Annual Financial Report

Fiscal Year 2016-2017

MICHIGAN STATE
UNIVERSITY

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MICHIGAN STATE UNIVERSITY
TRUSTEES, OFFICERS, AND FINANCE MANAGEMENT

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MICHIGAN STATE
UNIVERSITY

October 27, 2017

We are pleased to present Michigan State University's financial report and results of operations for fiscal years ended June 30, 2017, and June 30, 2016. The financial report was prepared by Finance staff in accordance with generally accepted accounting principles for public colleges and universities as defined by the Governmental Accounting Standards Board. The Board of Trustees adopted the report as part of MSU's commitment to report annually on its fiscal affairs. Plante & Moran, PLLC, certified public accountants, audited these financial statements. The enclosed information is accurate in all material respects and reported in a manner fairly representing the University's financial position, to the best of our knowledge.

Financial Report Highlights:

- The University's financial assets were $6.1 billion with a net position of $3.9 billion.
- Revenues totaled $3.0 billion, while expenses totaled $2.5 billion.
- Total net position grew by $482 million, primarily due to net investment income that totaled $391 million.
- Grants and contracts revenue, including capital grants, contributed $562 million.
- Charitable gift commitments received from donors totaled $201 million.

MSU has been working to advance the common good in uncommon ways for more than 160 years through more than 200 programs of study in 17 degree-granting colleges. Consistently ranked among the world's top universities, MSU remains among the most efficient of its peer research institutions.

MSU makes an impact across Michigan and the world. The University has a presence in every county in our state through our medical schools, research stations, partner hospitals, and MSU Extension. We take seriously our missions of education, research, and outreach. By maintaining a level of in-state enrollment that is well above the Big Ten average, MSU is providing a world-class education to the best and brightest of Michigan.

As the nation's pioneer land-grant university, MSU embraces its special mission of world-class instruction, research, and public service to solve the world's most pressing problems. Through the combined efforts of its faculty, staff, alumni, and worldwide supporters, MSU continues its role as the world's preeminent land-grant university by making a significant impact on Michigan, the nation, and the world. Spartans Will.

Mark P. Haas

Mark P. Haas
Vice President for Finance and Treasurer

OFFICE OF THE
VICE PRESIDENT FOR FINANCE

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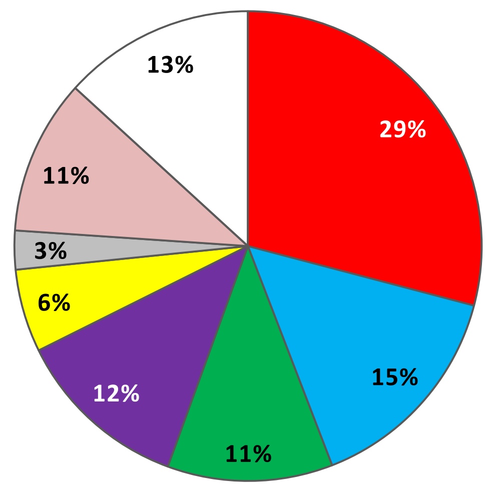
Since its humble beginnings over 160 years ago as the Agricultural College of the State of Michigan consisting of five faculty and 63 students, Michigan State University (MSU) has transformed itself into a globally recognized institution of excellence that has made a difference in the lives of over one million students from all 83 counties in Michigan, all 50 states in the United States, and over 130 countries around the world. Those students carry the torch of knowledge, science and innovation out to their communities around the world to effect change and better the countless number of individuals they will encounter over the course of their lives. MSU has established a campaign of recognition and inspiration using ***Spartans Will*** to describe the spirit that drives the Spartan community. This spirit relentlessly strives to advance knowledge and transform lives in practical, sustainable and innovative ways that address society's rapidly changing needs. Today, an estimated 552,000 living alumni carry that torch of goodwill worldwide.

In a challenging economic environment, MSU has managed to build a strong economic foundation with a total of $3.9 billion in net position at June 30, 2017, an increase of $482 million from June 30, 2016. Revenue diversification has long been an important strategy for the University to achieve financial stability and continues to be a focus moving forward.

Sources of Net Revenue (millions):

$ 859	Tuition, net of discounts
445	Grants and contracts
338	State/Capital appropriations
357	Auxiliary activities
169	Private gifts
79	Capital grants
316	Other departmental activities
391	Net investment income (endowments and operating cash)
$ 2,954	**Total net revenues**



The University's financial statements have been audited by Plante and Moran, PLLC, and MSU has once again received an unmodified ("clean") opinion. In the following sections, we will highlight how the collective ***Spartans Will*** spirit is contributing to the University's ranking as one of the top 100 universities in the world.

Spartans Will. Build a Stronger Academic Model

MSU recognizes that it is imperative that a high quality student experience continues to be a major focus of the University. Although MSU's freshman retention rate of 90% is much higher than the national average of 68%, studies have shown retention rates at colleges and universities are significantly higher for students who make connections with their peers and faculty within the first semester. In response, MSU is taking steps to encourage inclusion, foster connectivity and build a sense of belonging by implementing *Spartans Transition to Excellence Program (STEP*). The STEP program is a collaborative interdepartmental effort to engage students in small group settings with volunteer coaches during orientation and throughout their first year to help ease the transition to college life.

In addition to a focus on building relational connections with students, MSU introduced the ***Go Green, Go 15*** campaign to inform incoming MSU students about the benefits of course credit momentum. The campaign empowers students by creating opportunities for them to meet with academic advisors and learn about the advantages of appropriate course loads and to develop a pathway to graduation. Studies have shown that students who attempt 30 or more credits in their first year recorded higher graduation rates, higher grade point averages and were less likely to retake classes. In addition, the overall cost of a degree (housing, tuition, interest on student debt, and delayed employment) decreased for students that maintained a class schedule that averaged 15 credits per semester. MSU is committed to helping students realize value from their time on campus for years to come.

MSU and its donors are investing in academic facilities to enhance the student learning experience. This includes the following major academic construction projects that are in planning, under construction, or have been completed during 2017:

- A donor and University funded expansion to the College of Music facilities for additional rehearsal space, practice rooms, a large lecture hall, offices, a recording and multimedia room and a gathering space;
- A new Bio Engineering Facility that houses the Institute for Quantitative Health Sciences and Engineering and the Department of Biomedical Engineering funded through state capital appropriations and University funds;
- A new University funded Interdisciplinary Science and Technology Building that will provide modern research space that will promote interdisciplinary work to pursue big ideas, innovation, and global impact.

MSU is continuing to foster collaboration across departments in an effort to enhance the overall student experience. The new *1855 Place* integrates housing for 926 students with event parking, retail space, a ticketing office for MSU events, University administrative offices and outdoor recreational space. Leveraging synergy between Residential Housing and Intercollegiate Athletics, this new community provides a model for effectively integrating student housing with the student experience.

Spartans Will. Build a Stronger Research Model

Research is a fundamental part of MSU's mission and a natural output of the creative process that transforms Spartans from individual faculty and students to globally engaged citizen leaders. MSU researchers are united for the purpose of answering questions and creating solutions to challenges that stand in the way of a better quality of life for individuals and communities at home and around the world. To facilitate a continued emphasis on research, MSU has proactively invested financial resources to make MSU's campus an attractive location for grantors to consider for research funding. These investments include creating state of the art space for research, including:

- The Facility for Rare Isotope Beams (FRIB) project is a $730 million partnership with the U.S. Department of Energy and the State of Michigan in the field of nuclear science research. In fiscal year 2017, the facility's exterior infrastructure was substantially completed ahead of schedule and ongoing work to equip the facility to make it operational is expected to be completed by 2022. A recent economic impact study estimates that this project will create 1,000 ongoing operational jobs once the facility is placed in service;
- The Grand Rapids Research Center for biomedical research is expected to create 130 new operations jobs;
- The Food Processing and Innovation Center is a USDA/FDA certified facility and is expected to be an incubator to create more than 300 jobs annually.

2,228
local construction jobs for FRIB and Grand Rapids Research Center

$4.4 B
FRIB's expected economic impact to Michigan's economy

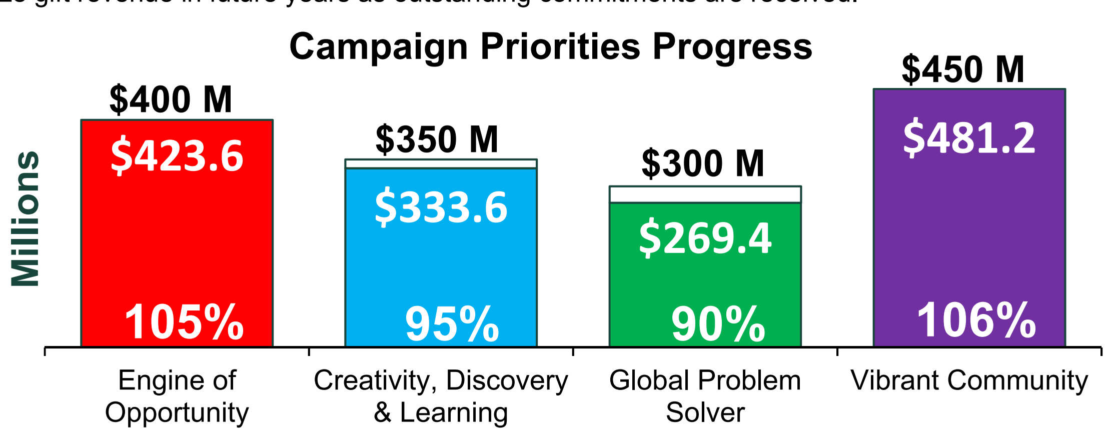
Research-related efforts by MSU have also focused on building partnerships with other research institutions to facilitate collaborative research opportunities throughout Michigan and beyond. Examples of such partnerships include:

- A lead role in the Detroit site for the Institute for Advanced Composites Manufacturing Innovation (IACMI), a 122-member consortium funded by a more than $70 million commitment over five years from the U.S. Department of Energy. This partnership will enhance our relationship with industry corporate partners, as well as complement MSU's already nationally recognized Composite Materials and Structures Center and the Composite Vehicles Research Center located in the College of Engineering;
- A partnership in the Cooperative Institute for Great Lakes Research (CIGLR), a regional consortium of 39 partner and affiliate organizations that is funded by a $20 million grant from the National Oceanic and Atmospheric Administration. This partnership will benefit from the intellectual capital of over 100 researchers from MSU who work on water-based research and will create new research opportunities that will benefit the environmental resources of the Great Lakes region;
- Great Lakes Bioenergy Research Center, in partnership with the University of Wisconsin-Madison, is one of 4 Bioenergy Research Centers funded by the U.S. Department of Energy that employs more than 400 researchers, students and staff conducting foundational bioenergy research;
- University Research Corridor (URC) is an alliance with the University of Michigan and Wayne State University that, according to the most recent economic impact report (based on FY15 data), is annually contributing more than a $16.5 billion net economic impact and over 68 thousand jobs to Michigan's economy;
- Michigan State University Bioeconomy Institute, with funding from the Michigan Economic Development Corporation and the U.S. Department of Commerce's Economic Development Administration, has been an incubator of growth for more than a dozen businesses, has attracted out-of-state businesses to Michigan and has provided an excellent opportunity for undergraduate and graduate students to participate in real world entrepreneurial activities.

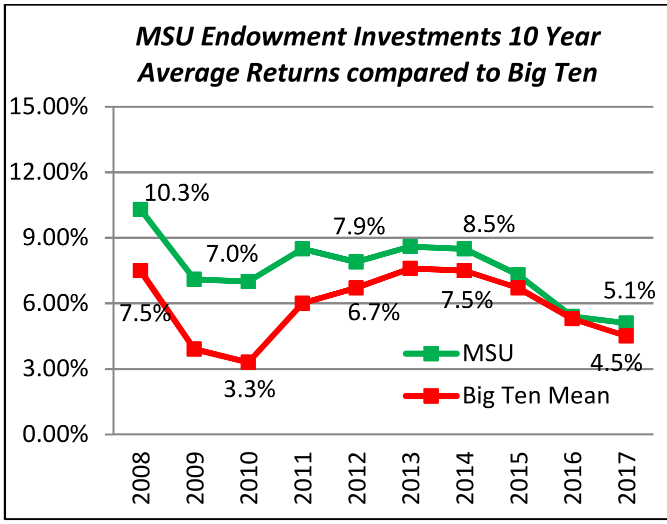
These partnerships create world-class research opportunities for faculty and students of MSU and act as economic engines that propel job creation and ignite an entrepreneurial spirit in Michigan and around the world.

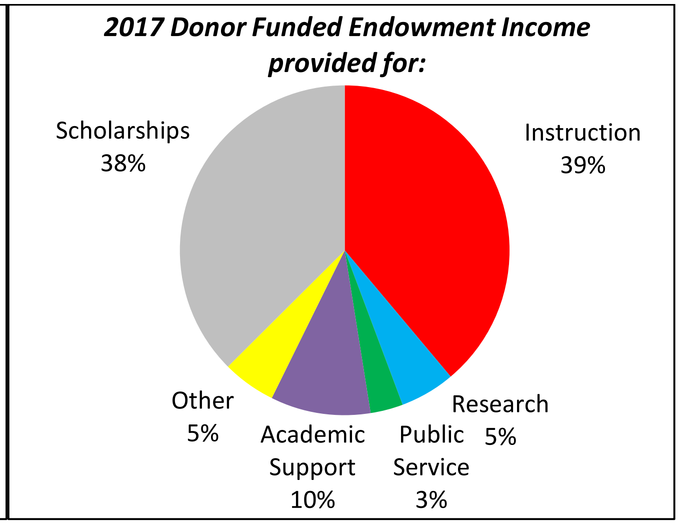
Spartans Will. Build a Stronger Financial Model

Launched in the fall of 2014, MSU has been engaged in the *Empower Extraordinary* capital campaign to build a solid foundation for the future. With the campaign scheduled to run through June 30, 2018, MSU has already exceeded its overall goal of $1.5 billion and is well positioned to fulfill its commitment in each of the four priority areas originally established. In fiscal year 2017, MSU received commitments of $201 million in gifts and pledges from donors. A required accounting adjustment is made to reflect discounted values of such gifts. Thus, gifts recognized totaled $169 million, including $58 million in additions to permanent endowments. MSU will continue to recognize gift revenue in future years as outstanding commitments are received.



The University's total investments, including endowment investments of $2.5 billion, have grown to $3.1 billion due primarily to gifts and strong investment returns. Over the ten-year period 2008-2017, MSU's endowment investments annual returns have averaged 5.1%, which exceeds the Big Ten average ten-year investment rate of return. This level of performance allows MSU to direct critical resources to mission-driven initiatives. It is important to effectively utilize our donor funds in order to provide value and recognition to both the recipient and the donor.





Spartans Will. Build a Stronger Community

As a public research university and the nation's pioneer land-grant, MSU's commitment to building community within and outside the physical boundaries of campus is not only evident in our mission statement, but also in the goodwill that student and alumni Spartans are able to build in their communities and around the world. MSU is proud of the way Spartans give back by contributing time, energy and resources in response to current events that challenge the fabric of our society. Whether working to bring attention to and find lasting solutions to tragedies such as the Flint water crisis, opening and operating a health clinic and venues for the arts in Detroit, creating STEM opportunities for K-12 students and teachers in the Great Lakes Bay Region, helping MSU Extension offices around the State find solutions to agribusiness needs, serving on medical teams to help underprivileged communities, fostering agribusiness opportunities for the people living in areas plagued by chronic drought, or scientific breakthroughs to fight disease around the world, Spartans can and do empower their communities to become beacons of hope and to help those in need.

