
Michael Reese Health Trust

Financial Report
June 30, 2018

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Independent Auditor's Report

To the Board of Directors
Michael Reese Health Trust

We have audited the accompanying financial statements of Michael Reese Health Trust (Michael Reese), which comprise the statement of financial position as of June 30, 2018 and 2017 and the related statements of activities and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Michael Reese Health Trust as of June 30, 2018 and 2017 and changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 3, the financial statements include investments value at \$142,022,096 (98.5 percent of net assets) and \$134,239,392 (96.5 percent of net assets) at June 30, 2018 and June 30, 2017, respectively, whose fair value has been estimated at net asset value in the absence of observable inputs used to determine market values. Management's estimates are based on information provided by the fund managers of the general partners. Our opinion is not modified with respect to this matter.

A handwritten signature in black ink that reads "Plante & Moran, PLLC".

November 16, 2018

Michael Reese Health Trust

Statement of Financial Position

June 30, 2018 and 2017

	2018	2017
Assets		
Cash and cash equivalents	\$ 1,787,408	\$ 4,084,583
Investments	142,022,096	134,239,392
Receivable from investment redemption	-	934,944
Federal excise tax deposits	3,173	18,952
Prepaid expenses	28,489	21,316
Beneficial interest in trusts	4,639,014	4,567,787
Equipment - Net of accumulated depreciation of \$62,500 and \$58,171, respectively	13,710	18,039
Total assets	\$ 148,493,890	\$ 143,885,013
Liabilities and Net Assets		
Liabilities		
Grants payable	\$ 4,011,653	\$ 4,355,561
Deferred federal excise tax	126,324	232,889
Accrued expenses	217,654	197,021
Total liabilities	4,355,631	4,785,471
Net Assets		
Unrestricted:		
Undesignated	105,452,250	101,370,513
Board designated	11,194,079	11,086,223
Temporarily restricted net assets	7,792,477	7,014,580
Permanently restricted net assets	19,699,453	19,628,226
Total net assets	144,138,259	139,099,542
Total liabilities and net assets	\$ 148,493,890	\$ 143,885,013

Michael Reese Health Trust

Statement of Activities and Changes in Net Assets

Years Ended June 30, 2018 and 2017

	2018				2017			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue								
Trust fund and other income	\$ 378,403	\$ -	\$ -	\$ 378,403	\$ 348,272	\$ -	\$ -	\$ 348,272
Contributions	5,225	-	-	5,225	-	-	-	-
Interest and dividend - Net of investment fees of \$1,349,582 and \$491,887 in 2018 and 2017, respectively	170,319	(28,443)	-	141,876	387,740	3,464	-	391,204
Net realized and unrealized gains on investments	8,592,026	1,807,645	-	10,399,671	13,551,998	2,878,798	-	16,430,796
Net assets released from restrictions	1,001,305	(1,001,305)	-	-	300,399	(300,399)	-	-
Total revenue	10,147,278	777,897	-	10,925,175	14,588,409	2,581,863	-	17,170,272
Expenses								
Grants	4,442,452	-	-	4,442,452	3,908,292	-	-	3,908,292
Salaries and employee benefits	872,183	-	-	872,183	659,816	-	-	659,816
Purchased services, legal, and consulting	113,589	-	-	113,589	155,333	-	-	155,333
Other operating expenses	340,818	-	-	340,818	356,976	-	-	356,976
Federal excise tax expense	295,208	-	-	295,208	246,775	-	-	246,775
Deferred excise tax expense	(106,565)	-	-	(106,565)	(162,256)	-	-	(162,256)
Total expenses	5,957,685	-	-	5,957,685	5,164,936	-	-	5,164,936
Increase in Net Assets - Before change in value of beneficial interests in trusts	4,189,593	777,897	-	4,967,490	9,423,473	2,581,863	-	12,005,336
Change in Value - Beneficial Interests in Trusts	-	-	71,227	71,227	-	-	219,916	219,916
Increase in Net Assets	4,189,593	777,897	71,227	5,038,717	9,423,473	2,581,863	219,916	12,225,252
Net Assets - Beginning of year	112,456,736	7,014,580	19,628,226	139,099,542	103,033,263	4,432,717	19,408,310	126,874,290
Net Assets - End of year	\$ 116,646,329	\$ 7,792,477	\$ 19,699,453	\$ 144,138,259	\$ 112,456,736	\$ 7,014,580	\$ 19,628,226	\$ 139,099,542

See notes to financial statements.

