by function**

| | | *(in thousands)* | | | *(in thousands)* | |
|---|---|---|---|---|---|---|
| | **2018 Original** | **Correction** | **2018 Corrected** | **2017 Original** | **Correction** | **2017 Corrected** |
| Instruction | $ 244,807 | (18,080) | $ 226,727 | $ 242,506 | (18,823) | $ 223,683 |
| Auxiliary services | 156,961 | 1 | 156,962 | 158,478 | - | 158,478 |
| Research and sponsored programs | 110,013 | 142 | 110,155 | 106,501 | 106 | 106,607 |
| Academic support | 74,229 | 16,465 | 90,694 | 75,173 | 14,532 | 89,705 |
| Student services | 48,291 | 595 | 48,886 | 45,435 | 697 | 46,132 |
| Institutional support | 42,043 | 863 | 42,906 | 40,115 | 3,474 | 43,589 |
| Operations and Maintenance | 31,097 | 14 | 31,111 | 29,841 | 14 | 29,855 |
| Fundraising and communications | 21,467 | - | 21,467 | 23,318 | - | 23,318 |
| Public service | 10,584 | - | 10,584 | 9,308 | - | 9,308 |
| **Subtotal current funds** | **$ 739,492** | **-** | **$ 739,492** | **$ 730,675** | **-** | **$ 730,675** |

# Audit results (continued)

Skepticism D&A Specialists Challenge

**9 Commitments and contingencies**

**Procedures performed**

- Obtained legal letters and reviewed any litigation assessments
- Reviewed disclosure of other commitments and contingencies
- Performed standard tax provision review in relation to financial statements

***Observations:***

- No significant matters noted

# Required communications and other matters

| Type | | Response |
|---|---|---|
| **Related parties** | OK | No matters to report. |
| **Illegal acts or fraud** | OK | No actual or suspected fraud involving management, employees with significant roles in internal control, or where fraud results in a material misstatement in the financial statements were identified during the audit. Maintained heightened awareness and professional skepticism regarding p-card fraud identified in FY2017 |
| **Noncompliance with laws and regulations** | OK | None noted. |
| **Modifications to auditors' report** | OK | Emphasis of Matter paragraph added to highlight adoption of GASB 75. Our report is not modified with respect to this matter. |
| **Subsequent events** | OK | None noted. |
| **Independence** | OK | We hereby confirm that as of October 25, 2018, we are independent accountants with respect to the System under all relevant professional and regulatory standards. |
| **Significant difficulties encountered during the audit** | OK | No matters to report. |
| **Disagreements with management or scope limitations** | OK | No matters to report. |
| **Management's consultation with other accountants** | OK | No matters to report, of which we are aware. |
| **Significant issues discussed, or subject to correspondence with management** | OK | No matters to report. |
| **Difficult or contentious matters for which the auditors consulted** | OK | No matters to report. |
| **Material written communications between KPMG and management** | OK | Engagement and management representation letters. |

# Appendix

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# Responsibilities

**Management is responsible for:**

— Preparation and fair presentation of the financial statements, including disclosures, in conformity with generally accepted accounting principles (GAAP).

— For 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.

— Ensuring that the System's operations are conducted in accordance with the provisions of laws and regulations, including compliance with the provisions of laws and regulations that determine the reported amounts and disclosures in the System's financial statements, and for informing the auditor of any known material violations of such laws and regulations.

— To provide access to all information of which management is aware that is relevant to the preparation and fair presentation of the financial statements, such as records, documentation, and other matters, additional information that we may request from management for the purpose of the audit, and unrestricted access to persons within the entity from whom we determine it necessary to obtain audit evidence.

— Adjusting the financial statements to correct material misstatements and affirming that the effects of any uncorrected misstatements aggregated by the auditor are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

— Providing the auditor with a letter confirming certain representations made during the audit that includes, but is not limited to, management's:

  - Disclosure of all significant deficiencies, including material weaknesses, in the design or operation of internal controls that could adversely affect the System's financial reporting.

  - Acknowledgement of their responsibility for the design and implementation of programs and controls to prevent, deter, and detect fraud.

