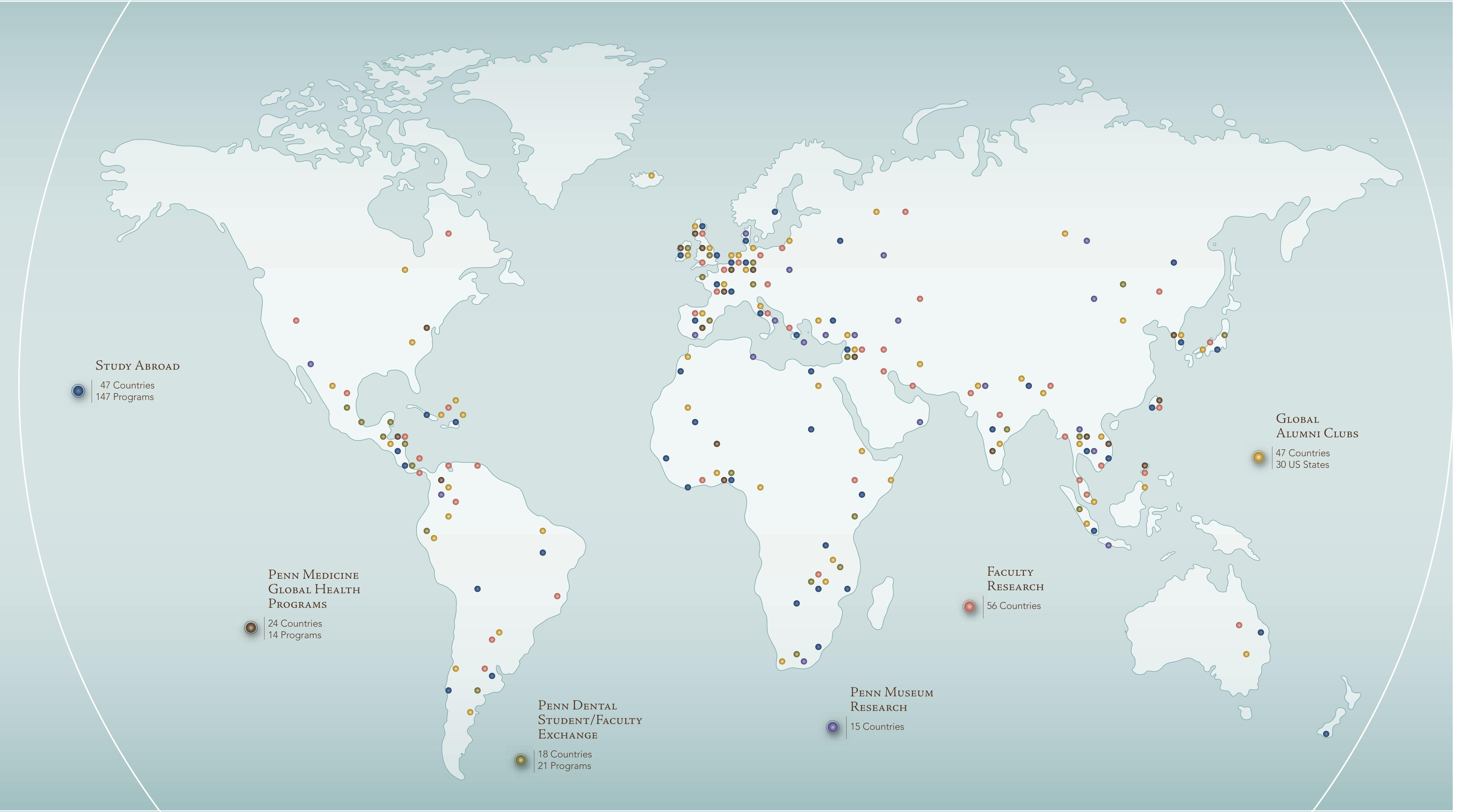
PENN CONNECTS
LOCALLY & GLOBALLY

The dynamic and innovative initiatives Penn has promoted and nurtured over the past decade have served to forge our reputation as a local and global leader. At Penn, the pursuit of knowledge has traditionally taken us far beyond the borders of our West Philadelphia campus. With an eye towards Penn's future as a premier urban research university, our campus development plan, Penn Connects, sets the stage for a profound transformation of campus that will foster still greater connections with our community, city and region.

The foundation of Penn's academic strength—the partnerships among our 12 schools—has afforded unique opportunities to learn and to serve. Our vast resources and collaborative environment foster dialogue and the exchange of ideas in academics, research, medicine and volunteer work.

Part of our mission as a University is to equip our students with the knowledge, skills and experience necessary to make a difference. Today our students, faculty and researchers are on the ground in over 90 countries putting theories and ideas into practice to help solve problems ranging from global warming and AIDS to the digital divide and avian flu. Penn people are exploring ancient civilizations, experiencing different cultures and improving the welfare of developing countries. The following pages provide a brief sampling of Penn's diverse involvement with communities around the corner and across the world.

Penn | A GLOBAL VIEW



University of Pennsylvania Nondiscrimination Statement

The University of Pennsylvania values diversity and seeks talented students, faculty and staff from diverse backgrounds. The University of Pennsylvania does not discriminate on the basis of race, sex, sexual orientation, gender identity, religion, color, national or ethnic origin, age, disability, or status as a Vietnam Era Veteran or disabled veteran in the administration of educational policies, programs or activities; admissions policies; scholarship and loan awards; athletic, or other University administered programs or employment. Questions or complaints regarding this policy should be directed to: Executive Director, Office of Affirmative Action and Equal Opportunity Programs, Sansom Place East, 3600 Chestnut Street, Suite 228, Philadelphia, PA 19104-6106 or by phone at (215) 898-6993 (Voice) or (215) 898-7803 (TDD).

FSC
Mixed Sources

The 2007 Annual Report was produced by the Office of the Vice President for Finance and Treasurer.

Project Manager: Suzanne Arcari

Student Editor: Rachel Omansky '08

Financial Editor: Russell Di Leo

Design: Penn Publication Services

Photographs: provided by students, faculty and staff from locations around the world.

"Through our collaborative engagement with communities all over the world, Penn is poised to advance the central values of democracy…As we prepare to expand Penn's campus to the east, we strengthen our ties with our neighbors and help drive economic and technological development throughout the City and Commonwealth. At the same time, we will share the fruits of our integrated knowledge wherever there is an opportunity for our students, faculty, and alumni to serve and to learn."

– Amy Gutmann

on engaging locally and globally
excerpt from Penn Compact

By the Numbers

Student Enrollment [1]

Undergraduate students 10,743

Graduate and professional students 10,470

Undergraduate Admissions Statistics [1]

Applications 22,646

Percent accepted 16.1%

Percent matriculated 66.5%

Financial Summary

Total operating revenue $ 4,756,883

Total operating expenditures $ 4,423,621

Principal Sources of Revenue

Tuition and fees (net) $ 638,143

Sponsored programs $ 726,625

Hospitals and physician practices [2] $ 2,619,941

Contributions $ 371,090

Investment income [3] $ 1,133,043

Principal Purposes of Expenditures

Instruction $ 847,491

Research $ 592,225

Hospitals and physician practices [2] $ 2,361,208

Endowment

Market value $ 6,635,187

One-year endowment performance 20.2%

Net Assets

Unrestricted $ 4,273,780

Temporarily restricted $ 2,313,624

Permanently restricted $ 2,125,223

Dollars in thousands

(1) Note that full-time equivalent enrollment is calculated based on the number of full-time students plus one-third of the headcount for part-time students. Student and admission statistics are for academic year beginning September 2007, while financial statistics are for fiscal year ending June 30, 2007.

(2) Includes inter-entity eliminations

(3) Includes gains and losses on investments




Table of Contents

Fiscal Year 2007 Performance Highlights

Penn experienced unprecedented growth in a number of key financial components during FY 07. A key highlight was this year's dramatic endowment growth, a result of strategic changes made to investment allocations three years ago. The endowment surged past the $6 billion mark for the first time, soaring from $5.3 billion to $6.6 billion, an increase of $1.3 billion or 24.9%. Endowment performance was a robust 20.2%, the highest return in over a decade. As a direct result of endowment performance, net assets from non-operating activities increased by $1.06 billion with investment income and gains accounting for $861 million of this total.

Total net assets increased $1.4 billion or 19.0% for the fiscal year due to solid investment performance and strong University of Pennsylvania Health System (UPHS) operating performance. Penn ended the fiscal year at June 30, 2007, with total assets of $12.1 billion, total liabilities of $3.4 billion and net assets of $8.7 billion. The consolidated University achieved a sizable increase in net assets from operating activities totaling $333.3 million, an increase of $98.1 million or 41.7% from the previous fiscal year due to continually improving UPHS operations.

COMMUNITY PARTNERSHIP

Sayre High School, a longtime site of community health projects coordinated by Penn, recently opened the Sayre Health Center, a Federally Qualified Health Center that will provide clinical services to residents of the surrounding community.

Led by Penn Medicine, this interdisciplinary effort also includes Dental, Nursing, Social Policy and Practice and Arts and Sciences, and will ultimately involve all of Penn's schools. Penn students assist in providing clinical care as well as health education and other community programs.

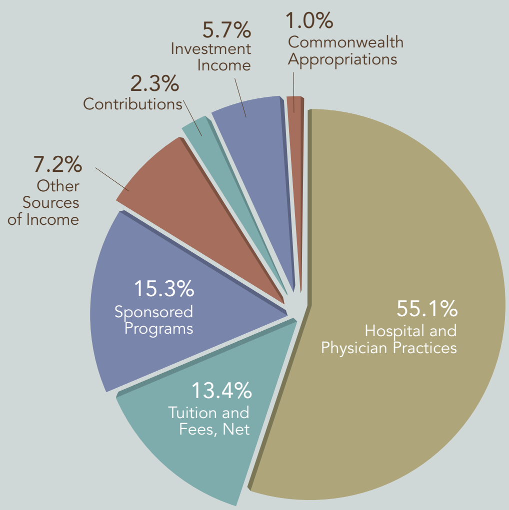
SERVE AND LEARN

PennSmiles is an oral health outreach program that travels throughout West and Southwest Philadelphia neighborhoods to area schools, Head Start programs and other community sites to provide oral health education and dental care. The PennSmiles mobile clinic van is fully equipped for on-site dental care. The program, which has been funded by the Health Resources Services Administration and the Commonwealth of Pennsylvania, is staffed by students and faculty as part of the academically based service learning courses at the School of Dental Medicine. The program began in 2002 and in the 2006-2007 Academic Year reached over 15,000 children and adults in the community.

The University's total revenue increased $324.2 million or 7.3% to almost $4.8 billion. Hospital and physician practices constituted 71.9% or $233.1 million of this overall growth in revenue, reflecting an increase in patient activity and strong operating performance. Tuition and fees (net of certain grants and scholarships) grew $39.0 million or 6.5%.

The University's long term debt received a rating upgrade from "Aa3" to "Aa2" from Moody's Investors Service and continues to be rated "AA" by Standard and Poor's. Enhanced selectivity in admissions, sustained endowment growth and strong fundraising results were cited in the rating assessment. UPHS's long term debt also received rating upgrades from Moody's to "A1 stable" and Standard and Poor's to "A+ positive" due to its strongly improved operational performance and declining debt levels.

Operating Revenue by Source - $4.76 Billion



AN INTERNATIONAL CAMPUS

In the fall of 2006, 4,437 or 19% of the total student population consisted of international students from 145 countries. "Although I did not study abroad, my experience at Penn has opened my eyes to the international community. Every day, I can exchange viewpoints and experiences with people from around the globe. Where else could I sit in my dorm with friends from the U.S., Canada, Guyana, Brazil, China and Sri Lanka and discuss topics ranging from political systems to the merits of Twinkies?"

–Jennifer R. SAS '08

NEW ORLEANS

Penn students, faculty, and staff offered incredibly strong support and assistance in the wake of Hurricane Katrina. For example, the Fox Leadership Program rendered immediate assistance to afflicted communities and continues to send 100 students each year to New Orleans for service trips as well as 20 students each summer to serve with community non-profit organizations.