Statement of Cash Flows

Years Ended June 30, 2018 and 2017

	2018	2017
Cash Flows from Operating Activities		
Increase in net assets	\$ 5,038,717	\$ 12,225,252
Adjustments to reconcile increase in net assets to net cash from operating activities:		
Depreciation	4,329	4,835
Realized and unrealized gains on investment	(10,399,671)	(16,430,796)
Change in value of beneficial interests in trusts	(71,227)	(219,916)
Changes in operating assets and liabilities which provided (used) cash:		
Federal excise tax deposits	15,779	-
Prepaid expense	(7,173)	(11,575)
Grants payable	(343,908)	(3,338,107)
Deferred tax	(106,565)	(163,407)
Accrued expense	20,633	(3,899)
Net cash used in operating activities	(5,849,086)	(7,937,613)
Cash Flows from Investing Activities		
Proceeds from sales of investments	17,421,591	106,508,161
Purchases of investments	(13,869,680)	(95,699,843)
Capital expenditures	-	(17,199)
Net cash provided by investing activities	3,551,911	10,791,119
Net (Decrease) Increase in Cash and Cash Equivalents	(2,297,175)	2,853,506
Cash and Cash Equivalents - Beginning of year	4,084,583	1,231,077
Cash and Cash Equivalents - End of year	\$ 1,787,408	\$ 4,084,583

Note 1 - Nature of Business

Michael Reese Health Trust (Michael Reese) is a private charitable foundation that is the successor organization to Michael Reese Hospital Foundation (formerly Michael Reese Hospital and Medical Center) (the "Center"), Michael Reese Second Century Foundation, and Michael Reese Health Plan Foundation. The Center operated a tertiary care hospital for both primary and specialty care and served as a major teaching and research facility. After the sale of its operating assets and liabilities in 1991, the Center's mission was changed to that of a grant-making organization, and its name was changed to Michael Reese Hospital Foundation, with the mission to support and encourage charitable, educational, and research activities related to health care in the Chicago metropolitan area. The Michael Reese Second Century Foundation and the Michael Reese Health Plan Foundation were entities affiliated with the Center and were included in the 1991 sale. These foundations were subsequently merged into Michael Reese Hospital Foundation, and Michael Reese Hospital Foundation's name was changed to Michael Reese Health Trust, which continues to fulfill its mission. The Jewish Federation of Metropolitan Chicago (the "Jewish Federation") is the sole member of Michael Reese (see Note 8).

Note 2 - Significant Accounting Policies

Basis of Accounting

Michael Reese maintains its accounting records and prepares its financial statements on an accrual basis, which is in accordance with accounting principles generally accepted in the United States of America, which requires Michael Reese to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Classification of Net Assets

Net assets of Michael Reese are classified as unrestricted, temporarily restricted, or permanently restricted depending on the presence and characteristics of donor-imposed restrictions limiting Michael Reese's ability to use or dispose of contributed assets or the economic benefits embodied in those assets.

Board-designated net assets consist of funds set aside by the board of directors for Fund for Innovation in Health, the Roe Health Improvement Funds, and the Herbert S. Wander Fund.

Donor-imposed restrictions that expire with the passage of time or can be removed by meeting certain requirements result in temporarily restricted net assets. Permanently restricted net assets result from donor-imposed restrictions that limit the use of net assets in perpetuity. Earnings, gains, and losses on restricted net assets are classified as unrestricted unless specifically restricted by the donor or by applicable state law.

Temporarily and permanently restricted net assets consist predominantly of funds for educational and research purposes.

Cash Equivalents

Michael Reese considers all investments with an original maturity of three months or less when purchased to be cash equivalents.

Michael Reese maintains its cash and cash equivalents in bank deposits accounts at MB Financial Bank and Charles Schwab Institutional, which at times may exceed federally insured limits. Michael Reese has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash.

Note 2 - Significant Accounting Policies (Continued)

Investments and Related Income, Gains, and Losses

Investments are presented in the financial statements at fair value.