**The Audit Committee is responsible for:**

— Oversight of the financial reporting process and oversight of ICOFR.

— Oversight of the establishment and maintenance by management of programs and controls designed to prevent, deter, and detect fraud.

**Management and the Audit Committee are responsible for:**

— Setting the proper tone and creating and maintaining a culture of honesty and high ethical standards.

**The audit of the financial statements does not relieve management or the Audit Committee of their responsibilities**

# Responsibilities (continued)

**KPMG is responsible for:**

— Planning and performing our audit, with an attitude of professional skepticism, to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by fraud or error. Accordingly, there is some risk that a material misstatement of the financial statements will remain undetected. Although not absolute assurance, reasonable assurance is a high level of assurance. Our audit is not designed to detect error or fraud that is immaterial to the financial statements.

— Conducting the audit in accordance with professional standards and complying with the rules and regulations of the Code of Professional Conduct of the American Institute of Certified Public Accountants and the ethical standards of relevant CPA societies, and relevant state boards of accountancy.

— Forming and expressing an opinion about whether the financial statements that have been prepared by management with the oversight of the Audit Committee are presented fairly, in all material respects, in conformity with GAAP.

— An audit of the financial statements includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting.

— Communicating to the Audit Committee all required information, including significant matters, that are in our professional judgment, relevant to the responsibilities of those charged with governance in overseeing the financial reporting process.

— Communicating to management and the Audit Committee in writing all significant deficiencies and material weaknesses in internal control identified during the audit and reporting to management in writing all deficiencies noted during our audit that, in our professional judgment, are of sufficient importance to merit management's attention. The objective of our audit of the financial statements is not to report on the System's internal control and we are not obligated to search for material weaknesses or significant deficiencies as part of our audit of the financial statements.

— Communicating to the Audit Committee circumstances that affect the form and content of the auditors' report, if any.

# Responsibilities for other information in documents containing audited financial statements

- The auditors' report on the financial statements does not extend to other information in documents containing audited financial statements, excluding required supplementary information.
- The auditors' responsibility is to make appropriate arrangements with management or the Audit Committee to obtain the other information prior to the report release date and to read the other information to identify material inconsistencies with the audited financial statements or material misstatements of fact.
- Any material inconsistencies or misstatements of facts that are not resolved prior to the report release date, and that require revision of the other information, may result in KPMG modifying or withholding the auditors' report or withdrawing from the engagement.
- We have performed the following procedures with respect to other information in documents:
  - We read Management's Discussion and Analysis, which is required supplementary information under U.S. GAAP.
  - We did not audit Management's Discussion and Analysis, but we noted no material inconsistencies between it and the financial statements.

# Report on the financial statements

**Independent Auditors' Report**

The Governor and
Legislative Fiscal Committee
State of New Hampshire; and
The Board of Trustees
University System of New Hampshire:

## Report on the Financial Statements

We have audited the accompanying statements of net position of the University System of New Hampshire (the System), a component unit of the State of New Hampshire, as of and for the years ended June 30, 2018 and 2017, the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the System's basic financial statements for the years then ended.

### *Management's Responsibility for the Financial Statements*

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

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. 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 opinion.

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of the University System of New Hampshire as of June 30, 2018 and 2017, and the changes in its net position and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

# Report on the financial statements (continued)

***Emphasis of Matter***

As discussed in Note 1 to the financial statements, in 2018 the System adopted Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

***Other Matter - Required Supplementary Information***

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages __–__ and the required supplemental information on page _____ 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 audits 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.

*(signed) KPMG LLP*

October _______, 2018

**Independent Auditors' Report**

The Governor and
Legislative Fiscal Committee,
State of New Hampshire, and
The Board of Trustees
University System of New Hampshire:

**Report on the Financial Statements**

We have audited the accompanying statements of net position of the University System of New Hampshire (the System), a component unit of the State of New Hampshire, as of and for the years ended June 30, 2018 and 2017, the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the System's basic financial statements.