SAN FRANCISCO

Wharton West offers top-quality management education to western U.S. and Pacific Rim business leaders and organizations through the Wharton MBA Program for Executives as well as through open enrollment and custom executive programs. Wharton has had a strong West Coast presence since 1996 and the current facility, which opened in 2001, hosts the first Wharton degree program beyond the main campus. Wharton West also facilitates strong connections and bolsters Wharton's regional presence with more than 5,500 graduates of Wharton West programs in California, and more than 8,000 graduates throughout the Asia-Pacific region.

Sponsored Programs and Commonwealth Appropriations

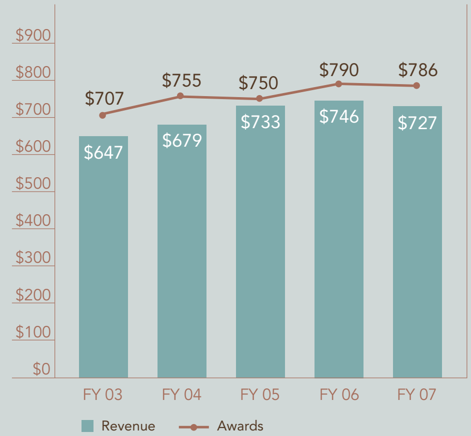
Sponsored program activity, which includes the direct and indirect costs of sponsored research activity, accounted for 15.3% of the University's total revenues in FY 07. Sponsored program revenue totaled $726.6 million, a decrease of almost $20 million or 2.6% compared to FY 06. The indirect cost component fell by $5.8 million to $188.2 million, a decline of 3.0%. Total awards received were $785.6 million, consistent with last year. The federal government provided nearly $573.6 million or 73% of total awards, 2.8% less than last year's federal awards.

The National Institute of Health's (NIH) cutbacks in research funding, forewarned since 2004, affected total sponsored program awards. NIH data from the latest available federal fiscal year (FY 06) shows that Penn received $453 million in awards, 4.2% less than the previous NIH fiscal year. The School of Medicine traditionally receives more than 80% of Penn's awards from the NIH and, due to its dominant share, accounted for most of the percentage decline. Although this decline was not unanticipated, it presents a competitive challenge going forward. Therefore measures have been implemented to find alternative funding opportunities.

Despite the tight funding climate, a five-year, $68 million grant, funded through NIH Clinical and Translational Science Awards (CTSAs), was awarded to Penn and its collaborators as one of a dozen academic health centers throughout the nation that are part of a new national consortium. Led by Penn, the Philadelphia interdisciplinary alliance includes the School of Medicine, eight other schools at Penn, Children's Hospital of Philadelphia, the Wistar Institute and the University of the Sciences. "It will enhance the development of interdisciplinary structures designed to foster and facilitate research and education in the emerging field of translational medicine," said Dr. Arthur Rubenstein, EVP of the University of Pennsylvania for the Health System and Dean of the School of Medicine.

The Commonwealth of Pennsylvania provided $49.4 million in annual support funding, an increase of 10.2% over the previous fiscal year. Seventy percent of this increase was allocated to the School of Veterinary Medicine's Center for Infectious Diseases which was added to the Commonwealth's appropriation program this year. This addition increases Penn Vet's share of the University's Commonwealth appropriations to almost 86%. As the sole veterinary school in Pennsylvania, Penn Vet is committed to research that will safeguard the health of the state's valuable dairy and poultry industries.

SPONSORED PROGRAMS
(IN MILLIONS)



Tuition, Fees and Financial Aid

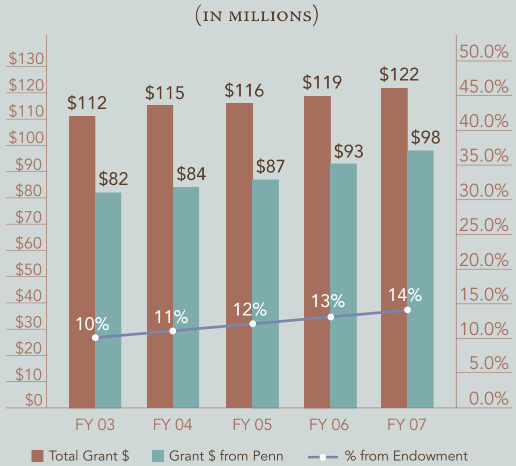
In FY 07, tuition and fees (net of certain grants and scholarships) provided 13.4% of Penn's total revenue. The University received tuition dollars for its undergraduate, graduate and professional programs, and for study abroad and executive education. In addition, fees to support student programs and services generated added revenue.

The undergraduate admission process for the Class of 2011 proved to be the most competitive ever. Penn received 22,646 applications for the class, an increase of 10.6% over the previous year. Only 16.1% of applicants were accepted for admission, and 66.5% of these admitted students chose to matriculate at Penn. In addition to the traditional Penn application, this past year was the first admissions cycle in which applicants could use the Common Application, a switch prompted by the desire to increase reach to economic groups that are traditionally underrepresented at institutions of higher education.

Illustrating our commitment to increasing access, Penn announced in March 2007 that, beginning in the 2007-2008 academic year, undergraduate students whose families earned incomes of less than $60,000 and who demonstrate high financial need will have loan requirements eliminated from aid packages. The initiative expands a previous program for families with incomes under $50,000. This program, along with Penn's ongoing policy of need-blind admission and commitments to meeting full financial need, is making Penn more affordable for all qualified students.

Aid totaling $121.7 million was awarded to 4,065 undergraduates with financial need during FY 07.

Undergraduate Financial Aid Grant Dollars (in millions)



GUATEMALA

Penn students and faculty from the Schools of Medicine and Nursing launched the Guatemala Health Initiative in 2005 to strengthen clinical services and community health promotion in resource-poor communities in Guatemala. The program has since expanded to involve faculty and students from Arts and Sciences, Wharton, and Engineering.

Of this total amount, $98 million was grant or scholarship aid, with $83 million coming from University resources. Fourteen percent of University grants were funded by endowment income. The average unrestricted grant-aided freshman package increased 10% over the previous year to $32,243. Overall, 6,010 undergraduates funded all or part of their education with $116.7 million from grants/ tuition waivers, $52.6 million from educational loans and $15.3 million from work-study programs. A total of 6,871 graduate and professional students received $113.4 million in grants, including teaching and research assistantships and fellowships, $179.1 million in educational loans and $2.9 million for work-study programs.

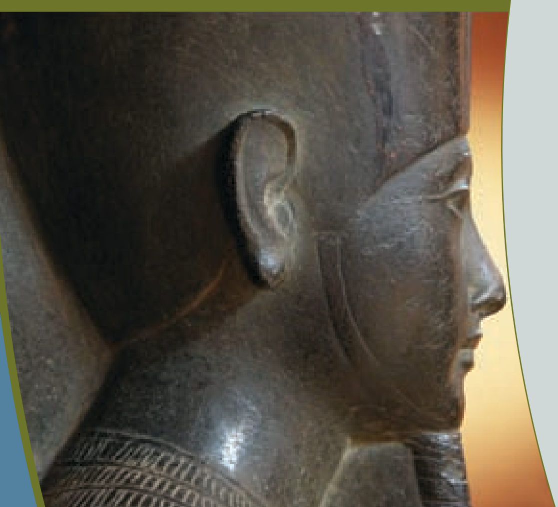
Information technology continues to remake every step of the admission, matriculation and academic processes. Penn's new Admissions System allows prospective applicants to enter personal information online and request an application. To date, nearly 14,000 prospective students have indicated their interest in Penn using this system and the system contains information on more than 45,000 secondary schools. In addition, the launch of the new student loan system allows students 24/7 online access to loan information, improves turnaround time for transactions, and increases staff efficiency. Finally, Penn also eliminated the need for paper grade sheets through a new online grading system.

COSTA RICA

Twenty percent of the world's oxygen is produced by tropical rainforests where deforestation and the loss of biodiversity are occurring at a rapid rate. Dr. Dan Janzen, a renowned researcher and conservationist, and his team, including 29 native parataxonomists, are in their 29th year of inventorying and cataloging insect species, their food plants, and their parasitoids found in the Area de Conservacion Guanacaste in northwestern Costa Rica. Funding sources include the National Science Foundation, private foundations and trusts.

STUDY ABROAD

Penn ranks first among schools in the Ivy League and seventh nationally in terms of the number of students who study abroad. Last year, more than 1,700 Penn students at all degree levels participated in some form of international study. In Europe alone, Penn coordinates with programs at institutions in 46 cities across 13 countries for formal study abroad. In addition, students from many of Penn's schools, particularly the School of Medicine and the School of Dental Medicine, complete practical training in Europe, and many faculty conduct research across the continent.



MUSEUM RESEARCH

Since its founding in 1887, the Penn Museum has been actively excavating sites throughout the Middle East, the Mediterranean and Europe. This year, the exhibition Amarna, Ancient Egypt's Place in the Sun was the centerpiece of the Museum's 'Year of Egypt' and features objects discovered on Penn excavations. One of the most significant sites of current research is Gordion, a rich site in Turkey long renowned as the center from which the famed King Midas ruled. Other current expeditions include ventures in Egypt, France, Crete, Italy, Greece, and Syria.

University of Pennsylvania Health System

In FY 07, the University of Pennsylvania Health System (UPHS) once again improved its financial position. For the seventh consecutive fiscal year, UPHS generated a surplus, with a net operating margin of $259 million, $100 million higher than FY 06. Total financial assets, comprised of cash and investments, rose by 16.6% to $1.75 billion.

UPHS's strong operating performance was accomplished primarily through quality of care improvements and patient activity increases in the "Relentless Advance of Medicine" programs. Other contributions to operating performance included increased liquidity, with days of cash-on-hand increasing from 158 to 190 days. The number of days in accounts receivable has been cut in half to 36 days since the initiation of the revenue cycle enhancement project.

Outpatient visits at the Penn hospitals and the faculty practices (Clinical Practices of the University of Pennsylvania—CPUP) increased by an average of 4.9%. Increases were also realized in our high intensity services, including emergency medicine, surgery, radiation therapy and chemotherapy. Adjusted admissions were 110,800, or 6.3% higher than FY 06. There was a 9.8% increase in hematology/oncology admissions as well as a 1.5% increase in cardiology admissions over FY 06. The performance results outlined above, plus declining debt levels, earned UPHS upgrades in outlook and ratings from Moody's Investors Service and from Standard and Poor's to "A1" and "A+" respectively.

UPHS purchased the former Graduate Hospital properties, located at 18th & Lombard Streets in Center City, from Tenet Healthcare Corporation. UPHS has partnered with

Allentown-based Good Shepherd Rehabilitation Network and will convert the hospital into a comprehensive rehabilitation center. In addition, outpatient services and a twelve bed inpatient hospice unit will be housed in the facilities. Once Graduate Hospital is refurbished, it will house rehabilitation and long-term acute care services and provide enhanced educational and research opportunities related to the science of rehabilitation medicine.

Three new buildings are scheduled to open within the next four years that will further enable the physicians and scientists at PENN Medicine to translate the latest advances of medical science into clinical benefits for patients. Construction is being completed on the 800,000 square foot Perelman Center for Advanced Medicine, opening in 2008, that will provide a broad spectrum of diagnostic and treatment services to patients, including advanced cancer care, cardiovascular services, and outpatient surgery. The Roberts Proton Therapy Center will open its doors in 2009 and will be the largest cancer treatment facility of its kind in the nation, able to provide patients unprecedented state of the art therapy combined with conventional therapies under one roof. In addition, a new medical research building has been approved to open in 2010 that will provide scientists and physicians with the enhanced ability for close cooperation and collaboration.

In 2007, UPHS achieved recognition through a number of prestigious awards, citations and commendations. The Hospital of the University of Pennsylvania (HUP) achieved Magnet status, the highest institutional honor awarded for nursing excellence. HUP was once again placed on the Honor Roll of best hospitals by U.S. News & World Report, one of only 18 hospitals chosen from approximately 5,400 facilities. The publication also placed the School of Medicine among the top three research-oriented medical schools in the nation. HUP was also recognized as one of America's 100 Choice Hospitals in 2007 by the American Alliance of Healthcare Providers. This award recognizes hospitals that reach out to the community's physicians and healthcare organizations in an effort to increase accessibility to hospital services.