Investment income, gains, and losses and any investment-related expenses are recorded as changes in unrestricted net assets in the statement of activities and changes in net assets unless their use is temporarily restricted by explicit donor stipulation or law. In the absence of donor stipulations or law to the contrary, losses on the investment of a donor-restricted endowment fund are recognized as reductions of temporarily restricted net assets to the extent that donor-imposed restrictions on net appreciation of the funds have not been met before the loss occurs. Any remaining loss reduces unrestricted net assets.

Earnings on permanently restricted endowment principal, including realized and unrealized gains or losses, are recorded as temporarily restricted investment income based on specific endowment restrictions.

Michael Reese's investment portfolio is subject to various risks, such as interest rate, market, and credit risks. Because of these risks, it is possible that changes in the value of the investments may occur and that such changes could materially affect Michael Reese's financial statements.

Equipment

Equipment is stated at its estimated market value at the date donated or at cost, if purchased. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which are currently five years.

Beneficial Interest in Trusts

Michael Reese was named an income beneficiary for various beneficial interests in perpetual trusts. Under the terms of the perpetual trusts, Michael Reese is to receive a portion of the trusts' annual net income based on the percentage of the trust allocated to Michael Reese. Payments from these entities range between 10 percent to 100 percent of the net income generated by these trusts.

In addition, Michael Reese is the income beneficiary of a perpetual trust for which the amount of the income distribution rests at the discretion of the advisory committee of this perpetual trust. Due to the uncertainty of the distribution amounts, if any, the financial statements do not reflect the fair value of this perpetual trust.

Income from all trusts is recorded at the time the payment is received. Income of \$378,403 and \$348,272 was received from these entities during the years ended June 30, 2018 and 2017, respectively.

Contributions

Contributions of cash and other assets, including unconditional promises to give in the future, are reported as revenue when received and measured at fair value. Donor promises to give in the future are recorded at the present value of estimated future cash flows.

Contributions without donor-imposed restrictions and contributions with donor-imposed time or purpose restrictions that are met in the same period as the gift are both reported as unrestricted support. Other restricted gifts are reported as restricted support and temporarily or permanently restricted net assets.

Note 2 - Significant Accounting Policies (Continued)

Federal Income Taxes

Michael Reese is exempt from income tax under provisions of Internal Revenue Code Section 501(c)(3). As a private foundation, Michael Reese is subject to an excise tax on net investment income, including realized gains, as defined in the Tax Reform Act of 1969. As of June 30, 2018 and 2017, Michael Reese had excise taxes payable of \$126,324 and \$232,889, respectively. Excise taxes paid by Michael Reese are paid from the respective unrestricted or temporarily restricted net assets. Michael Reese provides for deferred excise taxes, which represent taxes provided on the net unrealized appreciation of investments using a 2 percent tax rate.

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.

Upcoming Accounting Changes

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, in August 2016. ASU No. 2016-14 requires significant changes to the financial reporting model of organizations that follow FASB not-for-profit rules, including changing from three classes of net assets to two classes: net assets with donor restrictions and net assets without donor restrictions. The ASU will also require changes in the way certain information is aggregated and reported by Michael Reese, including required disclosures about the liquidity and availability of resources. The new standard is effective for Michael Reese's year ending June 30, 2019 and thereafter and must be applied on a retrospective basis. Management expects an impact to the classification of net assets and an enhancement of disclosure about liquidity, including qualitative and quantitative information.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for Michael Reese's year ending June 30, 2021 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The new lease standard is expected to have a significant effect on Michael Reese's financial statements as a result of the lease for office space currently classified as an operating lease. The effect of applying the new lease guidance is expected to increase assets and liabilities.

In June 2018, the FASB issued ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which provides enhanced guidance to assist entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal transactions) and (2) determining whether a contribution is conditional. The new guidance for contributions received will be effective for Michael Reese's year ending June 30, 2020 and will be applied on a modified prospective basis. Michael Reese has not yet determined the impact on the timing of recognition of foundation and individual grants and contributions. The new guidance also applies to not-for-profits making contributions, as well as those receiving contributions; therefore, Michael Reese is considering the impact on the timing of recognition of grant expenditures, which is effective for Michael Reese's year ending June 30, 2021.

Note 3 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the Michael Reese has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs, such as interest rates and yield curves, that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.