The following report provides a picture of the financial foundation that has been built over the years, but to see the broader institutional strength of MSU requires a glimpse beyond the numbers. It is the collective will of the Spartan community to challenge ourselves in areas of weakness to be better, while at the same time capitalizing on areas of strength to become the best that has transformed MSU from its humble beginnings into the globally recognized institution that is today. The vision of what MSU can be moves the Spartans of today to continue this trajectory toward greatness and will continue to drive the next generation of Spartans to take the lead in helping make the world a better place for all people.

50,344
total students

12,516
faculty, academic and support staff

70
MSU partner hospitals in Michigan

1,400
employees engaged in international research

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Independent Auditor's Report

To the Board of Trustees
Michigan State University

Report on the Financial Statements

We have audited the accompanying financial statements of Michigan State University (the "University") and its discretely presented component unit as of and for the years ended June 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Michigan State University's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We did not audit the financial statements of Michigan State University Foundation (the "Foundation"), which is the sole discretely presented component unit. Those financial statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Foundation, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, 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. The financial statements of the Foundation were not audited under *Government Auditing Standards*.

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

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

Opinions

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of Michigan State University and its discretely presented component unit as of June 30, 2017 and 2016 and the respective changes in its financial position, and, where applicable, cash flows, for the years then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Trustees
Michigan State University

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 10-20 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, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 26, 2017 on our consideration of the Michigan State University'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 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 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 Michigan State University's internal control over financial reporting and compliance.

Plante & Moran, PLLC

October 26, 2017

Introduction

The following discussion provides an overview of the financial position of Michigan State University (the "University") for the fiscal years ended June 30, 2017 and 2016.

Included is an analysis of the University's Statement of Net Position, which presents the assets, liabilities, and net position of the University, and when applicable, deferred outflows of resources and deferred inflows of resources. All are measured as of the fiscal year end. The Statement of Revenues, Expenses, and Changes in Net Position reflects revenues and expenses recognized during the fiscal year. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles.

The Michigan State University Foundation (the "Foundation") is a legally separate entity that meets the criteria set forth for component units under GASB regulations. The Foundation provides financial support for the objectives, purposes, and programs of the University. Although the University does not control the timing, purpose, or amount of its receipts from the Foundation, the resources (and income thereon) the Foundation holds and invests are solely for the benefit of the University. Because the Foundation's resources are solely for the benefit of the University, the Foundation is considered a component unit of the University and is discretely presented in the University's financial statements. The Foundation is a private organization that reports under Financial Accounting Standards Board (FASB) standards. As such, certain revenue recognition criteria and presentation features are sometimes different from GASB. No modifications have been made to the Foundation financial information included in the University's financial report to account for these differences.

The University's financial statements, related footnote disclosures, and discussion and analysis (which excludes the Foundation), have been prepared by management. The discussion and analysis, which is GASB-required supplemental information, is not audited and should be read in conjunction with the financial statements and footnotes.

Statement of Net Position

The Statement of Net Position includes all assets, deferred outflows of resources, liabilities, and deferred inflows of resources. It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when services are provided and expenses and liabilities are recognized when others provide the services, regardless of when cash is exchanged. Deferred outflows and deferred inflows of resources are recognized through the consumption or acquisition of resources by the University that is applicable to a future reporting period. Assets, deferred outflows of resources, liabilities, and deferred inflows of resources are generally measured using current values. One exception is capital assets, which are stated at historical cost less an allowance for depreciation rather than current market values.

A summarized comparison of the University's assets, deferred outflows of resources, liabilities, and net position at June 30, 2017, 2016, and 2015 follows (the University has no deferred inflows of resources):

	2017	2016	2015
		(in millions)	
Current assets	$ 542	$ 534	$ 534
Noncurrent assets:			
Restricted cash and cash equivalents and restricted investments	-	62	207
Endowment and other investments	2,792	2,441	2,483
Capital assets, net	2,614	2,365	2,107
Other	136	108	81
Total assets	6,084	5,510	5,412
Deferred outflows of resources	55	74	62
Current liabilities	586	533	559
Noncurrent liabilities	1,621	1,601	1,536
Total liabilities	2,207	2,134	2,095
Net position	$ 3,932	$ 3,450	$ 3,379

Current assets:

Current assets consist of cash and cash equivalents, investments, net accounts and interest receivable, and other assets. During 2017, net accounts receivable increased $27 million due in part to an increase of $23 million from federal, state, and local sponsored programs. Sponsored program accounts receivable balances generally reflect timing differences between amounts expended in accordance with grant or contract guidelines and actual cash draws from the grantor. In addition, inventory and other assets increased $4 million. Offsetting these increases, was a decrease of $22 million in cash and cash equivalents and investments, which is primarily a function of the University's operating, financing, and investing activities as reported in the Statement of Cash Flows.

During 2016, total current assets remained consistent with 2015 levels. Cash and cash equivalents and investments decreased $7 million (primarily a function of the University's operating, financing, and investing activities as reported in the Statement of Cash Flows), offset by a $7 million increase in pledges receivable.

Noncurrent assets:

Restricted cash and cash equivalents and restricted investments

All balances represent unspent bond proceeds, which are externally restricted for the construction or purchase of capital assets. The decreases in 2017 and 2016 represent the spending of Series 2015A bond proceeds for capital assets consistent with their restricted purpose.

Endowment and other investments

At June 30, 2017 and 2016, the University's endowment investments totaled $2,531 million (an increase of $337 million) and $2,194 million (a decrease of $48 million), respectively. Endowment gifts and University-designated additions to endowment investments totaled $66 million in 2017 and $51 million in 2016. In addition, $16 million in 2017 and 2016 of unspent spending policy distributions were reinvested into the respective endowments, consistent with the underlying endowment agreements. Investments of $30 million in 2017 and $120 million in 2016 were reallocated to designated endowment investments, consistent with the University's Board-approved cash management and investment plan. Partially offsetting these increases was a net draw on accumulated capital gains of $28 million in 2017 and $40 million in 2016 for programmatic and capital initiatives. Realized and unrealized net investment gains within the investment portfolio accounted for a $253 million increase in 2017, while net investment losses resulted in a $195 million decrease in 2016.

Other investments consist primarily of retirement and postemployment benefit reserves, which totaled $94 million and $87 million at June 30, 2017 and 2016, respectively. Also included in other investments was the Liquidity Reserve Pool component of the University's Operating Cash Pool ($104 million in 2017 and $82 million in 2016).

Capital assets

The University continues to implement its long-range plan to modernize and renew its teaching, research and residential life facilities in support of its mission. At June 30, 2017, 2016, and 2015, the University's investments in capital assets were as follows:

	2017	2016	2015
		(in millions)	
Land	$ 44	$ 43	$ 42
Buildings and site improvements	3,042	2,972	2,776
Construction in progress	712	459	316
Software and other intangibles	117	95	95
Equipment and other	853	826	777
Museum collections	14	14	13
Less: accumulated depreciation	(2,168)	(2,044)	(1,912)
	$ 2,614	$ 2,365	$ 2,107

Major additions to buildings and site improvements during 2017 included $18 million for the Engineering Building chiller replacement and room renovations, $14 million for the acquisition of 4000 Collins Road property, $5 million for the acquisition of 600 East Crescent Road property, and $5 million for the Facility for Rare Isotope Beams – 25 Mega Watt Electrical Duct Bank. Major additions to buildings and site improvements during 2016 included $69 million for the Bio Engineering Facility, $19 million for the Facility for Rare Isotope Beams – 25 Mega Watt Electrical Duct Bank, $18 million for Akers Hall Dining and Life Safety renovation, and $16 million for Steam Distribution Tunnel replacement.

Construction in progress reflects multi-year projects which, once completed and placed into service, are generally categorized as buildings and site improvements. The 2017 balance included $210 million for the Facility for Rare Isotope Beams, $118 million for 1855 Place, $78 million for the Grand Rapids Research Facility, $42 million for Breslin Center Facility, $30 million for the Cyclotron Building – Office additions, $29 million for Data Center, and $148 million for the Facility for Rare Isotope Beams specialized equipment fabrication. The 2016 balance included $195 million for the Facility for Rare Isotope Beams, $46 million for 1855 Place, $45 million for the Grand Rapids Research Facility, $21 million for the Cyclotron Building – Office additions, and $91 million for the Facility for Rare Isotope Beams specialized equipment fabrication.

As of June 30, 2017, the University had initiated plans and incurred certain contractual commitments related to the construction and renovation of various facilities. The costs to complete the projects are estimated to be $276 million and are to be funded over multiple years from debt proceeds, capital grants, private gifts, and other University funds.

Deferred outflows of resources:

Deferred outflows of resources consist of accumulated changes in the fair value of hedging derivative instruments and deferred losses on a refunding of debt in fiscal year 2010. Deferred outflows of resources decreased $19 million in 2017 and increased $12 million in 2016, due primarily to the change in the accumulated fair value of the hedging derivative instruments.

Current liabilities:

Current liabilities consist primarily of trade accounts and interest payable, accrued compensation and other personnel costs, unearned revenues, and other liabilities payable within one year or less. The net increase in 2017 was due in part to a $34 million increase in the current portion of long-term debt and other obligations and a $21 million increase in accounts and interest payable, partially offset with a $4 million decrease in the current portion of unearned revenues. The net increase in the current portion of long-term debt and other obligations was due in part to a net increase of outstanding General Revenue Commercial Paper (short-term financing) of $35 million. Trade accounts payable balances vary from year-to-year, due in part to timing of University initiatives and payments of related programmatic and capital costs.

The net decrease in 2016 was due in part to a $42 million decrease in the current portion of long-term debt and other obligations, partially offset with a $12 million increase in trade accounts and interest payable. The net decrease in the current portion of long-term debt and other obligations was due in part to a net reduction of outstanding General Revenue Commercial Paper (short-term financing) of $44 million.

Noncurrent liabilities, primarily debt:

At June 30, 2017, the University had noncurrent debt and other obligations outstanding of $1,040 million compared with $1,066 million at June 30, 2016. This balance was comprised primarily of outstanding General Revenue Bonds of $999 million and $1,025 million in 2017 and 2016, respectively (including $47 million and $50 million in 2017 and 2016, respectively, of related original issue premiums). The decrease was primarily due to scheduled principal debt payments of $26 million on outstanding General Revenue Bonds. The University periodically reviews its debt capacity and related capital asset needs to optimize the use of its long-term resources. The University's outstanding General Revenue debt carries an investment grade credit rating from Moody's and Standard & Poor's of Aa1 and AA+, respectively.

The University faces the continuing challenge of funding its increasing health care and dental benefits costs. This includes the cost of providing postemployment health and dental benefits to eligible retirees (other postemployment benefits, or OPEB) through a closed single employer defined benefit plan administered by the University. For the year ended June 30, 2017, the University estimated the cost (annual expense) of providing OPEB through an actuarial valuation as of January 1, 2016. The actuarial valuation computed an annual required contribution, which represents a level of funding that, if paid on an ongoing basis, is projected to cover current year costs and amortize any unfunded actuarial liabilities over a period of thirty years. The University's total unfunded OPEB obligation in 2017 and 2016 was estimated to be $1,086 million and $1,027 million, respectively, using a discount rate of 7%. Of these amounts, the University has recorded a noncurrent liability of $465 million and $406 million for 2017 and 2016, respectively, representing the net OPEB obligation (the cumulative difference between the annual required contribution less actual retiree health and dental payments made during the respective fiscal years). This increase of $59 million represents the continued amortization (year ten of thirty) of the total unfunded OPEB obligation. See footnote 12 for more information.

Effective for the fiscal year ending June 30, 2018, the University will be adopting GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* which changes the financial reporting requirements for OPEB. GASB 75 no longer allows the unfunded OPEB obligation to be amortized over a thirty-year period as allowed by GASB 45, but will be required to report the full unfunded actuarial liability in its entirety in the financial statements. In addition, GASB 75 changes certain actuarial assumptions previously allowed under current OPEB accounting guidance, including annual updates to estimated liabilities based on current year interest rates. To prepare for these changes, the University conducted an actuarial analysis of its OPEB liabilities under the new GASB 75 standard using fiscal year 2016 information. The analysis computed the total unfunded liability amount at varying interest rates to estimate the potential impacts to the University's OPEB liability and to estimate the sensitivity of the liability to changing interest rates. For the year ending June 30, 2017, the analysis estimated the following recomputed projected unfunded OPEB obligations:

Possible Range of Interest/Discount rates:	2%	4%	6%
GASB 75 – Total projected unfunded OPEB obligation (in millions)	$2,780	$1,916	$1,385

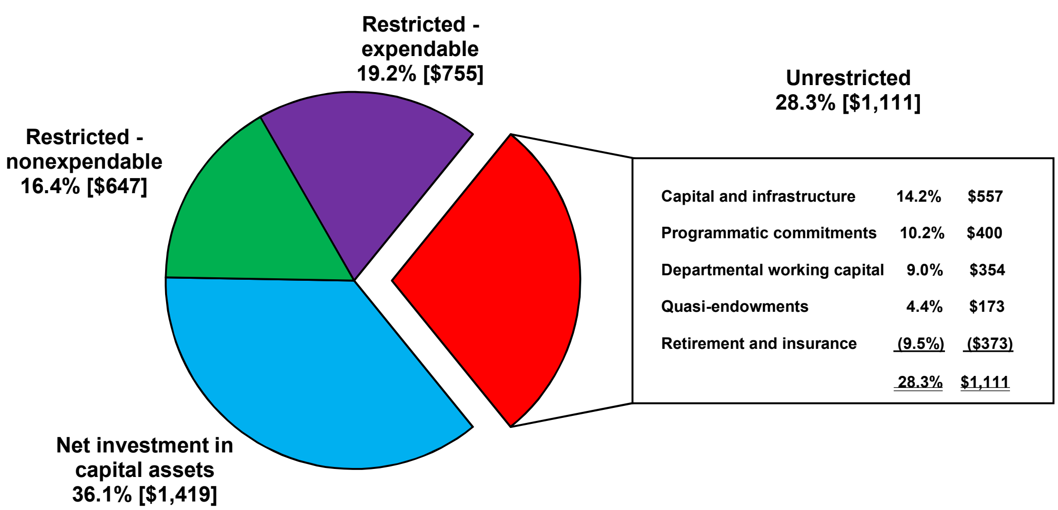
At June 30, 2017 and 2016, the interest rate that would have been used for computing the total unfunded OPEB obligation under GASB 75 would have been 3.78% and 2.85%, respectively. As GASB 75 requires annual updates to estimated liabilities based on current year interest rates, it is likely the liability estimate will vary dramatically from year to year in future reports. Although the financial reporting of the liability will be changing, MSU's approach on funding the retirement benefit on a pay-as-you-go basis will continue. Thus, there will be no impact on the payment of the benefits.

Net position:

Net position represents residual University assets and deferred outflows after liabilities are deducted. The University's net position at June 30, 2017, 2016, and 2015 was as follows:

	2017	2016	2015
		(in millions)	
Net investment in capital assets	$ 1,419	$ 1,227	$ 1,055
Restricted:			
Nonexpendable	647	583	530
Expendable	755	635	691
Total restricted	1,402	1,218	1,221
Unrestricted	1,111	1,005	1,103
Total net position	$ 3,932	$ 3,450	$ 3,379

The following is a breakdown of net position at June 30, 2017. See footnote 15 for further information (amounts are presented in millions of dollars):



TOTAL NET POSITION $3.9 BILLION

Net investment in capital assets represents the University's land, buildings, software, and equipment net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

Restricted nonexpendable net position is subject to externally imposed stipulations that they be maintained permanently. Such net position includes the corpus portion (historical value) of gifts to the University's permanent endowment funds and certain investment earnings stipulated by the donor to be reinvested permanently.