Campus and Community

Auxiliary programs, which generate Other Sources of Income, increased by 7% to $341.7 million, accounting for 7.2% of consolidated University revenues in FY 07. Sources of revenue include room and board, hotel and conference receipts and sales from the Penn bookstore and Computer Connection. The 45,000 students, faculty and staff that comprise Penn's on-campus community benefit from the services provided by these various operations as they represent an integral part of campus life.

Housing choices on campus for students, faculty and staff were augmented by the completion of two apartment complexes that were financed and built by external developers on land leased from Penn—the Hub at 40th and Chestnut Streets and Domus at 34th and Chestnut Streets. In addition, construction began on a similarly financed and developed mixed-use student housing project, the Radian Apartments on the 3900 block of Walnut Street.

Penn's current operations and expansion needs have created the opportunity for the University to encourage local business growth, empower minority and women business owners and to create more jobs. Local residents have filled more than half of the jobs created by Penn's retail ventures, approximately 35% of all Penn construction jobs have gone to minority and women workers, and 26% of all contracts have been awarded to businesses owned by minorities and women. Contributing to this endeavor, the Wharton Small Business Development Center provides business assistance and free consulting services to entrepreneurs and small businesses in the greater Philadelphia area, with over 16,000 hours of consulting to 600 individuals and small businesses annually in recent years.

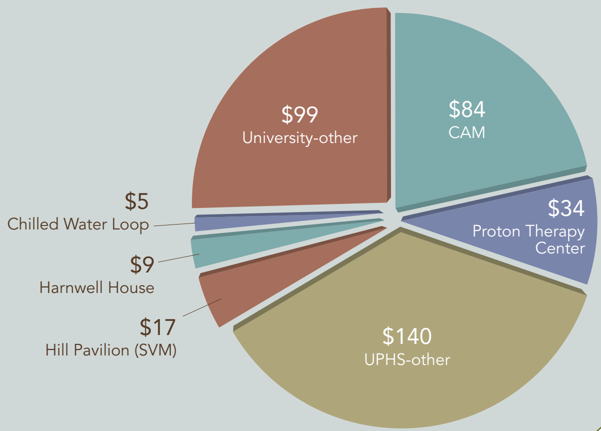
Capital Investments

Capital investments encompass a broad range of projects including property acquisitions, new construction, renovations, information systems and facilities renewal which includes building and campus infrastructure as well as compliance, code and safety upgrades. In FY 07, Penn spent $388 million on capital projects, a 5.5% increase over FY 06.

In new construction, the School of Veterinary Medicine's Hill Pavilion was completed, and the former Hillel building was demolished to make way for the Annenberg Public Policy Center. Construction continued on the Perelman Center for Advanced Medicine as well as on the Roberts Proton Therapy Center.

Building renovation and renewal are vitally important to sustaining the viability of an aging infrastructure, and the majority of capital projects initiated in FY 07 focused on infusing new life into old buildings. Renovations began on the Nursing School's Fagin Hall, the School of Dental Medicine's Evans Periodontic Clinic, the School of Medicine's Bio-safety Labs and the School of Veterinary Medicine's Widener Hospital. In addition, three high rise College Houses—Harnwell, Harrison and Rodin—are in various stages of extensive renovations.

Capital Expenditures – $388 Million
(in millions)



CAMEROON

Penn Engineers Without Borders is a student-run organization devoted to helping developing communities around the world with their engineering needs. In Cameroon, they have created a new, gravity-fed water distribution system in the villages of Kob and Tudig to provide these communities with sufficient water to meet current and projected future water needs. Similar to their approach in a sister project in Honduras, members planned, built, and are maintaining a sustainable water system.

BOTSWANA

Six years ago, School of Medicine physicians led by Dr. Harvey Friedman were invited to help develop and implement national HIV prevention and treatment programs and to assist in the training of local providers on managing the care of HIV infected patients. In Botswana, nearly one-third of its 1.7 million population is infected with HIV, and nearly half of those patients receive treatment. Since then, the program has expanded to include a referral clinic and the inclusion of medical students and residents completing rotations at the Botswana clinic. More recently, the School of Nursing has sent students and faculty to Botswana and the Wharton School is helping design a more efficient system to manage HIV/AIDS therapy.

CHINA

Recognizing the global nature of business today, Wharton Executive Education has established ongoing relationships with organizations throughout Asia, including many in China, Japan, South Korea, Singapore, and Thailand. In particular, Wharton has partnered with local business schools to deliver management and leadership development programs to Chinese executives. The Graduate School of Education has also pioneered the first-ever Doctorate of Education program in China in conjunction with Peking University in Beijing.

MONGOLIA

Members of the Biology Department, led by Dr. Peter Petraitis, are working in collaboration with the Academy of Natural Sciences in Philadelphia, the National University of Mongolia and the Mongolian Academy of Sciences to study the ecological consequences of global climate change and nomadic pastoralism. This region of the world is expected to experience some of the largest temperature increases due to global warming, and the study area along the shores of Lake Hövsgöl is of particular interest because it is home to two of the world's most important ecosystems, taiga forest and steppe. This study is funded by a five-year grant from the National Science Foundation.

Development and Alumni Relations

Penn's Development and Alumni Relations (DAR) programs maintained strong momentum during FY 07 as the University completed the second year of the silent phase of its new comprehensive capital campaign. The campaign's five-year public phase will be officially launched in October 2007 and will conclude on June 30, 2012.

New gift commitments during the year totaled $371.1 million with cash receipts of $321.9 million. Gifts contributed to critical campaign priorities—financial aid, endowed professorships, research support for faculty, and new and renovated facilities—as well as to a wide array of other programmatic initiatives, provided important resources for Penn's most urgent needs. This broad-based philanthropic support for the University's current and future priorities is a vital indicator of Penn's institutional strength and its ability to undertake an ambitious fundraising effort.

Annual giving programs across the University raised $53.4 million during FY 07, a 15.6% increase over the previous year's record-breaking performance. The Penn Fund also set a new record with $24.1 million raised, a 14.8% increase over FY 06.

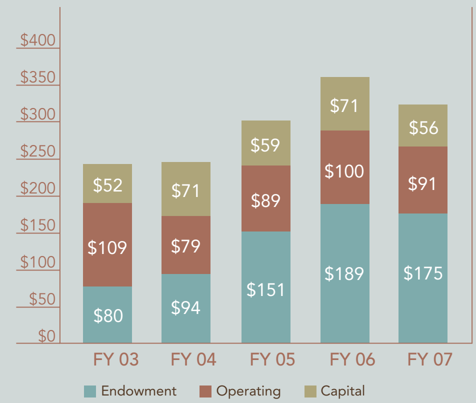
Class reunion fundraising brought in $20.5 million in gifts and pledges from more than 6,000 alumni in support of class gift goals. A number of classes set new records for either dollars raised or class participation, with the classes of 1942 and 1982 establishing new records in both areas. The Class of 1982 raised nearly $7 million from 1,046 donors, making it the first reunion in Penn's history to surpass 1,000 Penn Fund donors. The class also contributed to a record 40 new or existing endowed scholarship funds.

Again in FY 07, the undergraduate Senior Class gift drive set new records for both fundraising and class participation, further confirming that DAR's focused efforts to create programs that engage and involve current students to support Penn are having very positive effects.

QuakerNet, Penn's Online Alumni Community, grew to 64,500 users, and Development and Alumni Relations added 36,000 new e-mail addresses for alumni, bringing the number of alumni who can receive electronic communications to 160,000. This represents a more than 100% increase during the past four years.

Growth in Penn Traditions programming, engaging approximately 1,600 incoming freshmen during New Student Orientation, expansion of mailing of *The Pennsylvania Gazette* to include more graduate alumni, and the launching of PACNet, Penn's online alumni career networking tool, all reflected progress in Alumni Relations' strategic plan to establish a more unified and collaborative alumni relations effort across the University.

Gift Receipts
(in millions)



SOUTHEAST ASIA & THE PACIFIC RIM

Summary and Future Outlook

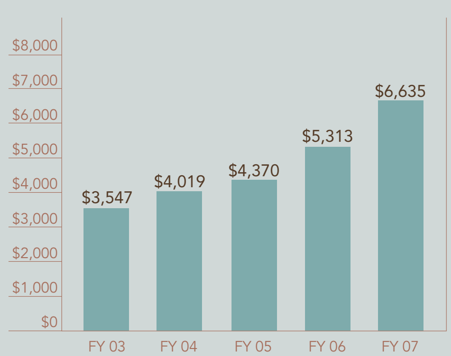
The trajectory of our success is not a simple path. The complexity of Penn as an institution requires insight, planning, and innovation in order to achieve significant programmatic and financial results. The fiscal year ending June 30, 2007 witnessed sustained growth and continued success. *Sustained growth*—just 14 years ago, the total value of Penn's endowment was less than this year's endowment increase of $1.3 billion. The endowment grew in FY 07 to a remarkable $6.6 billion. *Continued success*—UPHS posted its seventh consecutive year of positive operating performance.

A key long-term challenge for the University is the continued growth of sponsored program research funding. For the first time, planned cutbacks in NIH funding affected total sponsored revenue. Although the decline was minimal, the NIH is Penn's largest federal source of funds and every avenue must be explored to identify and develop additional funding sources from other government agencies, foundations and corporations to reinforce and strengthen Penn's competitive edge in research over the coming years.

A number of changes in key leadership positions occurred over the last year in both the administration and the schools. New appointments have been made to the leadership positions of Dean of the Wharton School, Dean of the Graduate School of Education, Vice President for Facilities and Real Estates Services, Chief Financial Officer of the Health System, Vice Provost for Research and Vice President and Chief of Staff. In addition, we would like to acknowledge and thank Mr. Scott Douglass for his contributions during his two and a half year tenure as the University's Vice President for Finance and Treasurer; a search for his replacement is underway.

FY 07 was also a year spent mapping out and coordinating efforts to unite the three major University initiatives into a focused, long-range plan with a clear direction and ambitious

Endowment Value
(in millions)



but attainable goals. The priorities of the Penn Compact are now synonymous with the goals of the *Making History* campaign and Penn Connects.

The early days of FY 08 saw the first results of this union:

Penn Compact – Several new programs were inaugurated, including the Penn Global Development Initiative (GDI) International Internship Program in collaboration with the Save the Children Federation and Penn World Scholars.

Making History – The five-year public phase of the fund-raising campaign, Making History, was launched on October 20, 2007. A substantial percentage of the $3.5 billion goal was already raised during the two year silent phase. Complete details on the campaign are available online at http://www.makinghistory.upenn.edu/

Penn Connects – After years of planning and negotiations, Penn took possession of the former U.S. postal properties. Penn has partnered with Brandywine Realty Trust to create development plans for the historic 30th Street Post Office as well as the surrounding area. At the same time, the design for Penn Park was added to the drawing board.

With these initiatives in mind, the University is entering an exciting period of unparalleled development and growth. Thanks to our distinguished faculty, talented students, and dedicated staff for providing the enthusiasm and energy necessary to reach our institutional objectives. Under the leadership of President Amy Gutmann, Penn is well-poised to achieve substantial results in the future as we look to sustain and enhance our institution.

Craig R. Carnaroli

Craig R. Carnaroli
Executive Vice President

A guiding principle of the Penn Connects plan is to connect the University to Center City through several major new open spaces and development that will improve the existing campus and help establish the east campus area as a vibrant new district. The greatly enhanced campus will allow for increased opportunities for research interaction in academic and social settings, and will foster connectivity with its broader urban context. Visit https://www.pennconnects.upenn.edu/

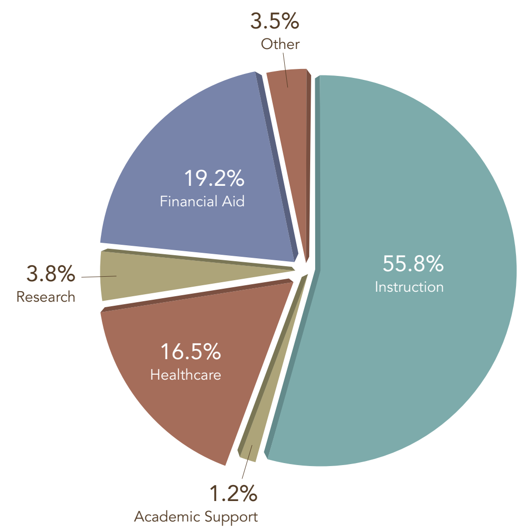
The development of the postal lands provides the University with the opportunity to build new structures to serve a wide range of programming priorities, including the need for athletic and recreation facilities, interdisciplinary research space, housing, student centers, conference facilities, retail shopping and dining, daycare space and non-academic offices. A phasing strategy allows for the seamless assimilation of the new facilities into the existing campus, in coordination with the strategic, financial and operational plans of the University.