***Management's Responsibility for the Financial Statements***

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

***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of the University System of New Hampshire as of June 30, 2018 and 2017, and the changes in its net position and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

# Report on the financial statements (continued)

***Emphasis of Matter***

As disclosed in Note 1 to the financial statements, the System adopted Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

***Other Matter – Required Supplementary Information***

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages __–__ and the required supplemental information on page _____ 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 audits 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.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October ____, 2018 on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control over financial reporting and compliance.

*(signed) KPMG LLP*

October _______, 2018

**Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards***

The Governor and
Legislative Fiscal Committee,
State of New Hampshire, and
The Board of Trustees
University System of New Hampshire

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the University System of New Hampshire (the System), a component unit of the State of New Hampshire, which comprise the statement of net position as of June 30, 2018, the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October _____, 2018. Our report includes an emphasis of matter paragraph noting that the System adopted Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the System's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the

# Report in accordance with *Government Auditing Standards* (continued)

determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*(signed) KPMG LLP*

October ______, 2018

# Management representation letter – Draft

October _______, 2018

KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

Ladies and Gentlemen:

We are providing this letter in connection with your audit of the statements of net position of the University System of New Hampshire (the System), a component unit of the State of New Hampshire, as of and for the years ended June 30, 2018 and 2017, the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, for the purpose of expressing opinions as to whether these financial statements present fairly, in all material respects, the net position, changes in net position, and cash flows thereof in accordance with U.S. generally accepted accounting principles.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, as of October ________, 2018:

1) We have fulfilled our responsibilities, as set out in the terms of the audit engagement letter dated April 19, 2018, for the preparation and fair presentation of the financial statements in accordance with U.S. generally accepted accounting principles.

2) We have made available to you:

   a) All records, documentation, and information that is relevant to the preparation and fair presentation of the financial statements.

   b) Additional information that you have requested from us for the purpose of the audit;

   c) Unrestricted access and the full cooperation of personnel within the entity from whom you determined it necessary to obtain audit evidence; and

   d) All minutes of the meetings of Board of Trustees, committees of the Board of Trustees, or summaries of actions of recent meetings for which minutes have not yet been prepared. All significant board and committee actions are included in the summaries.

# Management representation letter – Draft (continued)

3) Except as disclosed to you in writing, there have been no communications from regulatory agencies, governmental representatives, employees or others concerning noncompliance with laws and regulations in any jurisdiction, or deficiencies in financial reporting practices or other matters that could have a material adverse effect on the financial statements.

4) We have disclosed to you, in writing, all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

5) All material transactions have been recorded in the accounting records and are reflected in the financial statements.

6) There are no side agreements or other arrangements (either written or oral).

7) There are no events subsequent to the date of the statement of net position and through the date of this letter for which U.S. GAAP requires adjustment or disclosure.

8) The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with paragraphs 96 – 113 of Governmental Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.*

9) We have disclosed to you all known actual or possible litigation, claims, and assessments whose effects should be considered when preparing the financial statements.

10) We acknowledge our responsibility for the design, implementation, and maintenance of programs and controls to prevent, deter, and detect fraud; for adopting sound accounting policies; and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the financial statements and to provide reasonable assurance against the possibility of misstatements that are material to the financial statements whether due to error or fraud. We understand that the term “fraud” is defined as an intentional act by one or more individuals among management, those charged with governance, employees, or third parties, involving the use of deception that results in a misstatement in financial statements that are the subject of an audit.

11) There are no deficiencies, significant deficiencies, or material weaknesses in the design or operation of internal control over financial reporting of which we are aware, which could adversely affect the System’s ability to initiate, authorize, record, process, or report financial data. We have applied the definitions of a “significant deficiency” and a “material weakness” in accordance with the definitions in AU-C Section 265.07, *Communicating Internal Control Related Matters Identified in an Audit.*

12) We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

13) We have no knowledge of any fraud or suspected fraud affecting the System involving:

   a) Management

   b) Employees who have significant roles in internal control, or

   c) Others where the fraud could have a material effect on the financial statements.