Restricted expendable net position is subject to externally imposed restrictions governing its use. Such net position includes the net appreciation of the University's permanent endowment funds that have not been stipulated by the donor to be reinvested permanently, restricted quasi-endowments, restricted gifts, and federal and state sponsored programs.

Although unrestricted net position is not subject to externally imposed restrictions, virtually all of the University's unrestricted net position is subject to internal designation to meet various specific commitments. These commitments include funding the completion of the 2017 summer semester and the first quarter of fiscal year 2018, maintaining reserves for capital projects, continued recognition of the OPEB obligation, working capital for self-supporting departmental activities, and unrestricted quasi and term endowments.

The University's ongoing review of its infrastructure indicates a need for approximately $950 million over the next 10 years to modernize and renovate aging teaching, research, housing and other support facilities, utility systems, and roads, consistent with its just-in-time maintenance strategy, and to upgrade administrative and other campus-wide technology systems. The University intends to address these maintenance and technology needs through the use of capital and infrastructure reserves, appropriate use of additional borrowing, and efforts to obtain gifts, grants, and capital appropriations.

Statement of Revenues, Expenses, and Changes in Net Position

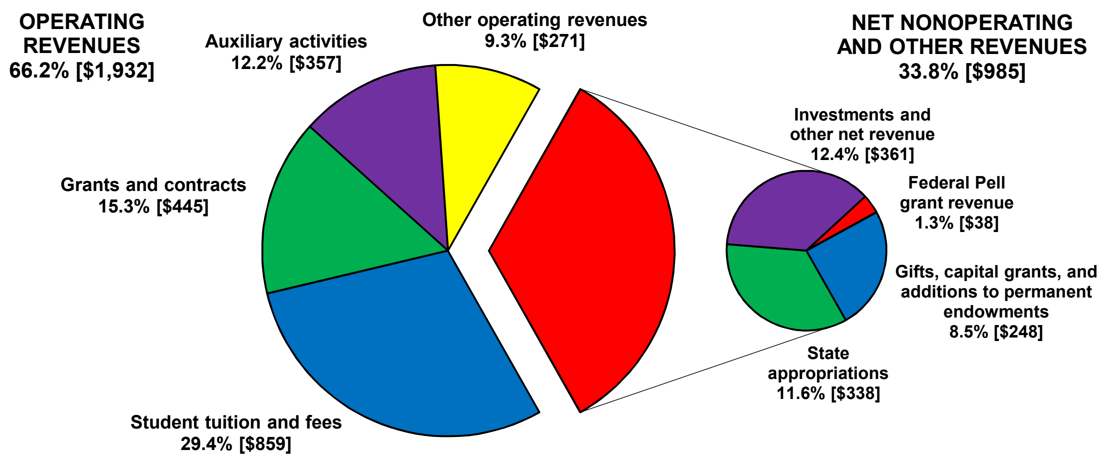
The Statement of Revenues, Expenses, and Changes in Net Position presents the operating results of the University, as well as the nonoperating revenues and expenses. Operating revenues primarily include net student tuition and fees, grants and contracts, and auxiliary activities. Given a public university's dependency on revenues such as state appropriations, gifts, and investment income, which are prescribed by GASB as nonoperating revenues, operating expenses will exceed operating revenues, resulting in an operating loss. Net nonoperating revenues or expenses are an integral component in determining the increase or decrease in net position.

A summarized comparison of the University's revenues, expenses, and changes in net position for the years ended June 30, 2017, 2016, and 2015 follows:

	2017	2016	2015
		(in millions)	
Operating revenues:			
Student tuition and fees, net of allowances	$ 859	$ 830	$ 797
Grants and contracts	445	421	415
Auxiliary activities	357	340	326
Other operating revenues	271	220	204
Total operating revenues	1,932	1,811	1,742
Operating expenses:			
Instruction and departmental research	762	706	669
Research	381	350	328
Public service	287	244	227
Academic support	131	128	105
Student services	51	54	52
Scholarships and fellowships	67	66	63
Institutional support	143	140	128
Operation and maintenance of plant	130	134	129
Auxiliary enterprises	321	318	307
Depreciation	154	147	155
Other operating expenses, net	8	4	4
Total operating expenses	2,435	2,291	2,167
Operating loss	(503)	(480)	(425)
Nonoperating revenues (expenses):			
State operating appropriation	276	269	264
State AgBioResearch appropriation	33	33	32
State Extension appropriation	29	28	28
Federal Pell grant revenue	38	39	38
Gifts	68	60	73
Net investment income (loss)	391	(103)	93
Interest expense on capital asset related debt	(38)	(44)	(37)
Other nonoperating revenues, net	8	4	1
Net nonoperating revenues	805	286	492
Income (loss) before other	302	(194)	67
State capital appropriations	-	44	48
Capital grants and gifts	122	176	54
Additions to permanent endowments	58	45	37
Increase in net position	482	71	206
Net position, beginning of year	3,450	3,379	3,173
Net position, end of year	$ 3,932	$ 3,450	$ 3,379

The University is supported by a diverse stream of revenue including student tuition and fees, state appropriations, federal and state sponsored programs, private gifts and grants, and investment income. The University continues to seek revenue from all possible sources consistent with its mission and to manage the financial resources to make quality education affordable to its students.

Total net revenue by source for the year ended June 30, 2017 is presented in millions of dollars:



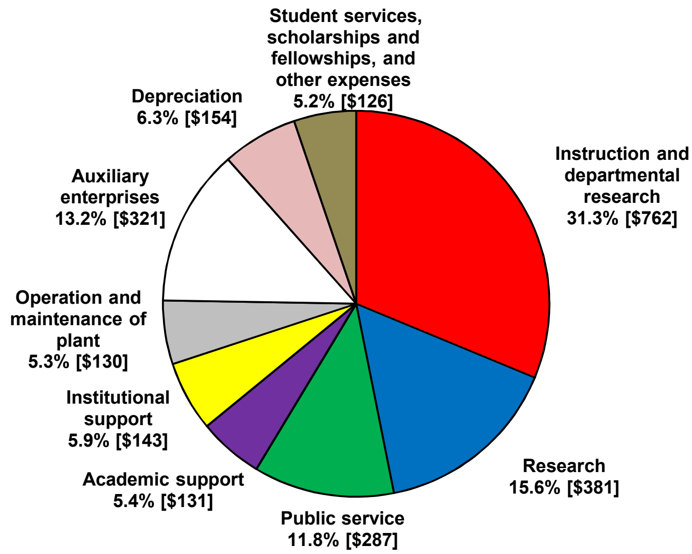
TOTAL REVENUE $2.9 BILLION

Operating revenues: The most significant source of operating revenue for the University was student tuition and fees (net of scholarship allowances), totaling $859 million and $830 million in 2017 and 2016, respectively. Gross tuition and fees revenue increased 3.8% and 4.8% in 2017 and 2016, respectively, due in part to increases in student credit hours and rates, and changes in the student blend. Other major revenue sources in 2017 included federal grants and contracts of $337 million (an increase of $12 million), including $325 million in sponsored programs, and auxiliary activities (activities that provide services to students, faculty, staff, and the public) totaled $357 million (an increase of $17 million). In 2016, net tuition and fees increased $33 million due in part to increases in student credit hours and rates and changes in student blend, and auxiliary activities increased $14 million.

Net nonoperating and other revenues: A primary source of this net revenue was State appropriations, which totaled $338 million in 2017, a decrease of $36 million. In 2017, the University received $276 million in funding for general operations, compared to $269 million in 2016. Michigan State University Extension and MSU AgBioResearch appropriations totaled $62 million, compared to $61 million in 2016. In 2017, the University received no additional State capital appropriations, as all amounts appropriated for the Facility for Rare Isotope Beams and MSU Bio Engineering Facility had been drawn ($44 million in 2016). Other significant components of net nonoperating revenues in 2017 included capital grants and gifts, which decreased $54 million in 2017 due to the completion of certain construction phases related to the Facility for Rare Isotope Beams in 2016 and net investment income that increased $494 million due to market conditions. In 2016, net investment income decreased $196 million and state appropriations increased $2 million.

During 2017, $1,430 million was expended for the core missions of the University: instruction and departmental research, research, and public service, an increase of $130 million (10.0%) over 2016. Instruction and departmental research expenses increased $56 million (7.9%), due in part to general fund salary and labor budget increases from 2016 to 2017 and increased health fringe benefit costs. Research and public service expenses increased $74 million (12.5%), due primarily to growth in certain medical service plan and Medicaid Enhanced Reimbursement program costs within the College of Human Medicine and College of Osteopathic Medicine ($51 million) and in sponsored programs ($7 million). Auxiliary enterprises totaled $321 million, an increase of $3 million. In 2016, expenses for the core mission of the University increased $76 million and auxiliary enterprises increased $11 million.

Operating expenses by source for the year ended June 30, 2017 are presented in millions of dollars:



TOTAL OPERATING EXPENSES $2.4 BILLION

The University's Economic Outlook

In fiscal 2017, MSU continued its efforts to diversify revenue streams beyond student tuition, while enhancing cost containment and efficient operation strategies. Existing appropriations to higher education in the State of Michigan continue to lag national averages. Michigan ranked 45th of 49 reporting states for its 10-year change in higher education State appropriations, and MSU does not anticipate increases to outpace inflation over the near term.

Despite ongoing regional and national economic challenges, MSU continues to thrive in its mission to serve the students of Michigan and the world. With the support of more than 230,000 alumni and friends, MSU has surged past its goal of raising $1.5 billion through the *Empower Extraordinary* capital campaign. With the infusion of private support from Spartans around the world, the University will propel forward in empowering students and faculty at MSU in making the discoveries of tomorrow, remain open and accessible to all who qualify, and build a greater university for generations to come.

Investment income continues to be an important component of MSU's ongoing revenue diversification. As strong stewards of University funds, the University manages its endowment spending rate to ensure necessary resources are available for operations, while maintaining the purchasing power of the endowment assets for decades to come. Over time, MSU's long-term diversified investment strategy has proven to provide an important source of support for University operations and help keep tuition increases lower.

For fiscal 2018, the University budget includes a modest 1.9% projected increase in State appropriations. As a result, the Board of Trustees approved a 2.8% increase in resident lower division undergraduate tuition, while increasing student financial aid by 4.5%.

Beginning in fiscal 2018, MSU launched the *Go Green Go 15* program as part of the University's overall Student Success Initiative. *Go Green Go 15* will encourage students to enroll in at least 15 credit hours each semester and set a pace for a 4-year graduation. In addition to significantly lower total cost of attendance for students that follow this program, research indicates it results in higher levels of academic success, including higher GPAs and faster times-to-degree completion. The goal is to increase University-wide graduation rates to 82% by 2020 and close opportunity gaps for lower-income, first-generation, and underrepresented minority student populations. To support this initiative and encourage new students to seize the momentum, MSU will freeze fiscal 2019 freshman tuition rates at fiscal 2018 levels. Anticipated improvements in student success not only aid the student experience, but will also improve the overall financial health of MSU.

MSU remains one of the top 100 research universities in the world with eight academic programs ranked first in the country and 35 programs ranked in the top 25 nationwide. We continue to embrace our land-grant philosophy: that excellent education should be accessible to all. The University enrolls more Michigan students and more Pell grant recipients than any other university in the State. This is the Spartan Will; the will to make a difference.

STATEMENTS OF NET POSITION

	June 30, 2017	June 30, 2016
ASSETS	(in thousands)	
Current assets:		
Cash and cash equivalents	$ 20,369	$ 10,005
Investments	270,804	303,369
Accounts and interest receivable, net	195,447	168,375
Student loans and pledges receivable, net	32,512	33,187
Inventories and other assets	23,151	19,198
Total current assets	542,283	534,134
Noncurrent assets:		
Restricted cash and cash equivalents	4	11,729
Restricted investments	-	50,591
Endowment investments	2,531,144	2,193,642
Other investments	260,809	247,642
Student loans and pledges receivable, net	100,110	88,009
Investments in joint ventures and other assets	34,614	18,994
Derivative instruments - swap asset	345	584
Capital assets, net	2,614,490	2,364,690
Total noncurrent assets	5,541,516	4,975,881
Total assets	**6,083,799**	**5,510,015**
DEFERRED OUTFLOWS OF RESOURCES	**54,749**	**74,236**
LIABILITIES		
Current liabilities:		
Accounts and interest payable	111,773	91,129
Accrued personnel costs	57,722	54,271
Accrued self-insurance liabilities	15,334	14,609
Payroll taxes and other payroll deductions	27,940	29,467
Deposits held for others	30,244	30,287
Unearned revenues	136,805	141,049
Current portion of long term debt and other obligations	206,283	172,322
Total current liabilities	586,101	533,134
Noncurrent liabilities:		
Accrued personnel costs	37,566	33,061
Accrued self-insurance liabilities	7,609	7,792
Unearned revenues	12,517	14,008
Derivative instruments - swap liability	57,178	73,685
Net other postemployment benefit obligation	465,452	406,383
Long term debt and other obligations	1,040,191	1,066,201
Total noncurrent liabilities	1,620,513	1,601,130
Total liabilities	**2,206,614**	**2,134,264**
NET POSITION		
Net investment in capital assets	1,419,260	1,226,525
Restricted:		
Nonexpendable	647,189	582,740
Expendable	754,587	635,390
Unrestricted	1,110,898	1,005,332
TOTAL NET POSITION	**$ 3,931,934**	**$ 3,449,987**

See accompanying notes

STATEMENTS OF FINANCIAL POSITION

	June 30, 2017	June 30, 2016
	(in thousands)	
ASSETS		
Cash equivalents	$ 10,279	$ 9,533
Interest and dividends receivable	129	114
Grants and contracts receivable, net	43	202
Receivable from related party	1,319	1,867
Other receivables, net	138	26
Investments:		
Marketable securities	215,094	194,272
Investments in limited partnerships	96,079	96,795
Venture capital	74,092	60,814
Cash value of life insurance	3,998	3,745
Land held for investment, net	4,956	4,011
Other investments, net	1,713	1,853
Investment in Research Park, net	5,386	5,877
Notes receivable/equity in start-up organizations, net	858	622
Prepaid expenses	9	56
Property and equipment, net	11,557	8,320
Intangible assets, net	1,016	1,114
Other assets	-	1
TOTAL ASSETS	**$ 426,666**	**$ 389,222**
LIABILITIES AND NET ASSETS		
Liabilities:		
Accrued expenses and other payables	$ 4,546	$ 4,397
Deferred revenue	526	-
Line of credit	1,000	1,000
Trusts and annuities payable	8,730	8,887
Deposit held for Michigan State University	18,866	17,690
Obligations under life estate agreements	754	554
Total liabilities	**34,422**	**32,528**
Net assets:		
Unrestricted	335,471	304,792
Temporarily restricted	39,859	36,252
Permanently restricted	16,914	15,650
Total net assets	**392,244**	**356,694**
TOTAL LIABILITIES AND NET ASSETS	**$ 426,666**	**$ 389,222**