Endowment and Investments

Penn's endowment ended FY 07 with $6.6 billion in investment assets. This represents an increase of almost 25% over the prior year-end due to a combination of new gifts, transfers and investment income. Over the course of the fiscal year, payouts from the endowment provided $176 million in budgetary support to the University.

Penn's total endowment is comprised of numerous individual endowments benefiting the full spectrum of Penn's schools and centers, and serves a variety of purposes as shown in the chart to the right.

Endowment by Purpose



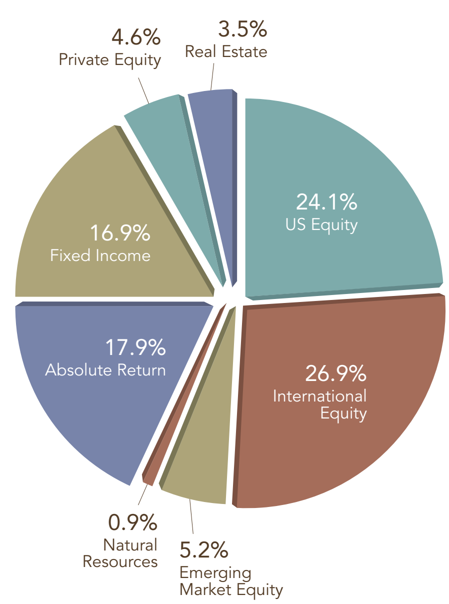
Associated Investments Fund

The vast majority of the endowment (92%) is invested in the Associated Investments Fund (AIF), a pooled investment vehicle in which the many individual endowments and trusts hold shares or units. The AIF had a market value of $6.1 billion as of June 30, 2007.

The AIF is managed by the Office of Investments under the oversight of an Investment Board appointed by the Trustees of the University. Over the past decade, the University has expanded the Office of Investments to ensure adequate oversight of an increasingly complicated portfolio.

The AIF is invested with the goal of achieving high, steady absolute returns while protecting against any permanent loss of capital. The portfolio is well diversified across asset classes and geographies. Approximately 56% of the portfolio is invested in public equities, 27% in alternatives (hedge funds, real estate, private equity and natural resources) and the remainder in fixed income. More than a third of the portfolio is invested overseas.

AIF Asset Allocation 6/30/07



AIF Performance

For FY 07, the AIF returned 20.2% versus the composite benchmark of 18.7% for an outperformance of 150 basis points. This represents the endowment's best performance in a decade with all asset classes registering impressive gains on account of strong global growth, solid earnings news and low interest rates. The US and international equity portfolios were each up more than 20%, emerging markets were up more than 40% and the alternatives portfolio (absolute return, private equity, real estate and natural resources) generated returns of more than 20%.

The table below shows the performance of the AIF for the past one, three, five and ten years. The portfolio has outperformed the composite benchmark for each of these periods. Recent performance has benefited from increased portfolio diversification and a somewhat more aggressive investment stance.

Performance Comparison
Periods Ended June 30, 2007
Annualized Returns (%)

Category	1 Year	3 Years	5 Years	10 Years
Associated Investments Fund (AIF)	20.2	13.6	12.4	8.9
Composite Index *	18.7	13.0	11.3	7.7
70% Russell 3000/30% Lehman Govt/Credit	15.8	10.0	9.9	7.5

* The Composite Index is a benchmark that weights the Russell 3000, MSCI World ex-US, MSCI Emerging Markets, NCREIF and Lehman Government indices proportional to the weights of the underlying assets classes in the AIF strategic asset allocation.

AIF Spending Rule

The University's endowment spending policy balances the objectives of maximizing budgetary support to endowed programs while ensuring that the purchasing power of the endowment is protected against inflation. The University has a target payout rate of 4.7%, with the actual payout in any given year determined by a formula designed to smooth the impact of short-term market moves on the endowment's value. For FY 07, the University adopted a new spending policy under which the spending rule distribution is the sum of: (i) 70% of the prior fiscal year distribution adjusted by an inflation factor; and (ii) 30% of the prior year-end market value of the AIF multiplied by 4.7%.

A Five-Year Review of Investments

(in thousands)

	2007	2006	2005	2004	2003
Investments:					
Investments:					
Fair Value					
Stocks	$3,662,497	$2,354,324	$2,155,577	$1,932,096	$1,548,637
Bonds	692,247	824,692	1,122,377	1,017,242	1,101,299
Short-term	752,835	1,014,993	331,897	367,685	354,914
Real estate	251,504	197,536	172,536	131,087	133,367
Absolute return	1,105,885	843,133	712,546	594,323	498,394
Private equity	288,036	207,275	159,279	118,154	81,875
Natural resources	57,202	34,909	14,812	0	0
Other	1,383	2,021	4,040	4,757	6,432
Total Investments*	6,811,589	5,478,883	4,673,064	4,165,344	3,724,917
Endowment:					
Fair Value	6,635,187	5,313,268	4,369,782	4,018,660	3,547,473
Associated Investments Fund:					
Fair Value	$6,108,050	$4,751,157	$3,873,965	$3,356,467	$2,859,041

* Total investments held by the University not invested in the Associated Investment Fund include $271 million held in trust, $10 million in assets held under indenture and escrow agreements, $108 million held in internally managed trusts, $277 million in other investments held by UPHS and $34 million in other investments held by the University. Total investments exclude securities held as collateral under a securities lending program.

Management Responsibilities for Financial Statements

The management of the University of Pennsylvania is responsible for the preparation, integrity and fair presentation of the financial statements. The financial statements, presented on pages 21 to 23, have been prepared in accordance with generally accepted accounting principles and, as such, include amounts based on judgments and estimates by management. The University also prepared the other information included in this annual report and is responsible for its accuracy and consistency with the financial statements.

The financial statements have been audited by the independent accounting firm PriceWaterhouseCoopers LLP, which was given unrestricted access to all financial records and related data, including minutes of all meetings of trustees. The University believes that all representations made to the auditors during their audit were valid and appropriate. PriceWaterhouseCoopers' audit opinion is presented on page 20.

The University maintains a system of internal controls over financial reporting, which is designed to provide a reasonable assurance to the University's management and board of trustees regarding the preparation of reliable published financial statements. Such controls are maintained by the establishment and communication of accounting and financial policies and procedures, by the selection and training of qualified personnel, and by an internal audit program designed to identify internal control weaknesses in order to permit management to take appropriate corrective action on a timely basis. There are, however, inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention of controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to financial statement preparation. Furthermore, the effectiveness of the internal control system can change with circumstances.

The trustees of the University of Pennsylvania, through the Committee on Audit and Compliance comprised of trustees not employed by the University, is responsible for engaging the independent auditors and meeting with management, internal auditors and the independent auditors to ensure that each carry out their responsibilities. Both internal auditors and the independent auditors have full and free access to the Committee on Audit and Compliance.

Amy Gutmann
President

Craig R. Carnaroli
Executive Vice President

Frank Claus
Vice President for Finance and Treasurer (interim)

John Horn
Comptroller

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Two Commerce Square, Suite 1700
2001 Market Street
Philadelphia PA 19103-7042
Telephone (267) 330 3000
Facsimile (267) 330 3300

Report of Independent Auditors

To the Trustees of the University of Pennsylvania:

In our opinion, the accompanying statements of financial position and the related statements of activities and cash flows, present fairly, in all material respects, the financial position of the University of Pennsylvania (the University) at June 30, 2007, and June 30, 2006, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

October 22, 2007

Statement of Financial Position

University of Pennsylvania
(in thousands)

	June 30, 2007	June 30, 2006
Assets		
Cash and cash equivalents	$ 739,660	$ 862,789
Accounts receivable,		
net of allowances of $10,463 and $11,224	138,674	140,326
Patient receivables,		
net of allowances of $105,633 and $110,946	250,090	219,113
Contributions receivable, net	379,422	326,663
Loans receivable,		
net of allowances of $2,994 and $3,083	94,155	89,455
Other assets	134,007	122,718
Assets held for sale	6,835	
Investments, at fair value	7,307,482	5,699,086
Plant, net of depreciation	3,067,833	2,909,176
Total assets	$ 12,118,158	$ 10,369,326
Liabilities		
Accounts payable	$ 90,411	$ 93,179
Accrued expenses and other liabilities	905,593	861,678
Collateral due broker	495,893	220,203
Deferred income	78,052	80,266
Deposits, advances, and agency funds	132,049	123,099
Federal student loan advances	77,247	77,737
Accrued retirement benefits	293,226	215,303
Debt obligations	1,333,060	1,374,459
Total liabilities	3,405,531	3,045,924
Net assets		
Unrestricted	4,273,780	3,612,342
Temporarily restricted	2,313,624	1,757,485
Permanently restricted	2,125,223	1,953,575
	8,712,627	7,323,402
Total liabilities and net assets	$ 12,118,158	$ 10,369,326

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

Statement of Activities

University of Pennsylvania
for the years ended June 30, 2007 and 2006 (in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	2007	2006
Revenue and other support:					
Tuition and fees, net	$ 638,143			$ 638,143	$ 599,190
Commonwealth appropriations	49,429			49,429	44,866
Sponsored programs	726,625			726,625	746,231
Contributions	45,400	$ 63,726		109,126	100,083
Investment income	163,116	108,832		271,948	236,430
Hospitals and physician practices	2,619,941			2,619,941	2,386,850
Sales and services of auxiliary enterprises	96,789			96,789	93,820
Other income	181,100			181,100	166,381
Independent operations	63,782			63,782	58,868
Net assets released from restrictions	186,691	(186,691)			
	4,771,016	(14,133)		4,756,883	4,432,719
Expenses:					
Program:					
Instruction	847,491			847,491	800,863
Research	592,225			592,225	592,791
Hospitals and physician practices	2,361,208			2,361,208	2,225,647
Auxiliary enterprises	111,813			111,813	109,820
Other educational activities	153,233			153,233	134,388
Student services	46,397			46,397	41,753
Support:					
Academic support	60,807			60,807	57,613
Management and general	190,233			190,233	177,544
Independent operations	60,214			60,214	57,176
	4,423,621			4,423,621	4,197,595
Increase (decrease) in net assets before nonoperating revenue, net gains, reclassifications and other	347,395	(14,133)		333,262	235,124
Nonoperating revenue, net gains, reclassifications and other.					
Gain on investment, net	351,137	509,963	$ 59,644	920,744	418,129
Investment income, net of amounts classified as operating revenue	(19,293)	(41,885)	1,529	(59,649)	(53,690)
Contributions	28,462	123,027	110,475	261,964	308,791
Change in minimum pension liability					45,953
Income from discontinued operations	394			394	
Net assets released from restrictions	20,833	(20,833)			
Increase in net assets before cumulative effect of change in accounting principle	728,928	556,139	171,648	1,456,715	954,307
Cumulative effect of change in accounting principle	(67,490)			(67,490)	(18,820)
Increase in net assets after cumulative effect of change in accounting principle	661,438	556,139	171,648	1,389,225	935,487
Net assets, beginning of year	3,612,342	1,757,485	1,953,575	7,323,402	6,387,915
Net assets, end of year	$ 4,273,780	$ 2,313,624	$ 2,125,223	$ 8,712,627	$ 7,323,402

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

Statement of Cash Flows

University of Pennsylvania
for the years ended June 30, 2007 and 2006 (in thousands)