Net asset value inputs include interests in investment companies at year end where the fair value of the investment held is estimated based on net asset value per share (or its equivalent) of the investment company.

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

The following tables present information about Michael Reese's assets measured at fair value on a recurring basis at June 30, 2018 and 2017 and the valuation techniques used by Michael Reese to determine those fair values.

	<u>Assets Measured at Fair Value on a Recurring Basis at June 30, 2018</u>			
	<u>Quoted Prices in</u>			
	<u>Active Markets</u>	<u>Significant Other</u>	<u>Significant</u>	
	<u>for Identical</u>	<u>Observable</u>	<u>Unobservable</u>	
	<u>Assets</u>	<u>Inputs</u>	<u>Inputs</u>	<u>Balance at</u>
	<u>(Level 1)</u>	<u>(Level 2)</u>	<u>(Level 3)</u>	<u>June 30, 2018</u>
Beneficial interest in trusts	\$ -	\$ -	\$ 4,639,014	\$ 4,639,014
Investments measured at NAV:				
Multistrategy hedge funds:				
International fund				3,489,181
Absolute return fund				28,296
Real assets fund				3,661,344
Pooled endowment portfolio				114,735,968
Private equity funds				20,107,307
				<u>142,022,096</u>
Total investments measured at NAV				<u>142,022,096</u>
Total assets				<u>\$ 146,661,110</u>

June 30, 2018 and 2017

Note 3 - Fair Value Measurements (Continued)

	Assets Measured at Fair Value on a Recurring Basis at June 30, 2017			Balance at June 30, 2017
	Quoted Prices in			
	Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Other Significant Unobservable Inputs (Level 3)	
Beneficial interest in trust	\$ -	\$ -	\$ 4,567,787	\$ 4,567,787
Investments measured at NAV:				
Multistrategy hedge funds:				
International fund				10,025,367
Absolute return fund				948,335
Real assets fund				3,247,273
Hedged equity funds				1,798,834
Pooled endowment portfolio				98,902,056
Private equity funds				19,317,527
Total investments measured at NAV				<u>134,239,392</u>
Total assets				<u>\$ 138,807,179</u>

Level 3 Inputs

Investments in Level 3 are composed of beneficial interests in perpetual trusts. The beneficial interest in trusts is stated at the estimated fair value, which is based on the percentage of the beneficial interest in trust designated to Michael Reese applied to the total fair value of the beneficial interest in trust, which is based primarily on quoted market prices. The changes in the fair value of the underlying trust assets, as determined by the trustees that hold and manage these assets, are recognized in the statement of activities and changes in net assets in the periods in which they occur.

Changes in Level 3 assets measured at fair value on a recurring basis for the years ended June 30, 2018 and 2017 are as follows:

	Beneficial Interest in Trusts
Balance at July 1, 2017	\$ 4,567,787
Change in value of beneficial interest in trusts	<u>71,227</u>
Balance at June 30, 2018	<u>\$ 4,639,014</u>
Balance at July 1, 2016	\$ 4,347,871
Change in value of beneficial interest in trusts	<u>219,916</u>
Balance at June 30, 2017	<u>\$ 4,567,787</u>

Investments in Entities that Calculate Net Asset Value per Share

Michael Reese holds shares or interests in investment companies at year end whereby the fair value of the investment held is estimated based on net asset value per share (or its equivalent) of the investment company.

Note 3 - Fair Value Measurements (Continued)

At year end, the fair value, unfunded commitments, and redemption rules of those investments are as follows:

	Investments Held at June 30, 2018			
	Fair Value	Unfunded Commitments	Redemption Frequency, if Eligible	Redemption Notice Period
Multistrategy hedge (a)	\$ 7,178,821	\$ -	Quarterly to annually	45 to 120 days
Private equity (b)	20,107,307	5,627,279	N/A	N/A
Pooled endowment portfolio (c)	114,735,968	-	Monthly	1 to 30 days
Total	\$ 142,022,096	\$ 5,627,279		