See accompanying notes

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

	Year ended June 30, 2017	2016
	(in thousands)	
OPERATING REVENUES		
Student tuition and fees	$ 988,877	$ 952,448
Less: scholarship allowances	129,760	122,072
Net student tuition and fees	859,117	830,376
State of Michigan grants and contracts	14,166	12,025
Federal grants and contracts	337,022	325,210
Local and private sponsored programs	93,853	83,975
Interest and fees on student loans	956	945
Departmental activities (net of scholarship allowances of $6,622 in 2017 and $5,716 in 2016)	269,901	218,494
Auxiliary activities (net of room and board allowances of $25,513 in 2017 and $25,614 in 2016)	356,538	340,110
TOTAL OPERATING REVENUES	**1,931,553**	**1,811,135**
OPERATING EXPENSES		
Instruction and departmental research	762,112	706,312
Research	380,481	349,725
Public service	286,991	244,511
Academic support	131,448	128,192
Student services	51,190	54,301
Scholarships and fellowships	67,013	65,661
Institutional support	142,707	139,915
Operation and maintenance of plant	129,603	134,246
Auxiliary enterprises	321,039	317,792
Depreciation	154,344	146,540
Other operating expenses, net	8,183	4,107
TOTAL OPERATING EXPENSES	**2,435,111**	**2,291,302**
Operating loss	(503,558)	(480,167)
NONOPERATING REVENUES (EXPENSES)		
State operating appropriation	275,862	268,771
State AgBioResearch appropriation	33,243	32,508
State Extension appropriation	28,673	27,995
Federal Pell grant revenue	37,775	39,151
Gifts	68,413	60,009
Net investment income (loss)	391,106	(102,965)
Interest expense on capital asset related debt	(37,461)	(44,089)
Other nonoperating revenues, net	7,567	4,529
Net nonoperating revenues	805,178	285,909
INCOME (LOSS) BEFORE OTHER	**301,620**	**(194,258)**
State capital appropriations	-	44,089
Capital grants and gifts	122,375	176,222
Additions to permanent endowments	57,952	44,958
Increase in net position	481,947	71,011
Net position, beginning of year	3,449,987	3,378,976
NET POSITION, END OF YEAR	**$ 3,931,934**	**$ 3,449,987**

See accompanying notes

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

	Year ended June 30, 2017			
	Unrestricted Funds	Temporarily Restricted	Permanently Restricted	Total
	(in thousands)			
REVENUE, GAINS AND OTHER SUPPORT:				
Contributions	$ 264	$ 2,339	$ 106	$ 2,709
Income from investments	45,315	3,217	1,708	50,240
Royalty income	1,489			1,489
Rental income	1,987			1,987
Rental expenses	(1,530)			(1,530)
Grants and contracts	974			974
Other income	1,237			1,237
Net assets released from restrictions:				
Satisfaction of program restrictions	290	(288)	(2)	-
Current year transfers	2,209	(1,661)	(548)	-
TOTAL REVENUE, GAINS AND OTHER SUPPORT	52,235	3,607	1,264	57,106
EXPENSES:				
Contributions to Michigan State University	11,538			11,538
Expenses related to land held for investment, net	392			392
Investment management fees	2,829			2,829
Investment consulting fees	569			569
Adjustments to value of annuities payable	(59)			(59)
Management and general	1,757			1,757
Unrelated business income tax	(45)			(45)
Postretirement benefits:				
Net periodic benefit cost	457			457
Changes other than net periodic benefit costs	(479)			(479)
Provision for uncollectible receivables, net	812			812
MBI expenses	1,716			1,716
Spartan Innovations expenses, net	1,848			1,848
UCRP-I expenses	221			221
TOTAL EXPENSES	21,556	-	-	21,556
Change in net assets	30,679	3,607	1,264	35,550
Net assets, beginning of year	304,792	36,252	15,650	356,694
NET ASSETS, END OF YEAR	$ 335,471	$ 39,859	$ 16,914	$ 392,244

	Year ended June 30, 2016			
	Unrestricted Funds	Temporarily Restricted	Permanently Restricted	Total
	(in thousands)			
REVENUE, GAINS AND OTHER SUPPORT:				
Contributions	$ 274	$ 5,446	$ 105	$ 5,825
Income (loss) from investments	(10,687)	(502)	455	(10,734)
Royalty income	1,482			1,482
Rental income	965			965
Rental expenses	(793)			(793)
Grants and contracts	2,204			2,204
Other income	1,273			1,273
Equity earnings from subsidiaries	116			116
Net assets released from restrictions:				
Satisfaction of program restrictions	(238)	248	(10)	-
Current year transfers	3,365	(2,878)	(487)	-
TOTAL REVENUE, GAINS AND OTHER SUPPORT	(2,039)	2,314	63	338
EXPENSES:				
Contributions to Michigan State University	13,360			13,360
Expenses related to land held for investment, net	234			234
Investment management fees	3,566			3,566
Investment consulting fees	565			565
Adjustments to value of annuities payable	(375)			(375)
Management and general	1,740			1,740
Unrelated business income tax	(120)			(120)
Postretirement benefits:				
Net periodic benefit cost	267			267
Provision for uncollectible receivables, net	388			388
MBI expenses	6,248			6,248
Spartan Innovations expenses, net	1,700			1,700
TOTAL EXPENSES	27,573	-	-	27,573
Change in net assets	(29,612)	2,314	63	(27,235)
Net assets, beginning of year	334,404	33,938	15,587	383,929
NET ASSETS, END OF YEAR	$ 304,792	$ 36,252	$ 15,650	$ 356,694

See accompanying notes

STATEMENTS OF CASH FLOWS

	Year ended June 30,	
	2017	2016
Cash flows from operating activities	(in thousands)	
Tuition and fees	$ 856,346	$ 831,482
Research grants and contracts	427,495	421,620
Auxiliary activities	351,249	358,675
Departmental activities	275,682	202,008
Interest and fees on student loans	956	945
Loans issued to students	(5,625)	(8,563)
Collection of loans from students	8,777	10,142
Scholarships and fellowships	(103,667)	(101,857)
Payments to suppliers	(597,993)	(543,193)
Payments to employees	(1,512,395)	(1,434,461)
Other payments	(19,711)	(18,603)
Net cash used by operating activities	(318,886)	(281,805)
Cash flows from noncapital financing activities		
State appropriations	336,232	328,322
Federal Pell grant revenue	37,775	39,151
Gifts	68,668	59,720
Endowment gifts	57,979	44,962
William D. Ford Direct Lending receipts	370,119	369,322
William D. Ford Direct Lending disbursements	(369,631)	(369,340)
Net cash provided by noncapital financing activities	501,142	472,137
Cash flows from capital and related financing activities		
Capital appropriations	-	58,645
Capital gifts and grants	107,515	152,878
Proceeds from issuance of debt and other long term obligations	98,590	20,135
Purchase of capital assets	(383,555)	(391,081)
Proceeds from sale of capital assets	1,381	1,794
Principal paid on capital debt	(88,546)	(84,985)
Interest paid	(49,473)	(46,935)
Other receipts	3,246	2,285
Net cash used by capital and related financing activities	(310,842)	(287,264)
Cash flows from investing activities		
Investment income, net	102,214	127,245
Proceeds from sales and maturities of investments	4,756,392	4,652,229
Purchase of investments	(4,731,381)	(4,876,845)
Net cash provided (used) by investing activities	127,225	(97,371)
Net decrease in cash	(1,361)	(194,303)
Cash and cash equivalents, beginning of year	21,734	216,037
Cash and cash equivalents, end of year	**$ 20,373**	**$ 21,734**

See accompanying notes

	Year ended June 30,	
Reconciliation of net operating loss to cash flows from operating activities:	**2017**	**2016**
	(in thousands)	
Operating loss	$ (503,558)	$ (480,167)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation expense	154,344	146,540
Change in assets and liabilities:		
Accounts receivable	(23,481)	(13,347)
Student loans receivable	3,152	1,579
Inventories and other assets	(3,953)	377
Investments in joint ventures and other assets	(15,620)	(11,817)
Accounts payable	9,968	(1,050)
Accrued personnel costs	7,956	2,569
Payroll taxes and other payroll deductions	(1,527)	1,792
Deposits held for others	(43)	(3,671)
Unearned revenues	(5,735)	18,041
Accrued self-insurance liabilities	542	677
Net other postemployment benefit obligation	59,069	56,672
Net cash used by operating activities	**$ (318,886)**	**$ (281,805)**

See accompanying notes

1. Organization, basis of presentation, reporting entity, and summary of significant accounting policies

Organization:

Michigan State University (the "University") was founded in 1855 as the Agricultural College of the State of Michigan. It was the first institution of higher learning in the nation to teach scientific agriculture and in 1863 became a pioneer land grant college under the Morrill Act. The University has grown into a comprehensive research university providing undergraduate, graduate, and professional degree programs. The University is not a component unit of the State of Michigan as defined by the Governmental Accounting Standards Board (GASB).

Basis of presentation:

The University follows all applicable GASB pronouncements. The accompanying financial statements have been prepared using the economic resource measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America for publicly owned colleges and universities and are presented in accordance with the reporting model prescribed in GASB Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*, and GASB Statement No. 35, *Basic Financial Statements-and Management's Discussion and Analysis-for Public Colleges and Universities*, as amended by GASB Statements No. 37, No. 38, and No. 63. The University follows the "business-type" activities requirements of GASB Statement No. 34. This approach requires the following components of the University's financial statements:

- Management's Discussion and Analysis.
- Basic Financial Statements: Statement of Net Position; Statement of Revenues, Expenses, and Changes in Net Position; Statement of Cash Flows; and Notes to the Financial Statements.

GASB Statement No. 34, as amended by No. 63, establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following four net position categories:

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

  Nonexpendable – Net position subject to externally imposed constraints that they be maintained permanently by the University. Nonexpendable net position includes the corpus portion (historical value) of gifts to the University's permanent endowment funds and certain investment earnings stipulated by the donor to be reinvested permanently.

  Expendable – Net position whose use by the University is subject to externally imposed constraints that can be fulfilled by actions of the University pursuant to those constraints or that expire by the passage of time. Expendable net position includes net appreciation of the University's permanent endowment funds that have not been stipulated by the donor to be reinvested permanently.

- Unrestricted: Net position that is not subject to externally imposed constraints. Unrestricted net position may be designated for specific purposes by action of management or the Board of Trustees (the "Board") or may otherwise be limited by contractual agreements with outside parties. Substantially all unrestricted net position is designated for academic, research, and outreach programs and initiatives, postemployment benefits, and capital asset renewals and replacements.

Reporting entity:

The Michigan State University Foundation (the "Foundation") is a legally separate, tax-exempt entity that meets the criteria set forth for component units under GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, as amended by GASB No. 61. The Foundation provides financial support for the objectives, purposes, and programs of the University. Although the University does not control the timing, purpose, or amount of its receipts from the Foundation, the resources (and income thereon) that the Foundation holds and invests are dedicated to benefit the University. Because the resources held by the Foundation can only be used by, or for the benefit of, the University, the Foundation is considered a component unit of the University and its Statements of Financial Position and Statements of Activities and Changes in Net Assets are discretely presented in the University's financial statements. In addition, the Foundation's significant notes are summarized in Footnote 4.

The Foundation is a private organization that reports under FASB standards. As such, certain revenue recognition criteria and presentation features are different from those under GASB. No modifications have been made to the Foundation financial information included in the University's financial report to account for these differences.

Complete financial statements for the Foundation can be obtained by a written request to:

Michigan State University Foundation, 2727 Alliance Drive, Suite C, Lansing, Michigan 48910-3338

Summary of significant accounting policies:

Cash and cash equivalents – For purposes of the Statement of Cash Flows, the University defines cash equivalents as highly liquid, short-term (90 days or less) investments that bear little or no market risk. Cash and cash equivalents held in the Liquidity Reserve Pool (LRP), Common Investment Fund (CIF), and other investment funds are included in investments because the intent of these funds is long-term appreciation. Any cash balances held in these funds at the date of the financial statements are due to timing of reinvesting the proceeds within the fund.

Restricted cash and cash equivalents and restricted investments – Restricted cash and cash equivalents and restricted investments represent unspent bond proceeds that are externally restricted for the construction or purchase of capital assets.

Pledges – Financial support in the form of pledges is received from business enterprises, foundations and individuals. Revenue from gift pledges is recorded only when there is an unconditional promise to pay and all eligibility requirements, including time requirements, have been met. Contributions to permanent and term endowments are not recognized as assets until actually received.

Inventories – Inventories are recorded using various methods, including last in first out (LIFO) and first in first out (FIFO).

Investments – Investments are stated at fair value, which represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The University values its investments using a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Observable inputs reflect market data obtained from sources independent of the University, while unobservable inputs reflect the University's own assumptions about how market participants would value an asset or a liability based on the best information available. The University uses various industry standard valuation techniques that are appropriate under the circumstances and for which sufficient data is available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

Capital assets – Capital assets are stated at cost or, when donated, at acquisition value at the date of the gift. Depreciation is computed using the straight-line method, with a full-year expense in the year of acquisition and none in the year of disposal. Assets are depreciated over the estimated useful lives ranging from four to forty years for the respective assets. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts. The University capitalizes but does not depreciate certain works of art and historical treasures that are held for exhibition, education, research, or public service. These collections are neither disposed of for financial gain nor encumbered in any way, and are subject to organizational policy that requires the proceeds of items that are sold to be used to acquire other items for collections.

Deferred outflows of resources – As prescribed by GASB Statement No. 63, the Statement of Financial Position reports a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period and so will not be recognized as an expense until then. Deferred outflows of resources consist of accumulated changes in the fair value of hedging derivative instruments and deferred losses on refunding of debt.

Compensated absences – University employees earn vacation and sick leave benefits based, in part, on length of service. Vacation pay is fully vested when earned. Upon separation from service, employees are paid accumulated vacation and sick pay based upon the nature of separation (death, retirement, or termination). Certain limitations have been placed on the hours of vacation and sick leave that employees may accumulate and carry over for payment at death, retirement, or termination. Unused hours exceeding these limitations are forfeited.

Unearned revenue – Unearned revenue consists primarily of advance ticket sales for athletic events, summer school tuition not earned during the current year, and contract and sponsored program advances.

Derivative instruments – Derivative instruments consist of interest rate swap agreements and are stated at fair value based on the zero coupon valuation method.

Operating and Nonoperating Revenues – Operating activities as reported in the Statements of Revenues, Expenses, and Changes in Net Position are those activities that generally result from exchange transactions, such as payments received for providing services and payments made for services or goods received. Nearly all of the University's expenses are from exchange transactions. Certain significant revenue streams relied upon for operations are recorded as nonoperating revenues, as defined by GASB Statement No. 34, including state appropriations, federal Pell grant revenue, gifts, and investment income. Restricted and unrestricted resources are spent and tracked at the discretion of the recipient University department within the guidelines of donor restrictions, if any.

Student tuition and fees – Student tuition and fee revenues are reported in the fiscal year in which the substantial portion of the educational term occurs, net of scholarship allowances in the Statements of Revenues, Expenses, and Changes in Net Position. Scholarship allowances represent the difference between the stated charge for goods and services provided by the University and the amount that is paid by the students or third parties on behalf of the students, where the University has discretion over such expenses.

Auxiliary activities – Auxiliary activities primarily represent revenues generated from University Residential and Hospitality Services, Intercollegiate Athletics, and various other departmental activities that provide services to the student body, faculty, staff, and general public.

Donor restricted endowments – Under Michigan law set forth in the Uniform Prudent Management of Institutional Funds Act, as adopted in Michigan in 2009 ("UPMIFA"), the Board acts in a fiduciary capacity as trustee of its endowment funds. UPMIFA requires that the Board exercise its fiduciary duties prudently and consider both the charitable purposes and needs of the University and the purposes of the specific endowment regarding current expenditures and preservation of the purchasing power of the funds. Under the programmatic spending policy established by the Board, 4.8% of the average market value of endowment investments for the twenty quarters of the five calendar years prior to the beginning of the fiscal year was authorized for expenditure for fiscal year 2017. For fiscal year 2018, 4.6% of the average market value of endowment investments for the twenty quarters of the five fiscal years prior to the beginning of the fiscal year was authorized for expenditure.