14) We have disclosed to you all information that we are aware of regarding allegations of fraud or suspected fraud affecting the System's financial statements communicated by employees, former employees, regulators, or others.

15) We have no knowledge of any officer or member of governing body of the System, or any other person acting under the direction thereof, having taken any action to fraudulently influence, coerce, manipulate, or mislead you during your audit.

16) Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

17) We have disclosed to you the identity of our related parties and all the related party relationships and transactions of which we are aware.

18) The following have been properly recorded or disclosed in the financial statements:

    a) Related party relationships and transactions of which we are aware in accordance with U.S. generally accepted accounting principles, including sales, purchases, loans, transfers, leasing arrangements, guarantees, ongoing contractual commitments, and amounts receivable from or payable to related parties.

       The term "related party" refers to government's related organizations, joint ventures, and jointly governed organizations, as defined in GASB Statement No. 14, *The Financial Reporting Entity*, as amended; elected and appointed officials of the government; its management; members of the immediate families of elected or appointed officials of the government and its management; and other parties with which the government may deal if one party can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests. Another party also is a related party if it can significantly influence the management or operating policies of the transacting parties or if it has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.

    b) Guarantees, whether written or oral, under which the System is contingently liable.

    c) The existence of and transactions with joint ventures and other related organizations.

19) The System has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets, nor has any asset been pledged as collateral.

20) The System has complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.

21) The System's reporting entity includes all entities that are component units of the System.

22) We have disclosed to you all accounting policies and practices we have adopted that, if applied to significant items or transactions, would not be in accordance with U.S. generally accepted accounting principles. We have evaluated the impact of the application of each such policy and practice, both individually and in the aggregate, on the System's current period financial statements, and the expected impact of each such policy and practice on future periods' financial reporting. We believe the effect of these policies and practices on the financial statements is not material. Furthermore, we

do not believe the impact of the application of these policies and practices will be material to the financial statements in future periods.

a) With respect to the System's practice used to report its endowment return, net of amounts used in operations as other changes in net position, we have adopted this practice because to do otherwise would cause volatility in the "Increase in net position from recurring activities" measure which may mislead readers of the financial statements. The endowment assets are invested to generate returns over a long-term horizon resulting in gains (losses) which can vary significantly on an annual basis due to prevailing market conditions. We acknowledge that the proper presentation is within non-operating revenues/expenses. We only use the annual payout from these investments to support ongoing expenses and have limited the income included in non-operating revenues to that amount.

23) We acknowledge our responsibility for the presentation of the required supplementary information which includes, management's discussion and analysis and the schedules of funding progress, in accordance with the applicable criteria and prescribed guidelines established by the *Governmental Accounting Standards Board* and:

a) Believe the required supplementary information, including its form and content, is fairly presented in accordance with the applicable criteria and prescribed guidelines.

b) The methods of measurement or presentation of the required supplementary information have not changed from those used in the prior period except as required by the implementation of GASB 75.

c) The significant assumptions or interpretations underlying the measurement or presentation of the required supplementary information are reasonable and appropriate.

24) In accordance with Government Auditing Standards, we have identified to you all previous audits, attestation engagements, and other studies that relate to the objectives of this audit, including whether related recommendations have been implemented.

25) We agree with the findings of specialists in evaluating the financial statement liabilities and costs associated with the retirement and other post-employment benefits and to determine information related to the System's funding progress related to such benefits for financial reporting purposes and have adequately considered the qualifications of the specialist in determining the amounts and disclosures used in the basic financial statements and underlying accounting records. We did not give or cause any instructions to be given to specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an impact on the independence or objectivity of the specialists.

26) The projected employer contributions in the Operating Staff Retirement Plan discount rate calculation are prepared in accordance with paragraphs 27-29 of GASB Statement 68.

27) We have received opinions of counsel upon each issuance of tax-exempt bonds that the interest on such bonds is exempt from federal income taxes under section 103 of the Internal Revenue Code of 1986, as amended. There have been no changes in the use of property financed with the proceeds of tax-exempt bonds, or any other occurrences, subsequent to the issuance of such opinions, that would jeopardize the tax-exempt status of the bonds. Provision has been made, where material, for the amount of any required arbitrage rebate.