	2007	2006
Cash flows from operating activities:		
Increase in net assets	$ 1,389,225	$ 935,487
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	234,684	211,500
Provision for bad debts	130,435	145,617
Gain on investments, net	(920,744)	(418,129)
Loss on disposal of plant, property and equipment	886	509
Donated equipment	(2,839)	(493)
Nonoperating income designated for the acquisition of long-lived assets and long-term investment	(202,709)	(255,101)
Change in minimum pension liability		(45,953)
Cumulative effect of change in accounting principle	67,490	18,820
Changes in operating assets and liabilities:		
Patient, accounts and loans receivable	(144,678)	(16,833)
Contributions receivable	5,385	7,215
Other assets	(6,342)	14,770
Accounts payable, accrued expenses and accrued retirement benefits	16,681	105,999
Deposits, advances and agency funds	8,950	6,120
Deferred income	(2,214)	4,056
Net cash provided by operating activities	574,210	713,584
Cash flows from investing activities:		
Purchase of investments	(10,158,231)	(8,110,486)
Proceeds from sale of investments	9,717,059	7,700,285
Purchase of plant, property and equipment	(388,357)	(368,236)
Net cash used by investing activities	(829,529)	(778,437)
Cash flows from financing activities:		
Proceeds from contributions received designated for the acquisition of long-lived assets and long-term investment	172,673	199,584
Federal student loan advances	(490)	(591)
Repayment of long-term debt	(49,293)	(128,886)
Proceeds from issuance of long-term debt	9,300	146,113
Net cash provided by financing activities	132,190	216,220
Net (decrease) increase in cash and cash equivalents	(123,129)	151,367
Cash and cash equivalents, beginning of year	862,789	711,422
Cash and cash equivalents, end of year	$ 739,660	$ 862,789
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of amounts capitalized	$ 51,043	$ 50,169

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

Notes to Financial Statements

1. Significant Accounting Policies

Organization

The University of Pennsylvania (the University), located in Philadelphia, Pennsylvania, is an independent, nonsectarian, not-for-profit institution of higher learning founded in 1740. The University Academic Component (Academic Component) provides educational services, primarily for students at the undergraduate, graduate, professional and postdoctoral levels and performs research, training and other services under grants, contracts and similar agreements with sponsoring organizations, primarily departments and agencies of the United States Government. The University also operates an integrated healthcare delivery system, the University of Pennsylvania Health System (UPHS). The University is a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code.

Basis of Presentation

The financial statements have been prepared on the accrual basis and include the accounts of the University of Pennsylvania and its subsidiaries. All material transactions between the University and its subsidiaries have been eliminated.

The net assets of the University are classified and reported as follows:

> *Unrestricted -* Net assets that are not subject to donor-imposed restrictions.
>
> *Temporarily restricted -* Net assets that are subject to legal or donor-imposed restrictions that will be met by actions of the University and/or the passage of time. These net assets include gifts donated for specific purposes and capital appreciation on permanent endowment, which is restricted by Pennsylvania law on the amounts that may be expended in a given year.
>
> *Permanently restricted -* Net assets that are subject to donor-imposed restrictions that require the original contribution be maintained in perpetuity by the University, but permits the use of certain investment earnings for general or specific purposes.

Expenses are reported as a decrease in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions recognized on net assets are reported as net assets released from restrictions from temporarily restricted net assets to unrestricted net assets. Donor-restricted resources intended for the acquisition or construction of long-lived assets are initially reported as temporarily restricted net assets and released from restrictions from temporarily restricted net assets to unrestricted net assets when the asset is placed in service.

The financial statements include certain prior-year summarized comparative information in total, but not by net asset category. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the University's financial statements for the year ended June 30, 2006 from which the summarized information was derived. Certain reclassifications have been made to the summarized financial information for comparative purposes.

Cash and Cash Equivalents

Cash equivalents include short-term, highly liquid investments and are carried at cost which approximates fair value. Short-term investments with maturities of three months or less when purchased are classified as cash equivalents, except for restricted investments which are classified as Investments.

Investments

Investments in equity and debt securities with readily determinable fair values are reported at fair value. Changes in fair value of investments are reported in the University's Statement of Activities. Fixed income investments with a maturity of less than one year when purchased are

Notes to Financial Statements

included in short-term investments. Derivative financial instruments held for investment purposes are carried at fair value with the resulting gains and losses included in investment earnings for the period. For the fiscal years ended June 30, 2007 and 2006, the University's principal derivative financial instruments are domestic and international equity future contracts and forward currency contracts. Alternative investments that include certain hedge funds, private equity, natural resources and real estate investments held through limited partnerships or commingled funds are carried at estimated fair value provided by the management of the alternative investment partnerships or funds as of March 31, 2007 and 2006, as adjusted by cash receipts, cash disbursements, and securities distributions through June 30, 2007 and 2006.

The University believes that the carrying amount of its alternative investments is a reasonable estimate of fair value as of June 30, 2007 and 2006. Because alternative investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investments existed and such differences could be material.

The majority of the endowment funds of the University have been pooled in the University's Associated Investments Fund (AIF), which is invested in equities, bonds, hedge funds, natural resources, private equity and real estate limited partnerships. The University has adopted an endowment spending policy governing the expenditure of the total return of funds invested in the AIF. The spending policy is designed to manage annual spending levels and is independent of the cash yield and appreciation of investments for the year. Effective July 1, 2006, the University adopted a new spending policy under which the spending rule distribution is the sum of: (i) 70% of the prior fiscal year distribution adjusted by an inflation factor; and (ii) 30% of the prior year-end market value of the AIF multiplied by 4.7%. For the fiscal year ended June 30, 2006, the spending policy for the AIF was 4.7% of the three-year average market value lagged one year.

Loans Receivable

Student loans receivable are reported at their net realizable value. Such loans include donor-restricted and federally-sponsored student loans with mandated interest rates and repayment terms. Determination of the fair value of student loans receivable is not practicable.

Plant

Plant is stated at cost, or fair value at the date of donation, less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets. Upon disposal of assets, the cost and related accumulated depreciation are removed from the accounts and the resulting net gain or loss is included in total expenses. Rare books and other collectibles, which appreciate in value, are not subject to depreciation.

Conditional Asset Retirement Obligations

In March 2005, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" (FIN 47), which was effective for the University as of July 1, 2005. FIN 47 was issued to provide clarity surrounding the recognition of conditional asset retirement obligations, as referred to in FASB Statement No. 143, "Accounting for Asset Retirement Obligations." FIN 47 defines a conditional asset retirement obligation as a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. Uncertainty with respect to the timing and/or method of settlement of the asset retirement obligation, does not defer recognition of a liability. The obligation to perform the asset retirement activity is unconditional, and accordingly, a liability should be recognized. FIN 47 also provides guidance with respect to the criteria to be used to determine whether sufficient information exists to reasonably estimate the fair value of an asset retirement obligation. Based on the guidance in FIN 47, management of the University determined that sufficient information was available to reasonably estimate the fair value of known asset retirement obligations.

Notes to Financial Statements

FIN 47 required the initial application of the interpretation to be recognized as a cumulative effect of a change in accounting principle. Specifically, FIN 47 required the recognition, as a cumulative effect, the cumulative accretion and accumulated depreciation for the time period from the date the liability would have been recognized had the provisions of the interpretation been in effect when the liability was incurred to the date of adoption of this Interpretation. The liability incurred date is presumed to be the date upon which the legal requirement to perform the asset retirement activity was enacted. The University's conditional asset retirement obligations primarily relate to asbestos contained in buildings and underground steam distribution piping.

Upon initial application of FIN 47, the University recognized $18,820,000 as the Cumulative effect of a change in accounting principle in the Statement of Activities.

Conditional asset retirement obligations, included within Accrued expenses and other liabilities in the Statement of Financial Position are as follows (in thousands):

June 30, 2006	$ 20,960
Less: Payments	(171)
Add: Accretion	492
June 30, 2007	$ 21,281

Split-Interest Agreements

The University's split-interest agreements with donors consist primarily of charitable gift annuities, pooled income funds and irrevocable charitable remainder trusts for which the University serves as trustee. Assets are invested and payments are made to donors and/or other beneficiaries in accordance with the respective agreements.

Contribution revenue for charitable gift annuities and charitable remainder trusts is recognized at the date the agreement is established, net of the liability recorded for the present value of the estimated future payments. Contribution revenue for pooled income funds is recognized upon establishment of the agreement at the fair value of the estimated future receipts discounted for the estimated time period to complete the agreement.

The present value of payments to beneficiaries of charitable gift annuities and charitable remainder trusts and the estimated future receipts from pooled income funds are calculated using discount rates, which represent the risk-free rates in existence at the date of the gift. Gains or losses resulting from changes in actuarial assumptions and accretions of the discount are recorded as increases or decreases in the respective contribution revenue net asset category in the Statement of Activities.

Tuition and Fees

The University maintains a policy of offering qualified undergraduate applicants admission to the University without regard to financial circumstance. This policy provides financial aid to eligible students in the form of direct grants, loans and employment during the academic year. Tuition and fees have been reduced by certain grants and scholarships in the amount of $160,716,000 in 2007 and $153,299,000 in 2006.

Sponsored Programs

The University receives grant and contract revenue from governmental and private sources. In 2007 and 2006, grant and contract revenue earned from governmental sources totaled $615,281,000 and $643,407,000, respectively. The University recognizes revenue associated with the direct and the applicable indirect costs of sponsored programs as the related costs are incurred. The University negotiates its federal indirect rate with its cognizant federal agency. Indirect costs recovered on federally-sponsored programs are generally based on predetermined reimbursement rates, which are stated as a percentage and distributed based on the modified total direct costs incurred.

Notes to Financial Statements

Indirect costs recovered on all other grants and contracts are based on rates negotiated with the respective sponsors. Funds received for sponsored research activity are subject to audit. Based upon information currently available, management believes that any liability resulting from such audits will not materially affect the financial position or operations of the University.

Contributions

Contributions are reported as increases in the appropriate net asset category based on donor restrictions. Contributions, including unconditional promises to donate, are recognized as revenue in the period received. Unconditional pledges are recognized at their estimated net present value, net of an allowance for uncollectible amounts, and are classified in the appropriate net asset category. Unconditional promises to donate and contributions of cash and other assets designated for the acquisition of long-lived assets and long-term investment are reported with Nonoperating revenue, net gains, reclassifications and other.

Because of uncertainties with regard to their realizability and valuation, bequest intentions and other conditional promises are not estimated by management and are recognized if and when the specified conditions are met. Irrevocable bequest intentions where the donor is over 75 years of age are recorded as revenue in the year the intention is made at the estimated net present value of the gift.

Hospital and Physician Practices

Hospital and physician practices revenue is derived primarily from UPHS patient services and is accounted for at established rates on the accrual basis in the period the service is provided. Patient service revenue is net of charity care and community service. Certain revenue received from third-party payers is subject to audit and retroactive adjustment. Additionally, UPHS has entered into certain contracts under which it is responsible for providing medical care to covered members at predetermined rates. Any changes in estimates under these contracts are recorded in operations currently.

Allocation of Certain Expenses

The Statement of Activities presents expenses by functional classification. Operation and maintenance of plant and depreciation are allocated to functional classifications based on square footage. Interest expense is allocated to the functional classifications of the activity that directly benefited from the proceeds of the debt.

Use of Estimates

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

New Authoritative Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109" (FIN 48). This interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, "Accounting for Income Taxes." This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition and is effective for fiscal years beginning after December 15, 2006. Due to the fact that University operations are generally tax exempt, management believes at this time that the adoption of FIN 48 will not have a material impact on the consolidated financial statements.

Notes to Financial Statements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" (SFAS 157). SFAS 157 defines the term fair value, establishes a framework for measuring it within generally accepted accounting principles and expands disclosures about its measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. University management is currently evaluating the impact SFAS 157 will have on the consolidated financial statements beginning in fiscal year 2009.

In September 2006, the FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)" (SFAS 158), which is effective for the University as of June 30, 2007. SFAS 158 requires the recognition of a defined benefit postretirement plan's funded status as either an asset or liability on the balance sheet. SFAS 158 also requires the immediate recognition of the unrecognized actuarial gains and losses and prior service costs and credits that arise during the period as a Cumulative effect of a change in accounting principle. Additionally, the fair value of plan assets must be determined as of the University's year-end.

Upon initial application of SFAS 158, the University recognized $67,490,000 as the Cumulative effect of a change in accounting principle in the Statement of Activities (see Note 12).