	Investments Held at June 30, 2017			
	Fair Value	Unfunded Commitments	Redemption Frequency, if Eligible	Redemption Notice Period
Multistrategy hedge (a)	\$ 14,220,975	\$ -	Quarterly to annually	45 to 120 days
Private equity (b)	19,317,527	11,120,426	N/A	N/A
Pooled endowment portfolio (c)	98,902,056	-	Monthly	1 to 30 days
Hedged equity (d)	1,798,834	-	Monthly to annually	30 to 90 days
Total	\$ 134,239,392	\$ 11,120,426		

(a) This category includes multistrategy absolute return investments focused on analyzing the probability-adjusted returns of individual securities and assets and capturing the alpha in mispriced assets/securities across conventional and alternative financial strategies. Management initiates long and short position targeting solid, absolute risk-adjusted returns. The fair values of the investments in this category have been estimated using net asset value per share of the investments. As of June 30, 2018 and 2017, 100 percent of the investments in this category has passed the initial lockup period. However, some have terms that make full liquidity unavailable at Michael Reese's report date.

(b) This category includes primarily private equity funds that focus on U.S. and international buyout and venture capital, real estate, and/or distressed debt. These investments are not redeemable. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets in the fund. The term for these investments ranges from 10 to 12 years. As of June 30, 2018 and 2017, the fair values of the investments in this category have been estimated using the practical expedient provided by the investment manager.

(c) The primary objectives of this category of funds are to invest prudently in order to preserve the inflation-adjusted value of the portfolio and guard against material reductions in its value, and to maximize risk-adjusted returns over a long period of time. A suitable balance between these objectives requires the pooled endowment portfolio (PEP) to be highly diversified with respect to asset categories, geographical regions, strategies, and investment managers so as to achieve a reasonable balance between short-term risk and long-term return. PEP is structured to protect capital during sharp market downturns, to participate meaningfully during market rallies, and to outperform over typical market environments. The portfolio engages over 80 investment managers, each with expertise across a wide range of asset categories including: domestic and international equities, domestic and international bonds, and nontraditional assets, such as commodities, private equity, real estate, and natural resources.

Note 3 - Fair Value Measurements (Continued)

(d) This category includes investments in hedge funds that invest both long and short primarily in U.S. common stocks. Management of the hedge funds has the ability to shift investments from value to growth strategies, from small to large capitalization stakes, and from a net long position to a net short position. The investments dominate exposure in the U.S. market, but will also take advantage of investment opportunities in Europe, Asia, and emerging markets. The fair values of the investments in this category have been estimated using net asset value per share of the investments. As of June 30, 2017, 100 percent of the investments in this category passed the initial lockup period. As of June 30, 2018, all investments in this category were liquidated.

Note 4 - Grants Payable

Grants payable consists of multi-year unconditional grants that are generally payable over one to three years. Management estimates these grants will be paid as follows:

2019	\$	3,326,653
2020		<u>685,000</u>
Total	\$	<u><u>4,011,653</u></u>

Note 5 - Donor-restricted and Board-designated Endowments

Michael Reese's endowment consists of 28 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the board of directors to function as endowments. Net assets associated with endowment funds, including funds designated by the board of directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. Michael Reese does not consider its beneficial interest in the perpetual trusts to be part of its endowment since it has no control over the assets included in the perpetual trusts.

Interpretation of Relevant Law

The board of directors of Michael Reese has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Michael Reese classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Michael Reese in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, Michael Reese considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

Notes to Financial Statements

June 30, 2018 and 2017

Note 5 - Donor-restricted and Board-designated Endowments (Continued)

Endowment Net Asset Composition by Type of Fund as of June 30, 2018				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 7,792,477	\$ 15,060,439	\$ 22,852,916
Board-designated endowment funds	11,194,079	-	-	11,194,079
Total	\$ 11,194,079	\$ 7,792,477	\$ 15,060,439	\$ 34,046,995

Changes in Endowment Net Assets for the Fiscal Year Ended June 30, 2018				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets - Beginning of year	\$ 11,086,223	\$ 7,014,580	\$ 15,060,439	\$ 33,161,242
Interest and dividends	(5,205)	(28,443)	-	(33,648)
Realized and change in unrealized gain	330,793	1,807,645	-	2,138,438
Appropriation of endowment assets for expenditure	(317,732)	(1,001,305)	-	(1,319,037)
Board designation	100,000	-	-	100,000
Endowment net assets - End of year	\$ 11,194,079	\$ 7,792,477	\$ 15,060,439	\$ 34,046,995

