



 University of  
**Kentucky**  
2016 Financial Statements

University of Kentucky  
A Component Unit of the Commonwealth of Kentucky  
Financial Statements  
Years Ended June 30, 2016 and 2015

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## MESSAGE FROM THE PRESIDENT



This institution, and the members of the UK family, have boldly confronted challenges, risen to meet new opportunities, and redefined what it means to be the university for Kentucky over the last 150 years.

The university was guided through substantial financial challenges by President James Patterson. Presidents Frank McVey and Herman Donovan helped navigate two world wars, meeting the calls to support our collective national effort. Though not soon enough, we opened our doors to all people, fulfilling the lofty intention of our establishing land grant legislation. Throughout history, our mission has been to teach, discover, heal, and serve.

We have faced difficult times - seemingly insurmountable odds that called into question our ability to carry out the noble purpose of this institution cast more than 150 years ago. Indeed, what the UK family was able to overcome in its earliest days illustrates the extent to which our people define this place and its purpose.

Today, faced with a new array of complex questions and issues, we find the university again climbing an increasingly steep mountain.

How have we responded? How have we continued to dream and to climb?

In the last five years, we initiated or approved some \$2.1 billion in capital investments to improve student success, instruction,

research and discovery, quality of life, and health care. Approximately 91 percent of that investment is the result of public-private partnerships, philanthropy, strategic use of university resources, or other collaborations such as unprecedented support from UK Athletics for the Academic Science Building.

We welcomed successive record-setting, first-year classes that have joined the UK family and moved total enrollment past 30,700 – the largest in our history. We recruited nearly 400 National Merit, National Achievement, and National Hispanic Scholars in the last five years, placing UK among the top 10 public universities in the nation. Our campus is home to more students from diverse backgrounds than ever before, further adding to the richness of our campus family.

And these students are succeeding at higher levels. UK's retention rates have increased more than six percentage points in the last decade to record levels, which are projected to continue climbing. Our first-to-second year retention rate was among the highest in UK's history, and, with more than 4,250 students, the returning cohort was the largest in UK's history. This trajectory translates to record degree attainment, including more than 6,600 over the last academic year.

Since 2011, we've invested more in UK-funded student financial aid and scholarships that did not have to be repaid by our students. Over the last five years, we've increased UK's investment in student financial aid and scholarships by \$60 million—now up to \$117 million – doubling the investment in the last decade.

Faculty and staff researchers added to a growing portfolio of transformative research, discovery, and creative scholarship. In fiscal year 2015-16, UK received \$316.5 million in external research grants and contracts – signifying that we are a major player among research institutions in the country. In October 2015, we broke ground on a \$265 million, multi-disciplinary research facility to advance discovery and address critical Kentucky needs.

UK HealthCare continued to meet the needs of patients and families who require complex, quality health care through our network of providers and state-of-the-art academic medical center. Annual patient discharges have grown by more than 98 percent since 2003, and UK HealthCare is now a \$1.5 billion enterprise that cares for patients throughout Kentucky and, increasingly, the region.

New partners joined in our progress as the university reached unprecedented levels of success in private philanthropy. Last year, UK received more than 95,000 gifts from more than 50,400 donors. As a result, our total work product exceeds \$208 million doubling UK's philanthropic outcomes in the last five years.

Our priorities and success have gained for us the confidence of external partners and expert analysts in our industry. At a time

when other major research universities are experiencing stagnant enrollment and finances, often accompanied by negative ratings outlooks, a recent upgrade from Standard & Poor's is a strong endorsement of our direction. In their report, S&P cited our increasing enrollment, revenue diversity aided by UK HealthCare, strong financial performance, and a low debt burden as strengths for our future.

In total, our work fueled Kentucky's economy by providing a 12-fold return on the Commonwealth's \$280 million investment in its flagship university. UK employees pay more than \$90 million annually in state/local taxes, and UK's research enterprise has a more than \$580 million impact on Kentucky's economy. Two-thirds of graduates are employed in Kentucky after graduation. UK's capital improvements create tens of thousands of direct and indirect construction, contracting, and supplier jobs.

Over the last five years, the university has made extraordinary progress and developed considerable momentum. The new 2015-2020 Strategic Plan is a pivot point in the transformation of the university in which we build upon the foundation created in the past four years with bold strategic thinking about the future.

Endorsed by the Board of Trustees in October 2015, the Strategic Plan embraces the institution's historic mission as a public flagship and land grant research university, and calls us to:

- Be the university of choice for aspiring undergraduate students within the Commonwealth and beyond, seeking a transformational education that promotes self-discovery, experiential learning, and life-long achievement.
- Strengthen the quality and distinctiveness of our graduate programs to transform our students into accomplished scholars and professionals who contribute to the Commonwealth, the nation and the world through their research and discovery, creative endeavors, teaching, and service.
- Enhance the diversity and inclusivity of our university community through recruitment, promotion, and retention of an increasingly diverse population of faculty, administrators, staff, and students, and by implementing initiatives that provide rich diversity-related experiences for all to help ensure their success in an interconnected world.
- Expand our scholarship, creative endeavors, and research across the full range of disciplines to focus on the most important challenges of the Commonwealth, our nation, and the world.

- Leverage leading-edge technology, scholarship, and research in innovative ways to advance the public good and to foster the development of citizen-scholars.

A university – by its design and the opportunities we have to teach, to share, to explore, to serve, to challenge, to question, and to comfort – is the place where we can, must, and will make progress on the complex questions of our day. Our Strategic Plan supports and informs this work.