Eliminations – In preparing the financial statements, the University eliminates inter-fund assets and liabilities that would otherwise be reflected twice in the Statements of Net Position. Similarly, revenues and expenses related to internal service activities are also eliminated from the Statement of Revenues, Expenses, and Changes in Net Position. Student tuition and fees are presented net of scholarships and fellowships applied to student accounts where the University has discretion over such expenses, while stipends and other payments made directly to students are presented as scholarship and fellowship expenses.

Use of estimates – The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

Income taxes – The University is a part of the State of Michigan for purposes of Internal Revenue Code Section 115, and is an organization as described in Internal Revenue Code Section 501(c)(3). The University's income generally is exempt from federal income taxes, although income from certain activities may be subject to taxation as unrelated business income.

2. Cash and cash equivalents

The University's cash and cash equivalents as of June 30, 2017 and 2016 were as follows:

	2017	2016
Cash and cash equivalents, current	$ 20,369	$ 10,005
Restricted cash and cash equivalents, noncurrent	4	11,729
Total cash and cash equivalents	$ 20,373	$ 21,734

Of the bank balances for cash, $832 of the total $50,577 in 2017 and $525 of the total $36,580 in 2016 were covered by federal depository insurance. Any remaining amounts were uninsured and uncollateralized, as banks holding deposits of the University are legally prohibited from collateralizing these deposits.

3. Investments

The University manages investments in accordance with the policy approved by the Board. The investment policy distinguishes guidelines for the Liquidity Pool (LP), Liquidity Reserve Pool (LRP), and Common Investment Fund (CIF). In addition, the University has other investments that are restricted by external agreements or by special donor limitations (Other).

As of June 30, 2017 and 2016, the University had the following investments:

	June 30, 2017				
Investment type	LP	LRP	CIF	Other	Total
Investment pools	$ 12,781	$ 43,080	$ 2,214,359	$ 61,541	$ 2,331,761
U.S. Treasury bonds	120,648	19,405	25,216	-	165,269
U.S. Government agencies	22,126	13,416	17,436	-	52,978
Municipal bonds	-	381	496	-	877
Corporate bonds	49,783	11,914	15,483	625	77,805
Asset-backed securities	41,041	11,860	15,413	2,299	70,613
U.S. equities	-	-	273,783	-	273,783
International equities	-	-	57,005	-	57,005
International bonds	24,425	3,584	4,657	-	32,666
Total	$ 270,804	$ 103,640	$ 2,623,848	$ 64,465	$ 3,062,757

	June 30, 2016				
Investment type	LP	LRP	CIF	Other	Total
Investment pools	$ 11,280	$ 30,457	$ 1,949,409	$ 64,098	$ 2,055,244
U.S. Treasury bonds	139,433	16,270	24,721	-	180,424
U.S. Government agencies	36,666	12,678	19,264	-	68,608
Municipal bonds	-	535	813	-	1,348
Corporate bonds	70,043	10,461	15,897	675	97,076
Asset-backed securities	65,464	9,148	13,902	2,325	90,839
U.S. equities	-	-	213,478	-	213,478
International equities	-	-	50,665	-	50,665
International bonds	31,074	2,575	3,913	-	37,562
Total	$ 353,960	$ 82,124	$ 2,292,062	$ 67,098	$ 2,795,244

Interest Rate Risk: As a means of managing its exposure to fair value losses arising from increasing interest rates, University investment policy limits the average duration of the LP portfolio to three years and the LRP and CIF portfolios to six years. At June 30, 2017 and 2016, the University was in compliance with its investment policy with regard to average duration. University policy does not address average duration of investments by investment type.

The maturities of fixed income investments as of June 30, 2017 and 2016 were as follows:

June 30, 2017
Fixed Income Investment Maturities

Investment type	Less than 1 year	1-5 years	6-10 years	More than 10 years	Total
Investment pools	$ -	$ -	$ 79,975	$ 2,170	$ 82,145
U.S. Treasury bonds	422	148,948	9,329	6,570	165,269
U.S. Government agencies	167	16,148	822	35,841	52,978
Municipal bonds	-	-	-	877	877
Corporate bonds	8,702	46,907	14,688	7,508	77,805
International bonds	2,343	25,217	4,064	1,042	32,666
Asset-backed securities	365	18,579	20,298	31,371	70,613
Total	$ 11,999	$ 255,799	$ 129,176	$ 85,379	$ 482,353

June 30, 2016
Fixed Income Investment Maturities

Investment type	Less than 1 year	1-5 years	6-10 years	More than 10 years	Total
Investment pools	$ -	$ -	$ 64,750	$ 2,384	$ 67,134
U.S. Treasury bonds	13,509	158,536	3,545	4,834	180,424
U.S. Government agencies	5,512	29,665	778	32,653	68,608
Municipal bonds	-	-	-	1,348	1,348
Corporate bonds	30,778	46,766	11,935	7,597	97,076
International bonds	11,932	21,845	2,854	931	37,562
Asset-backed securities	11,488	38,646	10,153	30,552	90,839
Total	$ 73,219	$ 295,458	$ 94,015	$ 80,299	$ 542,991

The University invests in asset-backed securities such as mortgage pass-through securities issued by U.S. Government agencies. These securities are based on cash flows from interest payments on underlying mortgages. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates.

Credit Risk: As a means of managing credit risk on its fixed income investments, University investment policy limits investments at time of purchase to the following minimum ratings issued by nationally recognized statistical rating organizations: LP portfolio – short-term A1/P1, long-term BBB; LRP portfolio – short-term A2/P2, long-term B; CIF portfolio – short-term A2/P2, long-term BB. Thereafter, the minimum quality for separately managed funds in all three portfolios is limited to AA. University policy does not address credit risk by investment type.

The Standard & Poor's credit ratings for fixed income investments at June 30, 2017 and 2016 were as follows:

	June 30, 2017							
Rating	Investment pools	U.S. Treasury bonds	U.S. Government agencies	Municipal bonds	Corporate bonds	International bonds	Asset-backed securities	Total
AAA	$ -	$ -	$ -	$ -	$ 841	$ -	$ 27,698	$ 28,539
AA	-	-	15,612	714	3,976	8,290	4,313	32,905
A	-	-	-	163	17,674	12,503	4,304	34,644
BBB	-	-	-	-	52,856	10,715	846	64,417
BB	-	-	-	-	269	247	-	516
Below BB	-	-	-	-	-	-	-	-
Not rated	82,145	165,269	37,366	-	2,189	911	33,452	321,332
Total	$ 82,145	$ 165,269	$ 52,978	$ 877	$ 77,805	$ 32,666	$ 70,613	$ 482,353

	June 30, 2016							
Rating	Investment pools	U.S. Treasury bonds	U.S. Government agencies	Municipal bonds	Corporate bonds	International bonds	Asset-backed securities	Total
AAA	$ -	$ -	$ -	$ -	$ 5,068	$ 2,015	$ 27,876	$ 34,959
AA	-	-	34,674	923	9,796	5,375	27,711	78,479
A	-	-	-	425	34,006	17,146	555	52,132
BBB	-	-	-	-	46,140	9,185	2,020	57,345
BB	-	-	-	-	165	-	-	165
Below BB	-	-	-	-	-	-	-	-
Not rated	67,134	180,424	33,934	-	1,901	3,841	32,677	319,911
Total	$ 67,134	$ 180,424	$ 68,608	$ 1,348	$ 97,076	$ 37,562	$ 90,839	$ 542,991

Concentration of Credit Risk: As a means of managing the concentration of credit risk, University investment policy limits the concentration of investments as follows: LP portfolio – No more than 15% of the portfolio's market value may be invested in dollar denominated foreign securities of developed countries (i.e., no emerging markets). No more than 10% of the portfolio's market value will be invested in securities of any single issuer, except those which are obligations of, or fully guaranteed as to both principal and interest by, the U.S. Government or its agencies. LRP portfolio – No more than 10% of the portfolio's market value may be invested in securities below BBB. No more than 10% of the portfolio's market value may be invested in securities of any single issuer, except those which are obligations of, or fully guaranteed as to both principal and interest by, the U.S. Government or its agencies. CIF portfolio – Investments are managed in accordance with asset allocation guidelines and manager guidelines established at the time of manager appointment and consist of equities, real assets, limited partnerships, absolute return funds, and fixed income assets.

As of June 30, 2017 and 2016, not more than 5% of the University's total investments were invested in any one issuer except those which are obligations of, or fully guaranteed as to both principal and interest by, the U.S. Government or its agencies.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. University investment policy does not limit the value of investments that may be held by an outside party. Of the University's investments at June 30, 2017, $165,269 of the U.S. Treasury bonds, $52,978 of the U.S. Government agencies, $877 of the municipal bonds, $77,805 of the corporate bonds, $32,666 of the international bonds, $70,613 of the asset-backed securities, $273,748 of the U.S. equities, $57,005 of the international equities, and $28,913 of the external investment pools are held by the University's counterparty, not in the name of the University. Of the University's investments at June 30, 2016, $180,424 of the U.S. Treasury bonds, $68,608 of the U.S. Government agencies, $1,348 of the municipal bonds, $97,076 of the corporate bonds, $37,562 of the international bonds, $90,839 of the asset-backed securities, $213,128 of the U.S. equities, $50,665 of the international equities, and $24,447 of the external investment pools are held by the University's counterparty, not in the name of the University.

Foreign Currency Risk: University investment policy limits foreign currency risk on its LRP portfolio to 30% of the portfolio's market value.

4. Foundation Investments

The Foundation records investments at fair value. It utilizes valuation techniques that maximize the use of observable inputs and minimizes the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques the Foundation is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets carried at fair value will be classified and disclosed in one of the following three categories:

Level 1: Quoted prices for identical assets or liabilities in active markets that the Foundation has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets and liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Foundation's estimated fair values of investments measured on a recurring basis as of June 30, 2017 and 2016 were as follows:

	Fair value measurement at June 30, 2017 using:			
	Balance at June 30, 2017	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Marketable securities:				
Short-term investments	$ 2,625	$ 2,625	$ -	$ -
Domestic equities	62,582	46,232	16,350	-
Foreign equities	97,758	59,485	38,273	-
Fixed income	11,729	11,729	-	-
Mutual funds - equities	27,147	27,147	-	-
Mutual funds - fixed income	13,253	13,253	-	-
Total marketable securities	215,094	160,471	54,623	-
Investments in limited partnerships	75,225	-	-	75,225
Other investments	1,145	48	1,097	-
Total investments by fair value level	$ 291,464	$ 160,519	$ 55,720	$ 75,225

At June 30, 2017, $20,854 of investments in limited partnerships and $74,092 of venture capital was valued at net asset value and not included above. In addition, $568 of other investments are not recorded at fair value.

	Fair value measurement at June 30, 2016 using:			
	Balance at June 30, 2016	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Marketable securities:				
Short-term investments	$ 2,136	$ 2,136	$ -	$ -
Domestic equities	56,006	42,279	13,727	-
Foreign equities	81,403	50,089	31,314	-
Fixed income	16,400	16,400	-	-
Mutual funds - equities	24,742	24,742	-	-
Mutual funds - fixed income	13,585	13,585	-	-
Total marketable securities	194,272	149,231	45,041	-
Investments in limited partnerships	72,584	-	-	72,584
Other investments	1,135	18	1,117	-
Total investments by fair value level	$ 267,991	$ 149,249	$ 46,158	$ 72,584

At June 30, 2016, $24,211 of investments in limited partnerships and $60,814 of venture capital was valued at net asset value and not included above. In addition, $718 of other investments are not recorded at fair value.

The fair value for marketable debt and equity securities are based on quoted market prices. Securities traded on the national securities exchange are valued at the reported sales price on the last business day of the year. Investments traded over the counter on the over-the-counter market and listed securities for which no sale was reported on that date are valued at the average of the last reported bid and ask price.

The Foundation has entered into various limited partnerships and managed accounts with investment managers. These investments are secured by the underlying value of the securities composing the portfolios. The carrying amount reported is stated at market value or estimated market value. Although limited partnership investments have been classified as Level 3, within certain individual funds there may be certain assets or liabilities that are classified as Level 1 or 2 by limited partnerships.

Venture capital investments are stated at market value or estimated market value. Management, external consultants, and the Board of Directors evaluate these investments for impairment on a quarterly basis. As of June 30, 2017, the Foundation has an outstanding commitment to fund limited partnerships and venture capital investments in the amount of $60,728.

5. Accounts and interest receivable

The composition of accounts and interest receivable at June 30, 2017 and 2016 is summarized as follows:

	2017	2016
State appropriations	$ 61,414	$ 59,868
Research and sponsored programs	77,997	54,944
Departmental activities	45,173	44,469
Interest receivable	1,578	1,533
Other	22,360	22,573
	208,522	183,387
Less: allowance for doubtful accounts	13,075	15,012
Total accounts and interest receivable, net	$ 195,447	$ 168,375

6. Student loans and pledges receivable

The composition of student loans and pledges receivable at June 30, 2017 and 2016 is summarized as follows:

	2017	2016
Student loans receivable:		
Perkins Federal Loan Program	$ 34,643	$ 37,723
Health Professions Student Loan Programs	9,433	9,378
Other	3,144	3,355
	47,220	50,456
Less: allowance for doubtful accounts	7,260	7,344
Total student loans receivable, net	39,960	43,112
Pledges receivable:		
Capital	71,252	54,655
Operations	32,766	33,102
	104,018	87,757
Less: allowance for doubtful accounts	11,356	9,673
Total pledges receivable, net	92,662	78,084
Total student loans and pledges receivable, net	132,622	121,196
Less current portion - student loans	9,515	9,456
Less current portion - pledges	22,997	23,731
Noncurrent portion	$ 100,110	$ 88,009

Principal repayment and interest rate terms of federal and University student loans vary considerably. Campus-based federal loan programs are funded principally with federal and institutional contributions to the University under the Perkins and various health professions loan programs.

Subsequent to year end, the Perkins loan program expired on September 30, 2017, which ended the issuance of new loans under this program. Pending additional information from the Federal government, the University will continue to service all outstanding loans in accordance with program specifications.

For the year ended June 30, 2017 and 2016, the University distributed $369,630 and $368,039, respectively, for student loans through the U.S. Department of Education William D. Ford Direct Loan Program. These distributions and related funding sources are not included as expenses and revenues in the accompanying financial statements.

As discussed in Note 1, pledges for permanent endowments do not meet eligibility requirements, as defined by GASB Statement No. 33, until the related gift is received. Accordingly, pledges for permanent endowments totaling $35,626 and $34,504 at June 30, 2017 and 2016, respectively, are not recognized as assets in the accompanying financial statements, but are expected to be received in future years.

Payments on pledges receivable at June 30, 2017, expected to be received in the following fiscal years ended June 30, are summarized below. The allowance for uncollectible pledges receivable is made based on prior collection experience and management judgment. Gift pledges expected to be collected in the future years are reported at the net present value of the related cash flows discounted at 4%.