Endowment Net Asset Composition by Type of Fund as of June 30, 2017				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 7,014,580	\$ 15,060,439	\$ 22,075,019
Board-designated endowment funds	11,086,223	-	-	11,086,223
Total	\$ 11,086,223	\$ 7,014,580	\$ 15,060,439	\$ 33,161,242

Changes in Endowment Net Assets for the Fiscal Year Ended June 30, 2017				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets - Beginning of year	\$ 10,609,875	\$ 4,432,717	\$ 15,060,439	\$ 30,103,031
Interest and dividends	913	3,464	-	4,377
Realized and change in unrealized gain	793,169	2,878,798	-	3,671,967
Appropriation of endowment assets	(317,734)	(300,399)	-	(618,133)
Endowment net assets - End of year	\$ 11,086,223	\$ 7,014,580	\$ 15,060,439	\$ 33,161,242

June 30, 2018 and 2017

Note 5 - Donor-restricted and Board-designated Endowments (Continued)

Return Objectives and Risk Parameters

The primary objective of Michael Reese is to increase the purchasing power of Michael Reese’s assets while reducing, to the greatest extent possible, the possibility of loss. Consistent with prudent standards for preservation of capital and maintenance of liquidity, the goal of Michael Reese is to earn the highest possible total rate of return consistent with Michael Reese’s tolerance for risk. A secondary objective is to have a sufficient degree of flexibility in order to meet unanticipated demands and changing environments. Endowment assets include those assets of donor-restricted funds that Michael Reese must hold in perpetuity, as well as board-designated funds. Under this policy, as approved by the board of directors, the endowment assets are categorized by asset class. Each asset class has a target range to ensure diversification. Rebalancing will occur when any asset class is outside its range for two consecutive quarters. Total performance will be measured and compared against that of the S&P 500.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, Michael Reese relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). Michael Reese targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

Each year, the board of directors approves the amount to be appropriated, taking into consideration the long-term expected return on its endowment.

Note 6 - Lease Commitments

Michael Reese leases its office space under a lease agreement that was extended to November 2020. The lease agreement requires monthly payments. Future minimum annual commitments under the operating lease are as follows:

Fiscal Years Ending	Amount
2019	\$ 104,657
2020	107,273
2021	45,815
Total	<u>\$ 257,745</u>

Rent expense for 2018 and 2017 was \$92,522 and \$100,365, respectively.

Note 7 - Functional Expenses

The costs of providing the program and support services are reported on a functional basis. Costs are allocated between the various programs and support services on an actual basis, where available, or based on reasonable methods. Although methods of allocation used are considered appropriate, other methods could be used that produce different amounts. Expenses related to providing these services are as follows:

	2018	2017
Program expenses	\$ 5,669,606	\$ 4,853,552
Administration	288,078	311,384
Total	<u>\$ 5,957,684</u>	<u>\$ 5,164,936</u>

June 30, 2018 and 2017

Note 8 - Related Party Transactions

The majority of the board of directors is appointed by the Jewish Federation. As of June 30, 2018 and 2017, grants payable to the Jewish Federation and its affiliates were \$2,250,000 and \$2,225,000, respectively. Grants awarded to the Jewish Federation and its affiliates were \$1,483,036 and \$780,612 for the years ended June 30, 2018 and 2017, respectively.

During fiscal year 2017, the board discussed and approved a plan to move the Michael Reese Health Trust investment pool to the Jewish Federation of Metropolitan Chicago's Pooled Endowment Portfolio (PEP). The primary investor in PEP is the Jewish Federation. Certain Jewish Federation affiliate beneficiary agencies, such as Michael Reese, are also allowed to invest in PEP. As of June 30, 2018 and 2017, Michael Reese had investments of approximately \$115 million and \$99 million in PEP, making up approximately 81 and 74 percent of Michael Reese's investments, respectively.

Note 9 - Subsequent Events

The financial statements and related disclosures include evaluation of events up through and including November 16, 2018, which is the date the financial statements were available to be issued.

Michael Reese submitted an advance ruling request to the Internal Revenue Service for reclassification as a public charity to be effective July 1, 2018. If approved, this request would terminate Michael Reese's private foundation status. As of the report date, a response has not yet been received.