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. University management is currently evaluating the impact SFAS 159 will have on the consolidated financial statements beginning in fiscal year 2009.

2. University of Pennsylvania Health System – Summarized Financial Information

The Trustees of the University of Pennsylvania formed Penn Medicine, the governance structure that oversees the activities of UPHS and the University of Pennsylvania School of Medicine. The governing body operates, oversees and coordinates the academic, research and clinical missions of Penn Medicine.

UPHS comprises the Clinical Practices of the University of Pennsylvania, Clinical Care Associates, Hospital of the University of Pennsylvania, Penn Presbyterian Medical Center, Pennsylvania Hospital of the University of Pennsylvania Health System and Wissahickon Hospice of the University of Pennsylvania Health System, Franklin Casualty Insurance Company, a wholly owned Risk Retention Group, and Quaker Insurance Company Ltd., a wholly owned offshore captive insurance company (collectively referred to as RRG/Captive).

Throughout the year, certain transactions are conducted between UPHS and the University. The effect of these transactions (primarily billings for allocations of common costs, physicians' salaries and benefits, certain purchased services and support for the School of Medicine) is included in the summarized financial information of UPHS. UPHS owed the University $11,540,000 at June 30, 2007, and the University owed UPHS $141,000 at June 30, 2006, which represents normal current inter-entity activity which is eliminated in the consolidated financial statements.

UPHS transferred to the School of Medicine from its operations $47,809,000 and $23,165,000 in 2007 and 2006, respectively, to further research and educational activities. These activities are integral to the overall mission of Penn Medicine and the effect of the transfers is reflected in UPHS, nonoperating, net. This transaction is eliminated in the consolidated financial statements.

Notes to Financial Statements

Final adjustments to revenue, resulting from settlements with third-party payers, are recorded in the year in which they are settled. The 2007 and 2006 Medicare net patient service revenue was increased by $49,037,000 and $4,248,000, respectively, as a result of final settlements and the revision or removal of allowances previously estimated that were no longer necessary.

During 2007, UPHS and Independence Blue Cross (IBC) reached agreement on terms of a new five-year agreement. Payments made for inpatient services provided to IBC traditional and managed care subscribers are effected on a per-case rate basis for most procedural based services and high-intensity medical cases (over 60% of all inpatient admissions in all) and a per diem basis for all other services. Payment for outpatient services is principally based upon negotiated fee schedules. Hospital rates also provide for annual inflationary increases.

During 2005, UPHS and Aetna reached agreement on terms of a five-year agreement. The terms of the agreement provide payments for inpatient hospital services on a per-case rate basis. Payments for outpatient services continue to be predominantly based upon negotiated fee schedules.

UPHS also has reimbursement agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for reimbursement under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

Notes to Financial Statements

Summarized financial information for UPHS as of and for the years ended June 30, 2007 and 2006, prior to eliminations for transactions between UPHS and other entities of the University, is as follows (in thousands):

	2007	2006
Net patient service	$ 2,470,757	$ 2,248,005
Other revenue	162,188	149,724
Total expenses	(2,374,401)	(2,239,328)
Excess of revenues over expenses from operations	258,544	158,401
Other unrestricted income, net	122,204	64,395
Excess of revenue over expenses	380,748	222,796
Nonoperating, net	32,989	89,243
Unrealized gain, net	17,808	7,913
Cumulative effect of change in accounting principle	975	(8,183)
Increase in net assets	$ 432,520	$ 311,769
Total current assets	$ 697,318	$ 648,189
Assets whose use is limited (including board-designated funds of $607,394 and $516,659 and trustee-held funds of $11,991 and $68,427 for 2007 and 2006, respectively)	1,176,746	1,090,858
Plant, net of depreciation	817,783	653,927
Investments and other assets	224,560	78,366
Total assets	$ 2,916,407	$ 2,471,340
Total current liabilities	$ 425,999	$ 395,719
Long-term debt, net of current portion	703,263	741,141
Other liabilities	384,242	364,097
Total liabilities	1,513,504	1,500,957
Net assets		
Unrestricted	873,438	521,944
Temporarily restricted	394,604	321,645
Permanently restricted	134,861	126,794
Total net assets	1,402,903	970,383
Total liabilities and net assets	$ 2,916,407	$ 2,471,340

Notes to Financial Statements

In 2007, UPHS purchased several buildings and land from Tenet Health Systems Graduate, LLC, in Philadelphia. Upon renovation, UPHS intends to use several of the buildings for operations. The properties not intended for use, both land and buildings, are recorded as Assets held for sale at their allocated cost of $6,835,000.

3. Investments

A summary of investments, stated at fair value, at June 30, 2007 and 2006, is as follows (in thousands):

	2007	2006
Short-term	$ 1,248,592	$ 1,234,997
Stocks	3,662,497	2,354,324
Bonds	692,383	824,891
Real estate	251,504	197,536
Absolute return	1,105,885	843,133
Private equity	288,036	207,275
Natural resources	57,202	34,909
Other	1,383	2,021
End of year	$ 7,307,482	$ 5,699,086
Beginning of year	$ 5,699,086	$ 4,859,151

The University employs derivative instruments (futures as well as currency forwards) to replicate long-only equity exposure more cost effectively and conveniently than by purchasing the underlying securities. The notional exposure of these instruments was approximately $672,405,000 as of June 30, 2007 and $419,560,000 as of June 30, 2006. The fair market value of these instruments, included in the value of Stocks, was $687,925,000 as of June 30, 2007 and $426,867,000 as of June 30, 2006. Included in these instruments are $27,221,000 and $22,554,000 of U.S. Treasury securities that were pledged as collateral to meet margin requirements under certain futures contracts at June 30, 2007 and 2006, respectively.

Included in investments are assets held in trust for the University with an aggregate fair value of $386,099,000 at June 30, 2007 and $353,566,000 at June 30, 2006.

In connection with a University-sponsored loan program, the University is required to invest in certificates of deposit of the lending institution. At June 30, 2007 and 2006, short-term investments held under this arrangement aggregated $2,807,000 and $3,221,000, respectively.

At June 30, 2007 and 2006, investments with a fair value of $10,244,000 and $71,841,000, respectively, were held by trustees under indenture and escrow agreements.

Included in investments is $6,899,000 and $5,273,000 of cash that is held in escrow at June 30, 2007 and 2006, respectively.

At June 30, 2007 and 2006, investments with a fair value of $483,072,000 and $214,633,000, respectively, were loaned on an overnight basis to various brokers. The University receives lending fees and continues to earn interest and dividends on the loaned securities. These securities are returnable on demand and are collateralized by cash deposits and U.S. Treasury obligations. Cash deposits included in short-term investments are $495,757,000 and $220,004,000 at June 30, 2007 and 2006, respectively. U.S. Treasury obligations included in

Notes to Financial Statements

Bonds are $136,000 and $199,000 at June 30, 2007 and 2006, respectively. The University is indemnified against borrower default by the financial institution that is acting as its lending agent.

At June 30, 2007 and 2006, short-term investments include $20,313,000 and $32,381,000, respectively, of outstanding receivables from trading activities. At June 30, 2007 and 2006, short-term investments include $603,000 and $21,601,000, respectively, of outstanding payables from trading activities.

The University is obligated under certain limited partnership investment fund agreements to advance additional funding periodically up to specified levels. At June 30, 2007, the University had unfunded commitments of $798,328,000 to a variety of private equity, real estate, natural resources and other drawdown funds. Based upon past experience, the University expects these commitments to be funded over the next three to five years depending on market conditions.

A summary of the University's total investment return for the years ended June 30, 2007 and 2006, as reported in the Statement of Activities, is presented below (in thousands):

	2007	2006
AIF investment income	$ 127,247	$ 100,551
AIF realized and unrealized gains	883,779	388,298
Return on AIF	1,011,026	488,849
Other investment income and gains	122,017	112,020
Total return on investments	$ 1,133,043	$ 600,869

Income distributed for operations under the AIF spending rule exceeded available income, net of expenses and net of income permanently reinvested by $68,184,000 in 2007 and by $62,554,000 in 2006.

Investments include amounts held to meet legally mandated annuity reserves of $28,140,000 and $31,093,000 as of June 30, 2007 and 2006, respectively, as required by the laws of the following states where certain individual donors reside: California, New Jersey and New York.

4. Accounts Receivable

The major components of receivables, net of reserve for doubtful accounts of $10,463,000 and $11,224,000 at June 30, 2007 and 2006, respectively, are as follows (in thousands):

	2007	2006
Sponsored research	$ 62,979	$ 67,365
Student	16,513	12,134
Trade	33,965	32,332
Investment income	7,348	7,717
Other	17,869	20,778
Total Accounts receivable	$ 138,674	$ 140,326

Notes to Financial Statements

5. Contributions Receivable

A summary of contributions receivable is as follows at June 30, 2007 and 2006 (in thousands):

	2007	2006
Unconditional promises expected to be collected in:		
Less than one year	$ 161,923	$ 145,623
One year to five years	307,928	251,777
Over five years	16,729	23,197
	486,580	420,597
Less: Discount and allowance for doubtful amounts	(107,158)	(93,934)
Contributions receivable, net	$ 379,422	$ 326,663

6. Other Assets

The major components of other assets at June 30, 2007 and 2006, respectively, are as follows (in thousands):

	2007	2006
Goodwill	$ 29,865	$ 31,585
Defined benefit pension asset	37,011	23,173
Inventory	22,473	23,398
Prepaid expenses	19,069	19,492
Deferred financing fees	14,633	16,215
Other	10,956	8,855
Total Other assets	$ 134,007	$ 122,718

Goodwill of $29,865,000 at June 30, 2007, and $31,585,000 at June 30, 2006, associated with the statutory merger of the Presbyterian Medical Center of Philadelphia into UPHS is being amortized over thirty years on a straight-line basis.

Notes to Financial Statements

7. Plant, net of depreciation

The components of plant at June 30, 2007 and 2006, are as follows (in thousands):

	2007	2006
Land	$ 110,791 (a)	$ 91,969
Buildings and fixed equipment	3,842,181 (a)	3,919,574
Contents	787,332	1,081,712
Construction-in-progress	348,538	241,178
	5,088,842	5,334,433
Less: accumulated depreciation	(2,021,009)	(2,425,257)
Plant, net of depreciation	$ 3,067,833	$ 2,909,176

(a) Includes $3,209,000 of land and $4,037,000 of completed facilities which serve as collateral for debt obligations.

The University recorded $233,180,000 and $209,183,000 of depreciation expense for the years ended June 30, 2007 and 2006, respectively. Rare books and other collectibles aggregate $23,809,000 at June 30, 2007, and $21,262,000 at June 30, 2006.