28) There have been no circumstances that have resulted in communications from the System's external legal counsel to the System reporting evidence of a material violation of securities law or breach of fiduciary duty, or similar violation by the System or any agent thereof.

29) Significant relationships with affiliated organizations, and the financial statements of those organizations, where required, have been properly recorded or disclosed in the System's financial statements.

30) There are no representations provided in connection with your audit of the financial statements as of June 30, 2017 and for the year then ended that require modification



Very truly yours,

**University System of New Hampshire**

_________________________________

Todd Leach, Chancellor

_________________________________

Cathy Provencher, Vice Chancellor

_________________________________

Carol Mitchell, Controller

# Update on emerging industry audit and accounting matters

**Governance and regulatory change:**

- New KPMG thought leadership: *The Board's Contribution to and Oversight of Strategy at Colleges and Universities*
- Department of Education – Proposed revisions to Title IV Financial Responsibility Standards

**GASB statements effective in future years**

**June 30, 2019**

- No. 83, *Certain Asset Retirement Obligations*

**June 30, 2020**

- No. 84, *Fiduciary Activities*

**June 30, 2021**

- No. 87, *Leases*

# The board's contribution to and oversight of strategy at colleges and universities

Along with selecting or replacing the CEO, involvement with and oversight of strategy is generally recognized as a chief responsibility of governance. Despite that recognition, governing boards have acknowledged challenges to fulfilling this critical role. While management typically develops the strategic plan (preferably with board involvement), the role of a board is to understand, discuss, and when appropriate, challenge underlying assumptions or other aspects of the plan. While governing the institution for the present, helping guide it into the future calls for board members to provide oversight, insight, and foresight.

Since the start of 2018, we have engaged in conversations with a few colleges and universities around a common theme—the board's oversight of strategy, particularly during a period of challenge and change for higher education.

That presidents and board members have raised the issue is not surprising and is, in fact, consistent with views expressed by public company directors. In his NACD Directorship article *Public Company Board Priorities for 2018* summarizing responses to the *2017–2018 NACD Public Company Governance Survey*, Friso van der Oord, Director of Research, National Association of Corporate Directors (NACD) noted that the survey queried board members regarding opportunities for improving board performance, and the most frequently cited area was the board's contribution to strategy. He added that "71 percent of directors indicate that their boards must better understand the risks and opportunities that affect performance and drive strategic choices … many boards still struggle to move from a traditional review-and-concur approach to deep and continual engagement with strategy."

Before providing a view into the NACD's recommendations, let's consider a few thoughts about the importance of the board understanding the strategic choices that likely have been discussed by senior management. The following was excerpted from an article in the April 2018 McKinsey Quarterly: "The goal of most strategy discussions is to approve or reject a single proposal…suggesting different options, or questioning the plan's premise is often unwelcome…choices are the essence of real strategy, and the planning process should be geared to shining a spotlight on them." Our experience with many colleges and universities supports the notion that more often than not it is a particular path forward that is brought to the board while management's deep and thoughtful deliberations of alternate paths go unpresented. Almost all of the time, this is based on a desire to use the board's time effectively rather than to keep them from considering other options. We encourage the development of a meeting agenda that allows significant time for strategy discussion, including sufficient time to cover the road(s) not taken.

Returning to the NACD's recommendations—Mr. van der Oord explains them as "among the concrete actions directors should consider: develop a more intimate understanding of your changing business and industry…engage with management on strategy issues…evaluate strategy options and underlying assumptions…and not be afraid to ask difficult questions about the viability of the business."

For colleges and universities, it is important that mission drive strategy and inspire all decisions made by institutional stewards to accomplish their vision. In the November/December 2017 issue of AGB's Trusteeship magazine, Dr. Ellen Chaffee, Senior Fellow for the Association of Governing Boards of Universities and Colleges (AGB), asserted "we need to start where we are and think about the future, focus on purpose and why we exist, and ask why anyone should care if we exist. That's very fundamental, and it's an area in which trustees can be very helpful in terms of giving us some perspective...they come to us with fewer assumptions and more experiences in other settings...people who will challenge the way we've been doing things, who will bring new ideas to how things could be done, who can enrich our sense of purpose and our direction..."