2018	$ 25,850
2019	26,130
2020	23,015
2021	14,365
2022	6,422
2023 and beyond	8,236
Total discounted pledges receivable	104,018
Less: allowance for uncollectible pledges	11,356
Total pledges receivable, net	$ 92,662

7. Investments in joint ventures and other assets

The composition of investment in joint ventures and other assets at June 30, 2017 and 2016 is summarized as follows:

	2017	2016
Investment in joint ventures	$ 10,555	$ 7,584
Other assets	24,059	11,410
Total investment in joint ventures and other assets	$ 34,614	$ 18,994

The University is a member of three separate incorporated nonprofit joint ventures, most of which are accounted for under the equity method. The University and Sparrow Health System are members of Mid-Michigan MRI, Inc., which provides high technology cross-sectional diagnostic imaging services. University Rehabilitation Alliance, Inc. (URA) has the University and Peckham Vocational Industries of Lansing as members and is an enterprise for the treatment of persons with brain injury. Alliance Corporation is an enterprise formed with Spectrum Health System to support and direct the collaboration of physicians and researchers to enhance patient treatments and increase the investigation of leading-edge medical research. The University is a 50% member in each of the foregoing nonprofit corporations. Copies of financial statements for these entities can be obtained by a written request to: Office of the Controller, Michigan State University, 426 Auditorium Rd., John A. Hannah Administration Building Room 305, East Lansing, Michigan 48824-1046.

Since its inception, the University has extended various lines of credit to URA for capital and operational needs. At June 30, 2017 and 2016, the University had a note receivable balance of $2,028 and $2,088, respectively. This receivable is due in equal monthly installments by March 2036 at a rate of 5.5% and is secured by the land, property, and equipment of URA. In addition, in June 2017 the Board of Trustees authorized an additional line of credit of $1,000 to be used by URA for capital and operational needs. As of June 30, 2017, no amounts had been drawn on this line of credit.

In June 2017, the Board of Trustees authorized the dissolution of the University's interest in Mid-Michigan MRI, Inc., which totaled $5,878 at June 30, 2017. Subsequent to year end, the University has received an initial net distribution of $4,000. Finalization of the dissolution is expected to be completed during fiscal year 2018.

Other assets is comprised of a $23,000 deposit made related to a facilities agreement with Consumers Energy and $1,060 of assets originally granted to the University under the Morrill Act as a pioneer land-grant college. The Consumers agreement called for the University to fund an initial deposit of $23,000 to Consumers Energy that was used for the construction of a 138kV electrical substation to provide energy to the University. The facility will be owned and operated by Consumers Energy. Once placed in service, the University will be entitled to an annual utility expense rebate from Consumers Energy, based in part on annual energy consumption for a period of up to 25 years, or up to an accumulated rebate total of $23,000. Any portion of the initial deposit not applied to future energy expenses through the annual rebate amount within the 25 year period will be forfeited.

8. Capital assets and collections

Capital asset and collection activity for the years ended June 30, 2017 and 2016 follows:

	2016	Additions	Disposals	Transfers	2017
Non-depreciated capital assets:					
Land	$ 42,788	$ 861	$ -	$ -	$ 43,649
Construction in progress	459,017	326,662	-	(73,515)	712,164
Museum collections	13,483	1,525	(17)	(330)	14,661
Total non-depreciated capital assets	515,288	329,048	(17)	(73,845)	770,474
Depreciated capital assets:					
Buildings and site improvements	2,971,885	19,407	(826)	52,015	3,042,481
Software and other intangibles	95,611	-	-	21,500	117,111
Equipment and other	826,243	57,329	(31,132)	330	852,770
Less: accumulated depreciation					
Buildings and site improvements	(1,312,117)	(96,566)	478	-	(1,408,205)
Software and other intangibles	(94,234)	(5,185)	-	-	(99,419)
Equipment and other	(637,986)	(52,593)	29,857	-	(660,722)
Total depreciated capital assets	1,849,402	(77,608)	(1,623)	73,845	1,844,016
Total capital assets	$ 2,364,690	$ 251,440	$ (1,640)	$ -	$ 2,614,490

	2015	Additions	Disposals	Transfers	2016
Non-depreciated capital assets:					
Land	$ 41,479	$ 1,399	$ (90)	$ -	$ 42,788
Construction in progress	316,226	341,948	-	(199,157)	459,017
Museum collections	13,329	159	-	(5)	13,483
Total non-depreciated capital assets	371,034	343,506	(90)	(199,162)	515,288
Depreciated capital assets:					
Buildings and site improvements	2,775,681	-	(2,953)	199,157	2,971,885
Software and other intangibles	95,611	-	-	-	95,611
Equipment and other	777,039	62,673	(13,474)	5	826,243
Less: accumulated depreciation					
Buildings and site improvements	(1,219,787)	(94,441)	2,111	-	(1,312,117)
Software and other intangibles	(92,564)	(1,670)	-	-	(94,234)
Equipment and other	(600,303)	(50,429)	12,746	-	(637,986)
Total depreciated capital assets	1,735,677	(83,867)	(1,570)	199,162	1,849,402
Total capital assets	$ 2,106,711	$ 259,639	$ (1,660)	$ -	$ 2,364,690

9. Deferred outflows of resources

The composition of deferred outflows of resources at June 30, 2017 and 2016 is summarized as follows:

	2017	2016
Accumulated changes in fair value of hedging derivative instruments	$ 43,656	$ 62,009
Loss on refunding of debt at June 30, 2010	11,093	12,227
Total deferred outflows of resources	$ 54,749	$ 74,236

10. Contingencies and risk management

The University is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The University complies with the requirements of GASB Statement No. 10, and related guidance, and records liabilities for legal proceedings and other contingent losses in those instances where the liability is deemed probable and the University can reasonably estimate the amount of the loss (or a range of the loss can be estimated). Once established, accruals are adjusted from time to time, as appropriate, to reflect (1) the facts and circumstances known at the time, including information regarding negotiations, settlements, rulings and other relevant events and developments, (2) the advice and analyses of counsel and (3) the assumptions and judgment of management. To manage these risks, the University uses various lines of commercial insurance purchased on an annual basis (including, but not limited to, general liability insurance, educators legal liability insurance, excess medical professional liability insurance, and property insurance) with differing self-insured retentions. The University evaluates self-insured retention amounts annually, and establishes retention amounts based on various factors, including historical claims experience.

The University's liability for various medical professional liability claims is funded based on actuarial valuations. The liability is reported at its present value of $5,813 and $5,647 as of June 30, 2017 and 2016, respectively. The discount rate used was 2%, which is based on industry standards.

The University is also self-insured for various employee benefits that include health care and dental insurance, workers compensation, and unemployment compensation. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Those losses include an estimate of claims that have been incurred but not reported. The workers compensation liability, which will be settled by fixed payments over an extended period of time, is reported at its present value of $3,768 and $3,680 as of June 30, 2017 and 2016, respectively. The discount rate used was 4%, which is based in part on the University's internal cost of capital.

Changes in the total reported general, professional, and self-insured employee benefit liabilities during 2017, 2016, and 2015 were as follows:

	2017	2016	2015
Balance, beginning of year	$ 22,401	$ 21,724	$ 21,112
Claims incurred and changes in estimates	192,687	168,723	158,630
Claim payments	(192,145)	(168,046)	(158,018)
Balance, end of year	22,943	22,401	21,724
Less: current portion	15,334	14,609	14,096
Noncurrent portion	$ 7,609	$ 7,792	$ 7,628

For those risks that the University has purchased commercial insurance, settled claims have not exceeded the commercial coverage in any of the past three years.

In August 2016, a criminal complaint was filed with the University Police Department against a physician then employed by the University. This and subsequent allegations were made by individuals who accused the physician of sexual assault based, in large part, on conduct that occurred under the guise of medical treatment, including on University non-campus property. The University terminated the employee from his position on September 20, 2016. The former employee is currently facing criminal charges. Civil actions relating to these allegations have been filed by 145 individuals against the former employee, naming the University and, in some cases, several other current and former employees, as co-defendants. It is possible that additional individuals may file similar civil actions. The outcome of the pending and potential litigation is unknown at June 30, 2017, and, therefore, no accruals for future costs have been recorded in the 2017 financial statements.

In the normal course of its activities, the University has been a party in various other legal actions. Historically, the University has not experienced material losses from such actions. After taking into consideration legal counsel's evaluation of other pending actions, the University is of the opinion that the outcome thereof will not have a material effect on the financial statements.

11. Retirement benefits

The University has a defined contribution base retirement program administered through TIAA and Fidelity Investments for all qualified employees. All regular employees are eligible to participate based on the service requirements specific to their employee group. Participants maintain individual accounts with the base retirement vendors and are fully vested.

Participating employees contribute 5% of their base salary or wages and the University contributes 10% of the employee's base salary or wages, subject to applicable University guidelines and Internal Revenue Service limits. In addition, for certain employees hired after June 30, 2010, and who are not eligible to receive postemployment benefits upon retirement, the University contributes an additional 0.5% or 0.75% (depending on total years of service) of the employee's base salary or wages, subject to applicable limits. Participants may elect to contribute additional amounts to a supplemental program and/or a deferred compensation plan, within specified limits, which are not matched by University contributions. Plan provisions and contribution requirements of plan members and the University are established and may be amended in accordance with University policies, union contracts, or plan provisions. Contributions under the base program, excluding the participants' supplemental contributions, for the years ended June 30, 2017 and 2016 were as follows:

	2017	2016
University contributions	$ 85,160	$ 81,567
Employee contributions	42,195	40,099

In addition, the University has a single-employer, defined benefit plan covering 338 employees hired prior to January 1, 1973. The plan is closed to new entrants and monies have been internally reserved by the University to fully fund program costs. The plan is not funded through a pension trust. For fiscal year ending June 30, 2017, the University adopted GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Accordingly, the University has recorded a liability of $4,443 representing the total remaining pension obligation based on an actuarial valuation as of January 1, 2017. The benefits are based on the employee's compensation during the last three years of employment and/or years of service.

12. Other postemployment benefits (OPEB)

Plan Description: The University provides retiree health and dental care benefits, including prescription drug coverage, to eligible retired employees and qualified spouses/beneficiaries. This is a closed single employer defined benefit plan administered by the University effective for employees hired prior to July 1, 2010. Benefits are provided to eligible faculty, academic staff and support staff who meet normal retirement requirements while still working for the University. Currently, the plan has approximately 14,000 members. The plan does not issue a separate stand-alone financial statement.

Funding Policy: The University's medical plans are self-funded and each plan's premiums are updated annually based on actual claims. The University contributes to the lowest cost health plan's single rate cost for which retirees are eligible. No payment is required by retirees who select the lowest cost health plan for coverage. In the event a retiree selects an alternative health plan, the retiree is responsible for payment of the difference in premium costs. Retirees are responsible for various co-payments. The University funds OPEB on a pay-as-you-go basis, and there is no obligation to make contributions in advance of when the insurance premiums or claims are due for payment.

Funding Progress: For the year ended June 30, 2017, the University has estimated the cost (annual expense) of providing retiree health and dental care benefits through an actuarial valuation as of January 1, 2016. In accordance with GASB Statement No. 45, the valuation computes an annual required contribution, which represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years. This valuation's computed contribution and actual funding are summarized as follows:

	2017	2016	2015
Annual required contribution	$ 95,417	$ 90,165	$ 74,039
Interest on the prior year's net OPEB obligation	28,258	24,480	20,975
Less: adjustment to the annual required contribution	(26,038)	(21,808)	(18,102)
Annual OPEB cost	97,637	92,837	76,912
Amounts contributed:			
Payments of current premiums and claims	(38,568)	(36,165)	(33,704)
Increase in net OPEB obligation	59,069	56,672	43,208
OPEB obligation - beginning of year	406,383	349,711	306,503
OPEB obligation - end of year	$ 465,452	$ 406,383	$ 349,711

The annual OPEB cost, the percentage contributed to the plan, and the net OPEB obligation for the current and two preceding years were as follows:

	Fiscal year ended June 30,		
	2017	2016	2015
Annual OPEB cost	$ 97,637	$ 92,837	$ 76,912
Percentage contributed	39.5%	39.0%	43.8%
Net OPEB obligation	$ 465,452	$ 406,383	$ 349,711

The funding progress of the plan as of the most recent and two preceding valuation dates were as follows:

	Valuation as of January 1,		
	2017	2016	2015
Actuarial value of assets	$ -	$ -	$ -
Actuarial accrued liability (AAL)	1,085,998	1,027,390	865,747
Unfunded AAL (UAAL)	$ 1,085,998	$ 1,027,390	$ 865,747
Funded ratio	0.0%	0.0%	0.0%
Annual covered payroll (annual payroll of active employees covered by the plan)	$ 674,257	$ 690,071	$ 693,596
UAAL as a percentage of covered payroll	161.1%	148.9%	124.8%

Actuarial methods and assumptions: Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health care cost trend. Amounts are determined regarding the funded status of the plan, and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

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

In the January 1, 2016 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions include a 7% investment rate of return (net of administrative expenses), which is a blended rate of the expected long-term and short-term investment returns on the University's own assets to be used for funding the current liability, and an annual health care cost trend rate of 5%, which includes a 4% inflation assumption. As part of the January 1, 2016, valuation, the University adopted updated mortality assumptions based on the RP-2014 General Healthy Mortality Tables, projected back to 2007 using scale Mortality Projection (MP)-2014 and then projected forward using MP-2015. The UAAL is being amortized over 30 years as a level percentage of projected payroll on a closed basis, with 20 years remaining as of June 30, 2017.

The University will be required to implement the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* effective with the fiscal year ending June 30, 2018. While the University has not yet determined the full impact of GASB Statement No. 75 on its financial statements, the University will be required to report the full unfunded actuarial liability in its entirety in the financial statements, rather than continue to amortize the unfunded OPEB obligation over a thirty-year period as allowed by GASB Statement No. 45. In addition, GASB Statement No. 75 changes certain actuarial assumptions previously allowed under current OPEB accounting guidance, including annual updates to estimated liabilities based on current year interest rates. Based upon the latest actuarial analysis (completed July 2016), the total OPEB obligation is estimated to range between $1.4 billion (6% interest rate) to $2.8 billion (2% interest rate), depending on interest rates effective at the measurement date.

13. Long term debt and other obligations

Long term debt and other obligations for the years ended June 30, 2017 and 2016 are summarized as follows:

	2016	Borrowed	Retired	2017	Current Portion
General Revenue Bonds:					
Series 2015A	$ 192,890	$ -	$ 1,000	191,890	$ 3,655
Series 2013A	164,545	-	3,405	161,140	3,565
Series 2010A	205,000	-	-	205,000	-
Series 2010C	222,740	-	13,700	209,040	14,230
Series 2007A	8,005	-	3,910	4,095	2,005
Series 2007B	25,000	-	-	25,000	-
Series 2005	54,140	-	-	54,140	-
Series 2003A	48,205	-	-	48,205	-
Series 2000A	77,130	-	5	77,125	-
	997,655	-	22,020	975,635	23,455
General Revenue Commercial Paper:					
Series B taxable	92,890	8,720	7,415	94,195	94,195
Series E tax-exempt	54,685	-	54,685	-	-
Series F tax-exempt	-	89,870	4,275	85,595	85,595
	147,575	98,590	66,375	179,790	179,790
Unamortized bond premiums	52,439	-	2,581	49,858	2,881
Student loan deposits	39,660	488	-	40,148	-
Lease obligations and other	1,194	-	151	1,043	157
	$ 1,238,523	$ 99,078	$ 91,127	$ 1,246,474	$ 206,283

	2015	Borrowed	Retired	2016	Current Portion
General Revenue Bonds:					
Series 2015A	$ 192,890	$ -	$ -	192,890	$ 1,000
Series 2013A	167,800	-	3,255	164,545	3,405
Series 2010A	205,000	-	-	205,000	-
Series 2010C	235,930	-	13,190	222,740	13,700
Series 2007A	11,730	-	3,725	8,005	3,910
Series 2007B	25,000	-	-	25,000	-
Series 2005	54,140	-	-	54,140	-
Series 2003A	48,205	-	-	48,205	-
Series 2000A	77,135	-	5	77,130	-
	1,017,830	-	20,175	997,655	22,015
General Revenue Commercial Paper:					
Series B taxable	83,000	16,920	7,030	92,890	92,890
Series E tax-exempt	109,105	3,215	57,635	54,685	54,685
	192,105	20,135	64,665	147,575	147,575
Unamortized bond premiums	54,549	-	2,110	52,439	2,581
Student loan deposits	39,142	1,283	765	39,660	-
Line of credit	536	-	536	-	-
Lease obligations and other	1,339	-	145	1,194	151
	$ 1,305,501	$ 21,418	$ 88,396	$ 1,238,523	$ 172,322

All bonds are secured by General Revenues and certain variable rate issues bear interest based on weekly or quarterly rates determined by the indexing agent or remarketing agent and are amortized through mandatory redemptions as follows:

- Series 2007B: from fiscal 2020 through 2037
- Series 2005: from 2021 through 2034
- Series 2003A: from 2021 through 2033
- Series 2000A: from 2022 through 2031

With the exception of the Series 2007B bonds, the foregoing bonds may be converted to a permanent fixed rate provided certain conditions are met.