8. Split-Interest Agreements

The liability to donors and beneficiaries under terms of split-interest agreements included in Accrued expenses and other liabilities is as follows (in thousands):

	2007	2006
Charitable gift annuities	$ 25,159	$ 25,791
Charitable remainder trusts	27,429	31,238
Pooled income funds	1,332	1,206
Total split-interest agreements	$ 53,920	$ 58,235

Notes to Financial Statements

9. Debt Obligations

Debt obligations at June 30, 2007 and 2006, are as follows (in thousands):

	Maturity	Interest Rate at June 30, 2007	June 30, 2007	June 30, 2006
Academic Component:				
Fixed Rate Debt Obligations:				
Pennsylvania Higher Education Facility Authority (PHEFA)				
Series C of 2005 Revenue Bonds	09/2038	3.20% - 5.00%	$ 141,620	$ 141,620
Unamortized Premium			4,095	4,312
Series A of 2005 Revenue Bonds	09/2025	3.00% - 5.00%	34,905	37,655
Unamortized Premium			1,344	1,553
Series B of 2005 Revenue Bonds	09/2015	5.00% - 5.25%	62,420	66,930
Unamortized Premium			4,134	5,114
Series A of 2002 Revenue Bonds	07/2008	4.00% - 5.00%	6,270	9,185
Unamortized Premium			37	107
Series of 1998 Revenue Bonds	07/2038	4.50% - 4.75%	111,255	113,600
Unamortized Discount			(957)	(1,028)
Department of Education Bonds	03/2007	N/A		60
Other Loans	Various	3.00% - 7.85%	1,088	3,626
Total Fixed Rate Debt Obligations			366,211	382,734
Variable Rate Debt Obligations:				
PHEFA				
Series B of 2002 Revenue Bonds	07/2032	3.75%	47,350	48,150
Series of 1990 Revenue Bonds	12/2020	3.85%	6,500	6,500
Series of 1985 Revenue Bonds	12/2015	3.85%	10,610	10,610
Quakertown General Authority Series of 2004	07/2034	3.63%	77,700	77,700
Washington County Authority Series of 2004	07/2034	3.76%	62,500	62,500
Other Loans	Various	4.30% - 5.92%	24,150	14,928
Total Variable Rate Debt Obligations			228,810	220,388
Total Academic Component Debt Obligations			595,021	603,122
UPHS:				
Fixed Rate Debt Obligations:				
PHEFA				
Series A of 2005 Revenue Bonds	08/2023	4.25% - 5.00%	260,375	272,980
Unamortized Premium			15,514	18,284
Series B of 2005 Revenue Bonds	08/2018	3.00% - 5.00%	80,655	86,555
Unamortized Premium			1,803	2,119
Series of 2004 Revenue Bonds	11/2010	3.35%	16,875	21,250
Pennsylvania Hospital Series of 2004	01/2024	7.50%	89,235	89,235
Series of 2002 Revenue Bonds	01/2024	7.50%	23,610	24,290
Series A of 1998 Revenue Bonds	01/2015	4.50% - 5.38%	37,115	38,750
Unamortized Premium			407	457
Capital Leases and notes payable	04/2009	4.64%	9,075	13,442
Total Fixed Rate Debt Obligations			534,664	567,362
Variable Rate Debt Obligations:				
PHEFA				
Series C of 2005 Revenue Bonds	4/2024	3.80%	103,675	103,675
Series D of 2005 Revenue Bonds	4/2027	3.75%	92,400	92,400
Pennsylvania Economic Development Financing Authority Series C of 1994 Revenue Bonds	09/2015	5.35%	7,300	7,900
Total Variable Rate Debt Obligations			203,375	203,975
Total UPHS Debt Obligations			738,039	771,337
Total University Debt Obligations			$ 1,333,060	$ 1,374,459

Notes to Financial Statements

The fair value of the University's debt obligations was $1,320,506,000 and $1,360,922,000 at June 30, 2007 and 2006, respectively. The fair value represents the quoted market value for PHEFA Revenue Bonds and Department of Education Bonds and carrying amounts for all other debt, which approximates fair value.

The University had unused letters of credit with various financial institutions in the amounts of $76,032,000 and $75,932,000 at June 30, 2007 and 2006, respectively.

Maturities of debt obligations are as follows (in thousands):

Fiscal Year	Amount
2008	$ 49,545
2009	52,721
2010	54,241
2011	47,987
2012	59,248
Thereafter	1,042,941
Total Principal	1,306,683
Unamortized Premium/Discount	26,377
Total Debt	$ 1,333,060

Academic Component

On August 18, 2005, PHEFA issued Revenue Bonds, Series 2005C ("PHEFA 2005C Bonds"), with an aggregate principal amount of $141,620,000. The proceeds were used to fund a construction project of approximately $70,000,000 and to fund an escrow that will be used to refund $72,640,000 from the PHEFA Series of 1998 Revenue Bonds ("Refunded 1998 Bonds"). The Refunded 1998 Bonds were legally defeased and, as such, have been excluded from the University's reported liabilities after August 18, 2005. The Refunded 1998 Bonds will be retired when they become callable on July 15, 2008. $113,600,000 of the PHEFA 1998 Bonds were not refunded and will be paid as they become due.

The note payable to the Redevelopment Authority of the City of Philadelphia, with an outstanding principal balance of $7,336,247, was satisfied on August 26, 2005.

UPHS

Pennsylvania Higher Education Facilities Authority Revenue Bonds

The PHEFA Revenue Bonds, exclusive of Series of 2004 and 2002, are secured by master notes issued under the UPHS Master Trust Indenture (MTI). The MTI and related agreements contain certain restrictive covenants that limit the issuance of additional indebtedness, and among other things, require UPHS to meet an annual debt service coverage requirement of "income available for debt service" (excess of revenue over expenses plus depreciation, amortization, interest expense and extraordinary items) at an amount equal to 110% of the annual debt service requirements. If the coverage requirement for a particular year is not met, within six months of the close of that fiscal year UPHS must retain the services of a consultant to make recommendations to improve the coverage requirement. UPHS must also implement the recommendations of the consultant to the extent that they can be feasibly implemented. UPHS will not be considered to be in default of the provisions of the MTI so long as UPHS has sufficient cash flow to pay total operating expenses and to pay debt service for the fiscal year. In both 2007 and 2006, UPHS met its debt service coverage requirement under the MTI. Additionally, UPHS has pledged its gross revenues to secure its obligation under the MTI.

10. Natural Classification of Expenditures

Expenses incurred were for (in thousands):

	Compensation	Student Aid	Depreciation	Interest	Other Operating	Total
June 30, 2007						
Instruction	$ 519,912	$ 48,428	$ 40,909	$ 2,598	$ 235,644	$ 847,491
Research	334,773	8,820	35,583	9,153	203,896	592,225
Hospitals and physician practices	1,278,651		95,019	28,504	959,034	2,361,208
Auxiliary enterprises	22,932		17,131	4,288	67,462	111,813
Other educational activities	92,419	17	7,321	227	53,249	153,233
Student services	25,863	171		77	20,286	46,397
Academic support	27,746		21,622	552	10,887	60,807
Management and general	150,633	45	12,519	377	26,659	190,233
Independent operations	6,569		3,076	2,106	48,463	60,214
Total	$ 2,459,498	$ 57,481	$ 233,180	$ 47,882	$ 1,625,580	$ 4,423,621
June 30, 2006	$ 2,345,349	$ 56,009	$ 209,183	$ 51,824	$ 1,535,230	$ 4,197,595

11. Operating Leases

The University leases research labs, office space and equipment under operating leases expiring through February 2027. Rental expense for the years ended June 30, 2007 and 2006 totaling $50,655,000 and $47,035,000, respectively, is included in the accompanying Statement of Activities.

At June 30, 2007, future minimum lease payments under operating leases with remaining terms greater than one year were as follows (in thousands):

2008	$ 41,328
2009	38,410
2010	35,108
2011	29,279
2012	24,612
Thereafter	145,002
Total minimum lease payments	$ 313,739

Notes to Financial Statements

12. Pension and Other Postretirement Benefit Costs

Retirement benefits are provided for academic employees and certain administrative and support personnel through a defined contribution plan. The University's policy with respect to its contribution is to provide up to 9% of eligible employees' salaries. The University's contributions amounted to $72,182,000 in 2007 and $67,951,000 in 2006.

The University has noncontributory defined benefit pension plans for substantially all other full-time employees. Benefits under these plans generally are based on the employee's years of service and compensation during the years preceding retirement. Contributions to the plans are made in amounts necessary to at least satisfy the minimum required contributions as specified in the Internal Revenue Service Code and related regulations.

Clinical Care Associates has a non-contributory defined contribution retirement plan covering all eligible employees. Clinical Care Associates has also established a non-qualified supplemental retirement plan to provide retirement benefits to a select group of physician employees. Contributions to these plans are based upon the annual compensation of the eligible employees. Retirement plan expense was $3,199,000 and $3,171,000 for 2007 and 2006, respectively.

Effective June 30, 2007, the University adopted FAS 158, which requires that the Statement of Financial Position reflect the funded status of the pension and postretirement plans. The funded status of the plans is measured as the difference between the plan assets at fair value and the projected benefit obligation or accumulated postretirement benefit obligation. The University has recognized the aggregate of all overfunded plans in Other Assets and the aggregate of all underfunded plans in Accrued Retirement Benefits in the Statement of Financial Position.

At June 30, 2007, previously unrecognized differences between actual amounts and estimates based on actuarial assumptions are included in Unrestricted Net Assets in our Statement of Financial Position as required by FAS 158. In future reporting periods, the difference between actual amounts and estimates based on actuarial assumptions will be recognized in Change in Unrestricted Net Assets in the period in which they occur.

Incremental Effect of Adopting FAS 158

The incremental effect of adopting FAS 158 on individual line items in the Statement of Financial Position at June 30, 2007, is shown below (in thousands):

	Before Application of FAS 158	Adjustment	After Application of FAS 158
Prepaid benefit cost in other assets	$ 24,800	$ 12,211	$ 37,011
Liability for pension benefits in accrued retirement benefits	23,059	(9,442)	13,617
Other postretirement benefit liability in accrued retirement benefits	183,445	89,143	272,588
Unrestricted Net Assets	4,341,270	(67,490)	4,273,780
Total equity	8,780,117	(67,490)	8,712,627

Notes to Financial Statements

Net Periodic Cost

The components of net periodic benefit cost for pension benefits and other postretirement benefits are as follows (in thousands):

	Pension Benefits		Other Postretirement Benefits	
	06/30/2007	06/30/2006	06/30/2007	06/30/2006
Service Cost	$ 27,126	$ 30,304	$ 14,203	$ 14,991
Interest Cost	48,316	43,794	24,480	21,619
Expected Return on Plan Assets	(61,049)	(54,797)	(12,060)	(10,347)
Amortization of:				
Net Prior Service Cost/(Credit)	1,634	1,638	(3,664)	(3,664)
Net Losses/(Gains)	-	9,183	3,430	5,867
Net Periodic Benefit Cost	$ 16,027	$ 30,122	$ 26,389	$ 28,466

Obligations and Funded Status

The following shows changes in the benefit obligation, plan assets and funded status. Accrued retirement benefits includes $7,021,000 and $6,089,000 for faculty early retirement program at June 30, 2007 and 2006, respectively. Benefit obligation balances presented below reflect the projected benefit obligation (PBO) for pension plans and accumulated postretirement benefit obligations (APBO) for other postretirement benefits plans (in thousands):

	Pension Benefits		Other Postretirement Benefits	
	06/30/2007	06/30/2006	06/30/2007	06/30/2006
Change in Benefit Obligation				
Benefit Obligation at Beginning of Year	$ 785,057	$ 853,333	$ 400,039	$ 433,238
Service Cost	27,126	30,304	14,203	14,991
Interest Cost	48,316	43,794	24,480	21,619
Plan Participants' Contributions	111	106	2,366	1,828
Retiree Drug Subsidy	-	-	1,370	610
Net Actuarial (Gain)/Loss due to Plan Experience	10,518	(121,641)	24,782	(57,483)
Benefits Paid from Fund	(21,718)	(20,839)	(11,815)	(10,946)
Benefits Paid directly by University	-	-	(6,445)	(4,950)
Plan Amendments	-	-	-	1,132
Benefit Obligation at End of Year	$ 849,410	$ 785,057	$ 448,980	$ 400,039
Accumulated Benefit Obligation	$ 734,925	$ 678,169	N/A	N/A

Notes to Financial Statements

	Pension Benefits		Other Postretirement Benefits	
	06/30/2007	06/30/2006	06/30/2007	06/30/2006
Change in Plan Assets				
Fair Value of Plan Assets at Beginning of Year	$ 733,890	$ 654,234	$ 138,633	$ 117,060
University Contributions	18,362	30,876	30,069	30,779
Plan Participants' Contributions	111	106	2,366	1,828
Benefits Paid from Fund	(21,718)	(20,839)	(11,815)	(10,946)
Benefits Paid directly by University	-	-	(6,445)	(4,950)
Actual Return on Assets	142,159	69,513	23,584	4,862
Fair Value of Plan Assets at End of Year	$ 872,804	$ 733,890	$ 176,392	$ 138,633
Funded Status				
Projected Benefit Obligation / Accumulated Postretirement Benefit Obligation	$ (849,410)	$ (785,057)	$ (448,980)	$ (400,039)
Plan Assets at Fair Value	872,804	733,890	176,392	138,633
Unrecognized Net Actuarial Loss	-	39,164	-	89,369
Unrecognized Prior Service Costs	-	11,593	-	(11,346)
Funded Status at End of Year	$ 23,394	$ (410)	$ (272,588)	$ (183,383)