Perhaps belatedly, let's raise the question: What is strategy? There are many dictionary definitions, media articles and even YouTube videos. The 2014 *Report of the NACD Blue Ribbon Commission on Strategy Development* offers the following: "strategy is the means to create economic value by gaining competitive advantage through a unique value proposition." In an April 2018 Harvard Business Review article *Your Strategic Plans Probably Aren't Strategic, or Even Plans*, Graham Kenny says "[strategy is] a scarily misunderstood concept in management and board circles. The most basic mix-up is between 'objective,' 'strategy,' and 'action'… The key to strategy is that it's the positioning of one business against others."

Recognizing that competition and competitive positioning are critical elements of strategy, the higher education challenge frequently comes down to how to gain (or perhaps maintain) market share in an industry that is overpopulated. Depending on the institution, the most pressing competitive battles may be for students, faculty, researchers and research dollars, or even state funding. Often, the competitive landscape can shift so quickly that institutional response is challenged to keep up with the pace of change amid considerable uncertainty. For example, New York State's Excelsior Scholarship program and its offer of free tuition to residents meeting family income criteria and other conditions became effective so quickly after being announced as a legislative priority that many private colleges and universities in the state—and many outside the state seeking to enroll students from New York—were faced with enrollment uncertainty and financial vulnerability.

Earlier this year, AGB issued its biennial edition (2018–2019) of *Top Strategic Issues for Boards,* which it designed to help boards with their work "that concentrates on strategy rather than management and on long-range issues instead of day to day concerns." The issues highlighted—Educational Quality, Financial Stability, Freedom of Speech, Innovation, Presidential Leadership, and Relevance—are each covered in depth, including proposed "Questions for Boards to Consider."

We will focus our attention on Financial Stability. With respect to this issue, AGB notes that various "financial trends combine to put severe pressure on the traditional higher education business model".

Once again we see the overlap of risks facing higher education and corporations, as business model pressures confront all industries. The top two risks identified in the Protiviti and NC State issued *Executive Perspectives on Top Risks for 2018* were:

— Rapid speed of disruptive innovations and/or new technologies…may outpace our organization's ability to compete…without making significant changes to our business model; and

— Resistance to change may restrict our organization from making necessary adjustments to the business model and core operations.

These risks identified by corporate executives could have come from a survey of higher education leaders. In fact, a United Educators survey in 2017 found the business model, including enrollment trends, staffing levels, and fiscal and tuition management, ranked as the top reputational risk confronting colleges and universities over the next three years. Also, in a survey of board members as reported in *The AGB 2017 Trustee Index* "58% say business models need to change moderately, and 34% say they need to change drastically…when asked to identify the biggest barrier to changing a higher education institution's business model, board members are most likely to cite lack of support from faculty (28%), followed by a lack of confidence among institutional leaders to make changes (19%)…".

Corporate executives cite resistance to change as a top risk. In meeting their oversight responsibilities, college and university board members face unique challenges with respect to the long-standing traditions of tenure (a challenge exacerbated by no mandatory retirement age) and shared governance. Many trustees believe their institutions need to consider significant changes to academic offerings—not only additions, but subtractions as well—and may have been led to believe that such changes, especially program closures, are nearly impossible, particularly for institutions that are currently in reasonably good financial condition.