The Series 2015A bonds bear interest at fixed rates from 2% to 5% and mature either serially through fiscal 2036 or are subject to mandatory redemption from fiscal 2037 through 2046.

The Series 2013A bonds bear interest at fixed rates from 3% to 5% and mature either serially through fiscal 2034 or are subject to mandatory redemption from fiscal 2035 through 2042.

The Series 2010A bonds bear interest at 6.17% and are subject to mandatory redemption from fiscal 2044 through 2050. Prior to March 1, 2013, in accordance with the Build America Bonds program, the University received semi-annual federal credit payments equal to 35% of actual interest expense incurred on the outstanding principal balance of the bonds. Pursuant to the requirements of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, certain automatic reductions took place on March 1, 2013. These required reductions included a reduction to refundable credits applicable to certain qualified bonds, including Series 2010A. The sequestration reduction rate is 6.9% for payments processed on or after October 1, 2016 and on or before September 30, 2017. The sequestration reduction rate was 6.8% from October 1, 2015 to September 30, 2016. The sequestration reduction rate will be applied unless and until a law is enacted that cancels or otherwise impacts the sequester, at which time the sequestration rate is subject to change.

The Series 2010C bonds bear interest at fixed rates from 3% to 5.125% and mature either serially through fiscal 2029 or are subject to mandatory redemption from 2030 through 2044.

The Series 2007A bonds bear interest at 5% and mature serially through fiscal 2019.

The University utilizes variable-rate commercial paper to provide interim financing. The Board has authorized the issuance of up to $250,000 in commercial paper secured by General Revenues and allows for tax-exempt and taxable issuances. Outstanding commercial paper debt is converted to long-term financing, as appropriate, within the normal course of business. Outstanding tax-exempt balances bear interest at rates from 0.84% to 0.96% and taxable balances bear interest at rates from 0.92% to 1.07%, with principal and accrued interest payments due within a maximum of 270 days from the date of issuance.

Hedging derivative instrument payments and hedged debt: Using rates as of June 30, 2017, scheduled fiscal year maturities of bonds payable and related interest expense are as follows. These amounts assume that current interest rates on variable-rate bonds and the current reference rates of hedging derivative instruments will remain the same for their term. As these rates vary, interest payments on variable-rate bonds and net receipts/payments on the hedging derivative instruments will vary. See Footnote 14 for information on derivative instruments.

Fiscal Year	Fixed-Rate Bonds		Variable-Rate Bonds		Hedging	
Ending June 30,	Principal	Interest	Principal	Interest	Derivatives, Net	Total
2018	23,455	37,707	-	1,980	6,219	69,361
2019	24,460	36,514	-	1,980	6,191	69,145
2020	23,290	35,385	1,990	1,970	6,135	68,770
2021	18,205	34,617	7,980	1,921	5,978	68,701
2022	16,245	33,848	10,880	1,816	5,637	68,426
2023-2027	66,570	159,313	81,095	6,888	21,041	334,907
2028-2032	66,615	145,872	85,105	2,668	7,383	307,643
2033-2037	102,245	128,758	17,420	299	396	249,118
2038-2042	142,210	100,036	-	-	-	242,246
2043-2047	185,105	58,720	-	-	-	243,825
2047-2052	102,765	10,515	-	-	-	113,280
Total	$ 771,165	$ 781,285	$ 204,470	$ 19,522	$ 58,980	$ 1,835,422

Interest expense was $37,461 (net of $11,708 capitalized interest) and $44,089 (net of $5,573 capitalized interest) for 2017 and 2016, respectively.

Unamortized bond premiums totaled $49,858 ($2,881 current) at June 30, 2017. Bond premium amounts are amortized over the applicable bond issue life.

Student loan deposits represent funds from the federal government and other private entities related to various student loan programs.

The University holds $75,000 in revolving lines of credit that are available for maintaining the required operating cash reserves of the University and providing necessary funds to meet extraordinary cash flow needs, if necessary. For the years ending June 30, 2017 and 2016, no amounts were drawn on these lines of credit.

Lease obligations and other is comprised of lease obligations of $1,043 ($157 current).

Accrued personnel costs include vacation and sick leave days earned but unused, including the University's share of payroll taxes, valued at the current rate of pay. Changes in the balances of accrued personnel costs during 2017 and 2016 were as follows:

	2017	2016
Balance, beginning of year	$ 87,332	$ 84,763
Additions	12,450	6,459
Reductions	(4,494)	(3,890)
Balance, end of year	95,288	87,332
Less: current portion	57,722	54,271
Noncurrent portion	$ 37,566	$ 33,061

14. Derivative instruments

At June 30, 2017 and 2016, the University was party to eight separate pay-fixed, receive-variable interest rate swaps and five separate pay-variable, receive-variable interest rate swaps. After considering any netting arrangements or other rights of offsets that may exist with each counterparty, interest rate swaps are reported at the net fair value as of the balance sheet date as either a noncurrent asset or noncurrent liability in the Statement of Net Position.

The fair value and notional amounts of derivative instruments outstanding at June 30, 2017 and 2016 were as follows:

	June 30, 2017		June 30, 2016	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Derivative instruments - swap asset:				
Investment derivatives:				
Pay variable interest rate swaps	$ 41,555	$ 345	$ 47,495	$ 584
Derivative instruments - swap liability:				
Cash flow hedging derivatives				
Pay-fixed interest rate swaps	$ 206,785	$ (43,656)	$ 207,535	$ (62,009)
Investment derivatives:				
Pay-variable interest rate swaps	366,070	7,568	383,380	18,144
Pay-fixed interest rate swaps	71,685	(21,090)	71,685	(29,820)
Total Derivative instruments - swap liability	$ 644,540	$ (57,178)	$ 662,600	$ (73,685)

In accordance with GASB Statement No. 53, an interest rate swap is considered an effective cash flow hedge if the swap payment received substantially offset the payment made on the associated debt and changes in fair value are deferred as either a deferred outflow or a deferred inflow of resources. An interest rate swap that is not considered an effective cash flow hedge, in accordance with the provisions of the Statement, is deemed to be an investment derivative instrument and changes in fair value are recorded as net investment income (loss). For the fiscal year ending June 30, 2017 and 2016, the fair value of hedging derivative instruments increased $18,353 and decreased $13,945, respectively, while the fair value of investment derivative instruments decreased $2,085 and $5,044, respectively.

Fair Value: The fair values of the interest rate swaps were estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swaps, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. The payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the dates of each future net settlement on the swaps.

Objective: The University is party to eight separate derivative instruments which are pay-fixed, receive-variable interest rate swaps that hedge the changes in cash flows on various variable-rate debt series. In order to protect against the potential of rising interest rates, the University entered into these derivative instruments at a cost less than what the University would have paid to issue fixed-rate debt. In order to benefit from both expected changes in the relationship of short and long-term interest rates and the relationships between the SIFMA Municipal Swap Index and both the ten-year USD-ISDA Index and the one-month USD-LIBOR-BBA Index and the relationship between the one-month USD-LIBOR-BBA Index and the ten-year USD-ISDA Index, the University also entered into five separate investment derivative instruments which are pay-variable, receive-variable interest rate swaps which relate to various debt series.

Terms, Fair Values, and Credit Risk: The following table displays the terms and fair values of the University's hedging derivative instruments outstanding at June 30, 2017 and 2016, along with the notional amounts and credit rating of the associated counterparty as of June 30, 2017.

Type	Cash Flow Hedge for Debt Series	2017 Notional Amount	Effective Date	Termination Date	Rate Paid	Rate Received	Counterparty/ Counterparty Credit Rating	2017 Fair Value	2016 Fair Value
Pay-fixed interest rate swap	2000A	$ 71,535	11/3/2008	8/15/2029	4.074%	67% USD-LIBOR-BBA one month	Deutsche Bank AG / Baa2/BBB+	$ (16,244)	$ (22,560)
Pay-fixed interest rate swap	CP Series B	915	10/17/2002	8/15/2018	4.330%	USD-LIBOR-BBA one month	Deutsche Bank AG / Baa2/BBB+	(31)	(79)
Pay-fixed interest rate swap	CP Series B	2,040	10/17/2002	8/15/2022	5.280%	USD-LIBOR-BBA one month	Deutsche Bank AG / Baa2/BBB+	(290)	(452)
Pay-fixed interest rate swap	2003A	48,205	11/3/2008	2/15/2033	3.618%	67% USD-LIBOR-BBA one month	Barclays Bank PLC / A2/A-	(10,106)	(14,477)
Pay-fixed interest rate swap	CP Series B	7,950	11/3/2008	2/15/2033	5.330%	USD-LIBOR-BBA one month	Barclays Bank PLC / A2/A-	(2,156)	(3,149)
Pay-fixed interest rate swap	2005	54,140	11/3/2008	2/15/2034	3.647%	67% USD-LIBOR-BBA one month	Barclays Bank PLC / A2/A-	(11,529)	(16,470)
Pay-fixed interest rate swap	2007B & CP Series E	22,000	5/17/2007	2/15/2028	4.139%	67% USD-LIBOR-BBA three month plus .58%	JP Morgan Chase Bank / Aa3/A+	(3,300)	(4,822)
		$ 206,785						$ (43,656)	$ (62,009)

The following table displays the terms and fair values of the University's investment derivative instruments outstanding at June 30, 2017 and 2016, along with the notional amounts and credit rating of the associated counterparty as of June 30, 2017:

Type	Associated Debt Series	2017 Notional Amount	Effective Date	Termination Date	Rate Paid	Rate Received	Counterparty/ Counterparty Credit Rating	2017 Fair Value	2016 Fair Value
Pay-variable interest rate swap	2000A, 2003A, 2005, 2010C	$ 229,680	8/15/2009	2/15/2034	67% USD-LIBOR-BBA one month	67% USD-ISDA Swap Rate ten year less 0.407%	Deutsche Bank AG / Baa2/BBB+	$ 4,499	$ 10,048
Pay-variable interest rate swap	CP Series B	10,905	5/26/2006	2/15/2033	USD-LIBOR-BBA one month	USD-LIBOR-BBA ten year less 0.575%	Deutsche Bank AG / Baa2/BBB+	346	702
Pay-variable interest rate swap	2010C	27,705	5/17/2010	8/15/2032	SIFMA Municipal Swap Index	67% USD-LIBOR-BBA one month plus 0.44%	Deutsche Bank AG / Baa2/BBB+	230	389
Pay-variable interest rate swap	2010C	41,555	5/17/2010	8/15/2032	SIFMA Municipal Swap Index	67% USD-LIBOR-BBA one month plus 0.44%	Bank of New York Mellon / Aa2/AA-	345	584
Pay-variable interest rate swap	2007A, 2007B, 2010C	97,780	5/17/2007	2/15/2037	SIFMA Municipal Swap Index	67% USD-ISDA Swap Rate ten year plus 0.0063%	JP Morgan Chase Bank / Aa3/A+	2,493	7,005
Pay-fixed interest rate swap	2007B, CP Series B & E	71,685	5/17/2010	2/15/2037	4.226%	67% USD-LIBOR-BBA three month plus 0.63%	JP Morgan Chase Bank / Aa3/A+	(21,090)	(29,820)
		$ 479,310						$ (13,177)	$ (11,092)

Subsequent to the original effective dates, the University amended three of its pay-variable, receive-variable interest rate swaps per the terms listed in the table below. After the amendment periods, these interest rate swaps revert back to the original terms as outlined in the table above.

2017 Notional Amount	Amendment Effective Date	Amendment Termination Date	Rate Paid	Rate Received	Counterparty/ Counterparty Credit Rating
$ 229,680	8/15/2011	8/14/2014	0%	1.407%	Deutsche Bank AG / Baa2/BBB+
	8/15/2014	8/14/2019	0%	0.857%	
$ 10,905	8/15/2011	8/14/2014	0%	2.1725%	Deutsche Bank AG / Baa2/BBB+
	8/15/2014	8/14/2019	0%	1.3530%	
$ 97,780	8/1/2011	7/31/2014	SIFMA Municipal Swap Index	67% USD-LIBOR-BBA one month plus 1.8653%	JP Morgan Chase Bank / Aa3/A+
	8/1/2014	2/14/2021	SIFMA Municipal Swap Index	67% USD-LIBOR-BBA one month plus 1.1245%	

Credit Risk: The University is exposed to credit risk on derivative instruments that are in asset positions. To minimize its exposure to loss related to credit risk, it is the University's policy to require counterparty collateral posting provisions. The University has never failed to access collateral when required. The aggregate fair value of derivative instruments in asset positions at June 30, 2017 and 2016 was $7,913 and $18,728, respectively. This represents the maximum loss that would be recognized at the reporting date if the counterparties to those derivatives failed to perform as contracted. This maximum exposure is offset by negative hedging and investment derivative fair values included in netting arrangements with the same counterparties as the derivative instruments in asset positions. The net exposure to credit risk with any individual counterparty is $345 and $584 at June 30, 2017 and 2016, respectively.

The following table demonstrates the thresholds and minimum transfers for collateralization:

	Deutsche Bank AG		JP Morgan Chase Bank N.A.		Bank of New York Mellon		Barclays Bank PLC	
Credit Rating	Threshold	Minimum Transfer	Threshold	Minimum Transfer	Threshold	Minimum Transfer	Threshold	Minimum Transfer
Aaa/AAA	$ 40,000	$ 1,000	$ 40,000	$ 1,000	$ 40,000	$ 1,000	$ 40,000	$ 1,000
Aa3/AA- to Aa1/AA+	6,000*	1,000	20,000	1,000	6,000*	1,000	6,000	1,000
A3/A- to A1/A+	1,500	500	5,000	500	1,500	500	1,500	500
Baa1/BBB+	500	250	500	250	500	250	500	250
Below Baa1/BBB+	-	250	-	250	-	250	-	-

* Threshold for the University is $20,000

Interest Rate Risk: The University is not exposed to interest rate risk on its derivative instruments.

Basis Risk: The University is exposed to basis risk on its pay-fixed, receive-variable interest rate swaps because the variable-rate payments received by the University on these hedging derivative instruments are based on a rate or index other than interest rates the University pays on its variable-rate debt, which bear interest based on periodic rates determined by the indexing agent or remarketing agent. These pay-fixed, receive-variable swaps expose the University to basis risk should the rates resulting from the 67% of USD-LIBOR-BBA swaps not equal the rate the University pays on the 2000A, 2003A, 2005, 2007B, and tax-exempt Commercial Paper Series debt, and should the rates resulting from the USD-LIBOR-BBA swaps not equal the rate the University pays on the taxable Commercial Paper Series debt.