Net Amounts Recognized in the Statement of Financial Position at June 30, 2007

	Pension Benefits		Other Postretirement Benefits	
	06/30/2007	06/30/2006	06/30/2007	06/30/2006
Unrestricted Net Assets – Recognized under SFAS 158				
Net Actuarial (Gain)/Loss	$ (21,653)	N/A	$ 96,826	N/A
Net Prior Service Cost/(Credit)	N/A	N/A	(7,683)	N/A
Net Transition Obligation/(Asset)	-	N/A	-	N/A
Total	$ (21,653)	N/A	$ 89,143	N/A
Adjustment to Unrestricted Net Assets	$ (21,653)	N/A	$ 89,143	N/A
Information for Plans with ABO/APBO in Excess of Plan Assets				
Projected Benefit Obligation	N/A	N/A	$ 448,980	$ 400,039
Accumulated Benefit Obligation	N/A	N/A	448,980	400,039
Fair Value of Plan Assets	N/A	N/A	176,392	138,633
Information for Plans with PBO/APBO in Excess of Plan Assets				
Projected Benefit Obligation/ Accumulated Postretirement Benefit Obligation	$ 688,328	$ 5,653	$ 448,980	$ 400,039
Accumulated Benefit Obligation/ Accumulated Postretirement Benefit Obligation	585,412	4,735	448,980	400,039
Fair Value of Plan Assets	674,711	4,769	176,392	138,633

Notes to Financial Statements

	Pension Benefits		Other Postretirement Benefits	
	06/30/2007	06/30/2006	06/30/2007	06/30/2006
Information for Plans with PBO/APBO Less Than Plan Assets				
Projected Benefit Obligation/ Accumulated Postretirement Benefit Obligation	$ 161,083	$ 149,629	N/A	N/A
Accumulated Benefit Obligation/ Accumulated Postretirement Benefit Obligation	149,513	139,118	N/A	N/A
Fair Value of Plan Assets	198,093	166,755	N/A	N/A

The estimated amount that will be amortized from Unrestricted Net Assets into net periodic benefit cost in 2008 is as follows:

	Pension Benefits	Other Postretirement Benefits
Amortization of Net Transition Obligation/(Asset)	$0	$0
Amortization of Prior Service Cost/(Credit)	1,634	(3,664)
Amortization of Net Losses/(Gains)	(20)	3,413

Actuarial Assumptions

The expected long-term rate of return of plan assets is management's best estimate of the average investment return expected to be received on the assets invested in the plan over the benefit period. The expected long-term rate of return on plan assets has been established by considering historical and future expected returns of the asset classes invested in by the pension trust, and the allocation strategy currently in place among those classes.

	Pension Benefits		Other Postretirement Benefits	
	06/30/2007	06/30/2006	06/30/2007	06/30/2006
Weighted-Average Assumptions Used to Determine Benefit Obligations at Year End				
Discount Rate	6.25%	6.25%	6.25%	6.25%
Salary Increase	4.125%	4.125%	N/A	N/A
Weighted-Average Assumptions Used to Determine Net Periodic Benefit Cost				
Discount Rate	6.25%	5.17%	6.25%	5.17%
Expected Long-term Return on Plan Assets	8.375%	8.375%	8.375%	8.375%
Salary Increase	4.125%	4.125%	N/A	N/A
Assumed Health Care Cost Trend Rates				
Initial Trend Rate	N/A	N/A	9.50%	10.00%
Ultimate Trend Rate	N/A	N/A	5.00%	5.00%
Fiscal Year End that Ultimate Trend Rate is Reached	N/A	N/A	2015	2013

Notes to Financial Statements

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the other postretirement benefits. A one-percentage-point change in assumed healthcare trend rates would have the following effects on other postretirement benefits (in thousands):

	1-Percentage Point Increase		1-Percentage Point Decrease	
	2007	2006	2007	2006
Effect on total of service and interest cost	7,998	6,978	(6,239)	(5,442)
Effect on accumulated postretirement benefit obligation	67,576	60,575	(54,657)	(48,954)

Plan Assets

The principal investment objectives for the pension and other postretirement benefits plans are: to ensure the availability of funds to pay pension benefits as they become due under a broad range of future economic scenarios; to maximize long-term investment returns with an acceptable level of risk based on the pension obligations; and to invest the pension trust in a diversified manner across equity and debt securities. The equity securities are diversified, and composed predominantly of developed market liquid assets, across a range of investment styles. Domestic equities comprised 37%, international equities comprised 28%, absolute return equities comprised 4% and emerging markets equities comprised 3% of plan assets at June 30, 2007. The average quality of debt securities at June 30, 2007, was AAA with an effective duration of 3.36 years.

Allocation of Plan Assets

	Target	2007	2006
Equity Securities	72.00%	72.00%	71.00%
Debt Securities	28.00%	28.00%	29.00%
Total	100.00%	100.00%	100.00%

Cash Flows & Estimated Future Benefit Payments

	Pension Benefits 06/30/2007	Other Postretirement Benefits 06/30/2007
University Contributions for the Year Ending:		
June 30, 2006	$ 30,876	$ 29,532
June 30, 2007	18,362	29,386
June 30, 2008	14,589	30,054
Benefits Paid Directly by the University for the Year Ending:		
June 30, 2006	$ 0	$ 5,693
June 30, 2007	0	6,444
June 30, 2008	0	7,064
Plan Participants' Contributions for the Year Ending:		
June 30, 2006	$ 106	$ 1,828
June 30, 2007	111	2,366
June 30, 2008	123	2,450

Notes to Financial Statements

Benefits Payments in Total

	Pension Benefits	Other Postretirement Benefits Before Medicare Part D Subsidy	Impact of Medicare Part D Subsidy
Actual Benefit Payments for the Year Ending:			
June 30, 2006	$ 20,839	$ 15,896	$ 610
June 30, 2007	21,718	18,260	1,370
Expected Benefit Payments for the Year Ending:			
June 30, 2008	$ 26,450	$ 21,696	$ 2,615
June 30, 2009	28,285	23,217	2,800
June 30, 2010	30,430	25,076	3,035
June 30, 2011	33,148	26,877	3,254
June 30, 2012	36,706	28,410	3,460
June 30, 2013, to June 30, 2017	242,331	164,500	20,312

13. Medical Professional Liability Claims

The University is insured for medical professional liability claims through the combination of the Medical Care Availability and Reduction of Error Fund (Mcare, formerly, the Medical Professional Liability Catastrophe Loss Fund of the Commonwealth of Pennsylvania — CAT Fund), various commercial insurance companies and a risk retention program.

Mcare levies healthcare provider surcharges, as a percentage of the Pennsylvania Joint Underwriters Association rates for basic coverage, to pay claims and pay administrative expenses of Mcare participants. These surcharges are recognized as expenses in the period incurred. In March 2002, the Pennsylvania General Assembly approved reforming the Commonwealth's medical malpractice insurance system. No provision has been made for any future Mcare assessments in the accompanying financial statements as the University's portion of the unfunded Mcare liability cannot be estimated.

The University accrues for estimated retained risks arising from both asserted and unasserted medical professional liability claims. The estimate of the liability for unasserted claims arising from unreported incidents is based on analysis of historical claims data by an independent actuary, which is recorded utilizing a 5.0% discount rate at June 30, 2007.

From July 1998 through June 2001, the University was insured by a commercial insurer to provide claims made primary layer coverage on a claims made premium basis. Premiums were expensed in each respective fiscal year. Additionally, the University has recorded the actuarially determined exposure for unreported and unasserted medical professional claims that occurred during the period covered by the commercial insurance policy.

Effective July 1, 2001, the University funded RRG/Captive, for purposes of administering its risk retention program, covering its primary layer exposures. The assets and respective liabilities of RRG/Captive are included in the accompanying financial statements.

Assets have been board designated to provide funding for the University's retained risk associated with medical professional liability claims. The assets are included in the accompanying financial statements.

Notes to Financial Statements

14. Contingencies, Guarantees and Commitments

The University has guaranteed certain obligations as follows (in thousands):

	June 30, 2007		June 30, 2006	
	Amount Guaranteed	Recognized Liability	Amount Guaranteed	Recognized Liability
Mortgage Loans	$ 41,083	$ -	$ 36,903	$ -
Student Loans	50,468	7,719	62,086	7,023
Other	7,415	309	8,416	351
	$ 98,966	$ 8,028	$ 107,405	$ 7,374

To encourage home ownership and home improvement in the University's geographic area, certain University and affiliate employee mortgage loans are guaranteed. On February 23, 2006, the University instituted an additional mortgage guarantee program, which extends the guarantee program for recruitment and retention purposes beyond the immediate West Philadelphia neighborhood. Under this program, the University guarantees the employee's first mortgage amount that is in excess of 80% loan-to-value, up to 105% loan-to-value. The maximum amount that will be guaranteed on any single loan is limited to $250,000. For all loans guaranteed upon default by the borrower, the University may be required to pay any loss incurred following the lender's foreclosure process or the University may be required to purchase the loan. If the University purchases the loan, it will work with the borrower to make the loan current or it may foreclose and recover a portion of any loan from the sale of the mortgaged property. Of the amount guaranteed, $27,046,000 and $24,672,000 at June 30, 2007 and 2006, respectively, was estimated to be recoverable from subsequent sale of underlying assets the University would acquire if it performed under the guarantees. The University does not anticipate that any significant net payments will result from these guarantees. FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" does not require a guarantee liability to be recognized for employee mortgages.

The University offers various loan programs for students and families to pay tuition, fees and other costs. Certain loans issued by private lending institutions are guaranteed by the University. Upon default by the borrower, the University is required to pay all or a portion of the outstanding loan balance. Of the amount guaranteed, $18,550,000 and $15,720,000 at June 30, 2007 and 2006, respectively, was estimated to be recoverable from subsequent collection efforts on loans the University would acquire if it performed under the guarantees. The amount of the liability recognized for defaults in the portfolio of guaranteed loans exceeds the estimated fair value of the guarantee that is required to be recognized by FIN 45.

The Other category principally includes guarantees of indebtedness for certain businesses in the University's geographic area whose activities benefit employees, students and the community. Of the amount guaranteed, $4,183,000 at June 30, 2007, and $4,851,000 at June 30, 2006, was estimated to be recoverable from subsequent sale of underlying assets the University would acquire if it performed under the guarantees and from other partners in the businesses. The University does not anticipate that any significant net payments will result from these guarantees. The recognized liability reflects the fair value of guarantees issued after December 31, 2002.

Various lawsuits, claims and other contingent liabilities arise in the ordinary course of the University's education and healthcare activities. Based upon information currently available, management believes that any liability resulting there from will not materially affect the financial position or operations of the University.

The University is currently involved in various projects that have resulted in capital and property acquisition commitments from the University. As of June 30, 2007, approximately $400,293,000 has been committed by the University.

Trustees of the University of Pennsylvania

June 30, 2007

Statutory Officers

as of June 30, 2007

President
Dr. Amy Gutmann

Provost
Dr. Ronald Daniels

Executive Vice President
Mr. Craig R. Carnaroli

Executive Vice President of the University of Pennsylvania for the Health System and Dean, School of Medicine
Dr. Arthur H. Rubenstein

Senior Vice President and General Counsel of the University of Pennsylvania and the University of Pennsylvania Health System
Wendy S. White, Esq.

Vice President for Budget and Management Analysis
Ms. Bonnie Gibson

Vice President for Business Services
Ms. Marie Witt

Vice President and Chief of Staff
Mr. Gregory Rost

Vice President for Communications
Ms. Lori Doyle

Vice President for Development and Alumni Relations
Mr. John H. Zeller

Vice President for Finance and Treasurer
Mr. Scott R. Douglass

Vice President for Government and Community Affairs
Mr. Vanda McMurty

Vice President for Human Resources
Dr. John J. Heuer

Vice President for Information Systems and Computing
Ms. Robin H. Beck

Vice President for International Affairs
Ms. Joann Mitchell

Vice President for Public Safety
Ms. Maureen Rush

Vice President for Facilities and Real Estate Services
Ms. Anne Papageorge

Secretary of the University
Ms. Leslie Laird Kruhly

Comptroller
Mr. John Horn