In a May 2018 Forbes opinion piece *Is Tenure Dying? Does it Matter?* Richard Vedder, Distinguished Professor of Economics Emeritus at Ohio University, wrote, "Tenure emboldens faculty members to be feisty, argumentative, and protective of their property rights in certain courses, office space, and even parking…. That is a huge problem if, as is increasingly the case, enrollment decline, changing student interests, or debilitating faculty performance make dismissal of the faculty member advisable…. Decision making in universities thus often becomes costly, time consuming, and is filled with dubious compromises to minimize brutal academic wars. Shared governance is expensive and often leads to non-optimal decisions." The 2017 issued *AGB Board of Directors' Statement on Shared Governance* acknowledges the challenges noting "Boards, faculty, and presidents…continue to struggle with its value and its effectiveness," but asserted "In higher education's volatile environment, shared governance is essential." AGB has also recommended that institutions regularly review their shared governance practices for potential improvements, and notes that "perhaps the best indicator of how well shared governance is working on any campus is whether it enables, rather than constrains, thoughtful decisions to enhance student success, institutional health, and innovation."

Although the NACD advised public company directors to better understand their business and industry, the *AGB 2017 Trustee Index* concluded that "board members seem to be well aware of the challenges facing the sector." Our own experience with college and university audit committees and boards supports AGB's conclusion that issues and trends, including rating agency views (e.g., Moody's current negative outlook for the sector), struggles to reach enrollment goals, rising discount rates, declining or modestly increasing state funding, demographic changes, public questioning of higher education's value proposition, student debt, and rising costs are generally well understood. That said, we see opportunity for board members to deepen the conversation regarding their institutions, without crossing the line into management. Board retreats, which are increasingly common in the industry and take place away from the more routine business of committee agendas, may provide such an opportunity. With respect to the financial stability and business model issue, AGB's Questions for Boards to Consider are presented below.

# Financial stability

**QUESTIONS FOR BOARDS TO CONSIDER**

- Does your board include members with the skills, knowledge, and background needed to plan for the financial future of your institution? How can your board best achieve collective "financial literacy," while recognizing that not all board members need to be financial experts?
- Do recent fiscal results and future financial and demographic trends point to a need to rethink or reform your institution's current business model? What changes would lead to greater financial stability and long-term sustainability?
- Has your board taken a close look at your institution's cost structure to identify the potential for reductions that would not negatively affect the mission or educational quality and student success? Are there any programs that could be consolidated, costs that could be cut, or economies that could be taken advantage of in order to increase productivity and efficiency?
- What are the key factors affecting net tuition revenue at your institution? Is financial aid being used effectively?
- Could your institution gain a competitive advantage by diversifying its educational offerings or launching new programs that attract new types of students and increase enrollments? What efforts are underway to promote student retention and completion?
- Does your board have a system for tracking key financial metrics that provides data relevant to long-term financial decision making?

Excerpted from AGB's *Top Strategic Issues for Boards* (2018–2019)

We recognize that deeper dives into net tuition revenue and financial aid may lead to some sensitive conversations, but the criticality of these business model components for most institutions warrants the discussion. Additional questions that may be considered include: Are aid policies consistent with our mission? Is aid used strategically to build the desired student population? How is aid allocated between merit-based and need-based awards? What controls are in place to mitigate the risk of over-awarding institutional aid? and What is the debt burden being taken on by our students? Also, the percentage of students receiving Pell Grants—a metric widely used to measure the enrollment of low income students—may be of interest to board members at many institutions and perhaps particularly important for elite schools or those whose missions promote socio-economic diversity and access.

For those institutions with significant research enterprises, board members may want to consider the following questions: How are the direct and indirect costs of our research efforts, including compliance, funded (i.e., federal, corporate, foundation or other external sources vs. internally)? Is the institution's research enterprise supported by an appropriate infrastructure? Is the intellectual property associated with our research understood, leveraged, and protected? What is the level of annual royalties earned from our research and how are those royalties shared? For those schools which seek to raise their research profile, questions surrounding the return on investment should be, and likely are being, discussed.

Strategic plans need a means, such as milestones and performance metrics, to enable the board to monitor progress and timely determine whether revision is needed. Revision is by no means failure, as strategy must be dynamic because of the pace of change. To help guide the institution toward achievement of strategic goals, beyond internal information including analysis of financial and operational data, board members need information with respect to industry trends, forward-looking indicators, and competitors.

Not only is involvement with strategy a top responsibility of governance, but active involvement from formation to ultimate achievement offers opportunity to truly lead, add value, and advance institutional mission.

# Contact us


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