Termination Risk: The University or any of the involved counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract. If at the time of termination, a hedging derivative instrument is in a liability position, the University would be liable to the appropriate counterparty for a payment equal to the liability, subject to any netting arrangement.

Rollover Risk: The University is not exposed to rollover risk on its derivative instruments.

Contingencies: All of the University’s derivative instruments include provisions that require the University to post collateral at certain thresholds depending on the University’s credit rating. See the table under “Credit Risk” for thresholds and minimum transfers for collateralization. As of June 30, 2017, the University’s credit ratings were Aa1 as assigned by Moody’s and AA+ as assigned by Standard & Poor’s. The aggregate fair value of all derivative instruments with these collateral posting provisions as of June 30, 2017 was ($56,833). The related collateral postings totaled $22,040 posted by the University to its counterparties and $0 held by the University posted by its counterparties.

15. Net position

Restricted and unrestricted net position for the years ended June 30, 2017 and 2016 were as follows:

	2017	2016
Restricted - nonexpendable:		
Permanent endowments	$ 647,189	$ 582,740
Restricted - expendable:		
Gifts, endowment income and sponsored programs	$ 454,190	$ 374,763
Quasi and term endowments	200,008	176,195
Capital projects	93,129	77,244
Student loans	7,260	7,188
Total Restricted - expendable	$ 754,587	$ 635,390
Total Restricted Net Position	$ 1,401,776	$ 1,218,130
Unrestricted	$ 1,110,898	$ 1,005,332

Restricted – Net position is restricted when it is subject to externally imposed constraints.

Unrestricted – Unrestricted net position is not subject to externally imposed constraints. However, this net position is subject to internal designations. Unrestricted net position includes amounts designated for specific purposes by action of the Board or management or may otherwise be subject to pending contractual commitments with external parties. Substantially all unrestricted net position is internally designated for programmatic initiatives or capital asset renewals.

16. Grants and contracts

The University receives grants and contracts from certain federal, state, and local agencies to fund research and other activities. Revenues from grants and contracts are recognized when all eligibility requirements have been met. The University records indirect costs related to such grants and contracts at predetermined rates that are negotiated with the University's federal cognizant agency. Both direct and indirect costs charged to the grants or contracts are subject to audit and approval by the granting agencies. University management believes adjustments of costs, if any, resulting from such examination by the granting agency would not be material.

17. Commitments

At June 30, 2017, the University had initiated plans and incurred certain contractual commitments related to the construction or capital improvement of various facilities. The costs to complete the projects are estimated to be $276,138 and are to be funded from debt proceeds, capital grants, private gifts, and other University funds. Certain University facilities have been, or are scheduled to be, financed in whole or in part by SBA bond issues secured by a pledge of rentals to be received from the State of Michigan pursuant to lease agreements among the SBA, the State of Michigan, and the University. During the lease terms, the SBA will hold title to the respective buildings, the State of Michigan will make all lease payments to the SBA, and the University will pay certain operating and maintenance costs. The SBA will be obligated to sell each building to the University for one dollar, after full payment of all rentals due under the related lease.

At June 30, 2017, the University had entered into various limited partnerships with investment managers of oil and gas, real estate, venture capital, private equity, and restructuring funds. As of June 30, 2017, $633,064 of the initial $1,426,675 investment commitment remains outstanding.

The University has entered into an electric power purchase and site access agreement for renewable solar energy. Under the terms of the contract, the University has granted a third party access to construct, operate, and maintain solar arrays on the University's property. The University is committed to purchase, at a fixed rate, all of the electric power generated from the solar arrays. The University has the option to purchase the solar array infrastructure at specific dates throughout the term of the contract.

18. Fair value measurements

The University categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The following describes this hierarchy and the primary valuation methodologies used by the University for financial instruments measured at fair value on a recurring basis:

Level 1: Quoted prices in active markets for identical assets or liabilities. Market-price data are generally obtained from relevant exchanges or dealer markets.

Level 2: Inputs other than Level 1 that are observable either directly or indirectly, such as quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for similar assets or liabilities. Inputs are obtained from various sources, including market participants, dealers, and brokers.

Level 3: Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The University's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

The University's recurring estimated fair value of investments and derivatives at June 30, 2017 and 2016, grouped by the valuation hierarchy outlined above were as follows:

	Fair value measurement at June 30, 2017 using:			
	Balance at June 30, 2017	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Investments by fair value level:				
Equity securities:				
U.S. equities	$ 452,251	$ 452,251	$ -	$ -
International equities	96,444	42,551	53,893	-
Debt securities:		-	-	-
U.S Treasury bonds	164,847	164,847	-	-
U.S Government agencies	52,978	-	52,978	-
Corporate bonds	77,805	-	77,805	-
International bonds	32,666	-	32,666	-
Municipal bonds	877	-	877	-
Asset-backed securities	70,613	-	69,662	951
Other fixed income	4,779	4,715	-	64
Real assets	36,546	-	-	36,546
Money market and mutual funds	25,210	25,210	-	-
Funds held at MSU Foundation	18,866	-	-	18,866
Other investments	19,136	15,429	-	3,707
Total investments by fair value level	1,053,018	$ 705,003	$ 287,881	$ 60,134
Investments measured at the net asset value (NAV):				
Hedge funds - event driven	263,377			
Hedge funds - long/short	389,843			
International equities	580,997			
Private investments - opportunistic	40,301			
Private investments - private equity	258,194			
Private investments - secondaries	48,579			
Private investments - venture capital	162,781			
Real assets	160,010			
Fixed income	79,975			
U.S. equities	18,110			
Total investments measured at NAV	2,002,167			
Total investments measured at fair value	$ 3,055,185			

	Balance at June 30, 2017	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	Fair value measurement at June 30, 2017 using:			
Derivative instruments by fair value:				
Investment derivatives - swap assets	$ 345	$ -	$ 345	$ -
Cash flow hedging derivatives - swap liability	(43,656)	-	(43,656)	-
Investment derivatives - swap liability	(13,522)	-	(13,522)	-
Total derivative instruments by fair value	$ (56,833)	$ -	$ (56,833)	$ -

	Balance at June 30, 2016	Quoted prices in active markets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	Fair value measurement at June 30, 2016 using:			
Investments by fair value level:				
Equity securities:				
U.S. equities	$ 357,792	$ 357,792	$ -	$ -
International equities	78,854	31,948	46,906	-
Debt securities:				
U.S Treasury bonds	179,424	179,424	-	-
U.S Government agencies	68,608	-	68,608	-
Corporate bonds	97,076	-	97,076	-
International bonds	37,561	-	37,561	-
Municipal bonds	1,348	-	1,348	-
Asset-backed securities	90,839	-	89,650	1,189
Other fixed income	2,939	2,939	-	-
Real assets	53,269	24,611	-	28,658
Money market and mutual funds	20,819	20,819	-	-
Funds held at MSU Foundation	17,691	-	-	17,691
Other investments	22,510	19,714	-	2,796
Total investments by fair value level	1,028,730	$ 637,247	$ 341,149	$ 50,334
Investments measured at the net asset value (NAV):				
Hedge funds - event driven	197,964			
Hedge funds - long/short	389,255			
International equities	488,886			
Private investments - opportunistic	34,067			
Private investments - private equity	202,391			
Private investments - secondaries	41,446			
Private investments - venture capital	121,267			
Real assets	163,875			
Fixed income	64,750			
U.S. equities	42,323			
Total investments measured at NAV	1,746,224			
Total investments measured at fair value	$ 2,774,954			
Derivative instruments by fair value:				
Investment derivatives - swap assets	$ 584	$ -	$ 584	$ -
Cash flow hedging derivatives - swap liability	(62,009)	-	(62,009)	-
Investment derivatives - swap liability	(11,676)	-	(11,676)	-
Total derivative instruments by fair value	$ (73,101)	$ -	$ (73,101)	$ -

As prescribed by GASB Statement No. 72, certain investments held by the University are to be valued using methods other than fair value. For the fiscal year ending June 30, 2017 and 2016, the University valued U.S. Treasury bond investments with original maturities of less than one year at amortized cost that totaled $422 and $1,000, respectively. In addition, certain funds held by interest rate swap counterparties totaling $7,150 and $19,290 at June 30, 2017 and 2016, respectively, reflect cash balances on deposit in accordance with counterparty collateral posting provisions.

Investments classified in Level 1 at June 30, 2017 and 2016 are valued using prices quoted in active markets for those securities.

The fair value of various equity and debt securities held at June 30, 2017 and 2016 was determined primarily on Level 2 inputs. The University estimates the fair value of these investments using other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Investments classified in Level 3 at June 30, 2017 and 2016 are valued using the University's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.

Derivative instruments classified in Level 2 of the fair value hierarchy are valued using a market approach that considers benchmark interest rates.

The University holds shares or interests in investment companies where the fair value of the investments are measured on a recurring basis using net asset value (or its equivalent) of the investment companies as a practical expedient. For the year ended June 30, 2017 and 2016, the fair value, unfunded commitments, and redemption rules of those investments were as follows:

			As of June 30, 2017		
	June 30, 2017	June 30, 2016	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Hedge funds	$ 653,220	$ 587,219	$ -	Various	4-180 days
International equities	580,997	488,886	-	Various	1-90 days
Private investments	509,855	399,171	458,663	Not applicable	Not applicable
Real assets	160,010	163,875	95,652	Various	7 days
Other fixed income	79,975	64,750	-	Daily	10 days
U.S. equities	18,110	42,323	1,683	Annually	90 days
Total	$ 2,002,167	$ 1,746,224	$ 555,998		

The University invests in hedge funds seeking equity-like returns while reducing volatility . The University will consider funds with a diversifier mandate (lower expected volatility and lower correlation to broad market trends), as well as funds with a growth-oriented mandate (higher expected volatility and higher correlation to broad market trends). Managers with either type of mandate will employ risk management techniques intended to reduce downside potential to a degree considered appropriate for their respective strategy. Managers employing “long/short” strategies invest primarily in equities and mitigate market risk by purchasing equity shares that are expected to appreciate in value and selling short equity shares that are expected to decline in value. Managers employing event-driven and arbitrage strategies seek to maximize returns by investing in publicly announced corporate transactions, such as mergers, tender offers, liquidations, bankruptcies and reorganizations or in arbitraging temporary discrepancies in securities pricing in the equity and fixed income markets. Distressed security managers invest primarily in bonds and bank loans trading at a significant discount to par value as a result of the debtor’s troubled financial condition.

The University invests in international equities that are marketable equity securities in developed and emerging countries outside the U.S. The investment is intended to provide long-term performance similar to or in excess of U.S. equities and provide diversification.

The University seeks to enhance the total return of the CIF by investing a portion of its funds in private investments, which include distressed, private equity, and venture capital investments. These investments are illiquid and higher risk/return assets than marketable securities. Risk will be controlled by diversifying across a number of fund managers and by geographic focus, industry emphasis, financing stage, and vintage year. This core private investments portfolio may be supplemented with less diversified specialty funds or direct investments.

The University seeks to reduce volatility and provide a hedge against sudden, unanticipated inflation by investing in both public and private real assets. Risks related to the investments will be minimized by diversifying through use of investment pools or partnerships that are varied as to property type, location, investment life cycle, and investment manager. This core real asset portfolio may be supplemented with less diversified specialty funds or direct investments.

The University invests in other fixed income assets that are intended to reduce exposure to market risk and provide a hedge against sudden, unanticipated deflation.

The University invests in U.S. equities that are marketable equity securities of primarily U.S.-based companies. Several sub-categories of this asset class include: large capitalization companies, small capitalization companies, value-style investing, and growth-style investing.

The investments in the private investments class (limited partnerships) are committed to funds for extended periods of time, often multiple years. The pacing of investment returns is determined by market activity and the discretion of the general partner. Secondary markets exist into which limited partnerships can sell their interest in funds, but often at a steep discount to the fair value of the investment. In addition, $128,002 and $97,582 of the real asset class at June 30, 2017 and 2016, respectively, and $4,502 and $5,238 of the hedge fund class at June 30, 2017 and 2016, respectively, can never be redeemed. Distributions from each fund will be received only as the underlying investments of the funds are liquidated. It is estimated that the underlying assets of the fund will be liquidated over the next 1 to 10 years.

Approximately, 8% of the value of the investments in the hedge funds class, 5% of the value of the investments in the international equities class, and 4% of the value in the U.S. equities class cannot be redeemed because the investments include restrictions that do not allow for redemption in the first 12 to 60 months after acquisition. The remaining restriction period for these investments ranged from 12 to 30 months at June 30, 2017. Generally, longer redemption restrictions are offered with a lower fee structure.

The hedge fund class above includes an investment, valued at $593, for which a gate has been imposed by the hedge fund manager and redemptions are allowed over time rather than all at once. This redemption restriction has been in place for six months and will lapse on September 30, 2017.

19. New accounting pronouncements

The University will be required to implement the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* effective with the fiscal year ending June 30, 2018. This GASB Statement aims to improve accounting and financial reporting of postemployment benefits other than pensions (other post employment benefits, or OPEB). See footnote 12 for additional information.

The University will be required to implement the provisions of GASB Statement No. 81, *Irrevocable Split-Interest Agreements,* effective with the fiscal year ending June 30, 2018. This GASB Statement aims to improve accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement. The University is in the process of determining the full impact of this standard on its financial statements.

The University will be required to implement the provisions of GASB Statement No. 83, *Certain Asset Retirement Obligations,* effective with the fiscal year ending June 30, 2019. This GASB Statement aims to improve accounting and financial reporting for asset retirement obligations by providing criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources. The University is in the process of determining the full impact of this standard on its financial statements.

The University will be required to implement the provisions of GASB Statement No. 84, *Fiduciary Activities,* effective with the fiscal year ending June 30, 2020. This GASB Statement aims to improve guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and how those activities should be reported. The University is in the process of determining the full impact of this standard on its financial statements.

The University will be required to implement the provisions of GASB Statement No. 86, *Certain Debt Extinguishment Issues,* effective with the fiscal year ending June 30, 2018. This GASB Statement aims to improve accounting and financial reporting for in-substance defeasance of debt and prepaid insurance of debt that is extinguished. The University is in the process of determining the full impact of this standard on its financial statements.

The University will be required to implement the provisions of GASB Statement No. 87, *Leases,* effective with the fiscal year ending June 30, 2021. This GASB Statement aims to improve accounting and financial reporting for leases by establishing a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The University is in the process of determining the full impact of this standard on its financial statements.

Financial report prepared under the direction of Mark P. Haas, Vice President for Finance and Treasurer;
Gregory J. Deppong, Controller; John L. Thelen, Assistant Controller;
and Elizabeth L. Powers, University Tax Manager.

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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*

Independent Auditor's Report

To Management and the Board of Trustees
Michigan State University

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 Michigan State University (the "University") and its discretely presented component unit as of and for the year ended June 30, 2017, and related notes to the financial statements, which collectively comprise the University's basic financial statements, and have issued our report thereon dated October 26, 2017. Our report includes a reference to other auditors who audited the financial statements of Michigan State University Foundation (the "Foundation"), as described in our report on Michigan State University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of Michigan State University Foundation were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Michigan State University'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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control. Accordingly, we do not express an opinion on the effectiveness of the University'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 a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the University'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 Michigan State University'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 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*.

To Management and the Board of Trustees
Michigan State University

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 University'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 University's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Plante & Moran, PLLC

October 26, 2017

MICHIGAN STATE
UNIVERSITY

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