But our work today – and our focus on the future – reminds us in compelling ways of our legacy, our history of confronting and overcoming challenge to meet the needs of those we serve.

In the wake of the First World War, amid a tumultuous period in our history, President Frank McVey believed that the university needed to be viewed, “as more than an economic asset. It served, in fact, as an essential component of the well-being of the state, and in that position it needs to be free to seek truth.”

In his words, he concluded that, “what will save this nation after the war are the universities.”

Each day we are, together, grappling with how we continue to fulfill this vision. We are working with a sense of common purpose at an uncommon and distinctive place to find those answers.

I look forward to sharing that future with you.



Eli Capilouto  
President

## Independent Auditor's Report

Board of Trustees  
University of Kentucky  
Lexington, Kentucky

### Report on the Financial Statements

We have audited the accompanying basic financial statements of the University of Kentucky (University), a component unit of the Commonwealth of Kentucky, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the University's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

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

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Kentucky Medical Services Foundation, Inc. (KMSF), a blended component unit of the University, which statements reflect total assets of \$196,673 and \$195,126 as of June 30, 2016 and 2015, respectively, and total revenues of \$318,003 and \$304,167, respectively, for the years then ended (dollars in thousands). Those statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for KMSF, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. The financial statements of KMSF, which are included in the University's reporting entity, were not audited in accordance with *Government Auditing Standards*.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that

are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

## **Opinion**

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the University as of June 30, 2016 and 2015, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and post-employment and long-term disability benefit plan information listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

## **Other Information**

Our audits were conducted for the purpose of forming an opinion on the basic financial statements that collectively comprise the University's basic financial statements. The governing board listing and the message from the president as listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated October 3, 2016, on our consideration of the University's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.

*BKD, LLP*

Louisville, Kentucky  
October 3, 2016

# Management's Discussion and Analysis

The following Management's Discussion and Analysis (MD&A) provides an overview of the financial position and activities of the University of Kentucky (the University or UK) and its affiliated corporations for the years ended June 30, 2016 and 2015. Management has prepared this discussion, and suggests that it be read in conjunction with the financial statements and the notes appearing in this report.

## About the University of Kentucky

**Mission.** The University of Kentucky is a public, land-grant university dedicated to improving people's lives through excellence in education, research and creative work, service and health care. As Kentucky's flagship institution, the University plays a critical leadership role by promoting diversity, inclusion, economic development and human well-being.

The University of Kentucky:

- Facilitates learning, informed by scholarship and research;
- Expands knowledge through research, scholarship and creative activity; and
- Serves a global community by disseminating, sharing and applying knowledge.

The University, as the flagship institution, plays a critical leadership role for the Commonwealth of Kentucky (the Commonwealth) by contributing to the economic development and quality of life within Kentucky borders and beyond. The University nurtures a diverse community characterized by fairness and equal opportunity.

**Vision.** As Kentucky's indispensable educational institution, we transform the lives of our students and advance the Commonwealth we serve and beyond through our teaching and learning, diversity and inclusion, discovery, research and creativity, promotion of health, and deep community engagement.

**Background.** Under provisions of the federal Morrill Land-Grant Colleges Act (1862), Kentucky State Agricultural and Mechanical College was established in 1865 as part of Kentucky University (now Transylvania University). The College separated from Kentucky University in 1878 and was established on a 52 acre site (the University's current location) donated by the city of Lexington. In 1908, the College was re-named the State University, Lexington, Kentucky. In 1916 it became the University of Kentucky.

According to the Kentucky Revised Statutes (KRS) 164.125(2):

In carrying out its statewide mission, the University of Kentucky shall conduct statewide research and provide statewide services, including, but not limited to, agricultural research and extension services, industrial and scientific research, industrial technology extension services to Kentucky employers and research related to the doctoral, professional and postdoctoral programs offered within the University. The University may establish and operate centers and utilize state appropriations and other resources to carry out the necessary research and service activities throughout the state. The University may enter into joint research and service activities with other universities in order to accomplish its statewide mission.

In 1997, the Kentucky General Assembly reformed the state's public system of colleges and universities. According to the ***Kentucky Postsecondary Education Improvement Act of 1997***: The University of Kentucky is mandated to become a major comprehensive research institution ranked nationally in the top twenty public universities by 2020.

At its December 2005 meeting, the UK Board of Trustees approved the ***Top 20 Business Plan***.

The University's ***Strategic Plan for 2009-2014*** was adopted by the UK Board of Trustees at its June 2009 meeting. The ***Strategic Plan*** was designed to measure the University's progress by establishing specific goals for teaching, research and service at the department, college and university level.



Today, the University continues to focus on the core academic mission of the institution and the original tenets of the Morrill Land-Grant Colleges Act (1862). UK remains steadfast in its covenant with the Commonwealth – to produce graduates prepared for a 21<sup>st</sup> century economy; to conduct research that extends the boundaries of scientific discovery; and to render service and patient care that uplifts our community and region.

The UK Board of Trustees adopted the **Strategic Plan for 2015-2020** at its October 2015 retreat. The plan builds on extraordinary progress from previous planning documents, a dramatic investment in the institution's physical spaces, and the insight garnered from considerable campus conversation and constituent input. The plan considers the current operating context for higher education and focuses on five strategic objectives that support our role as Kentucky's indispensable institution:

- **Undergraduate Student Success** – To be the University of choice for aspiring undergraduate students within the Commonwealth and beyond, seeking a transformational education that promotes self-discovery, experiential learning, and life-long achievement.
- **Graduate Education** – Strengthen the quality and distinctiveness of our graduate programs to transform our students into accomplished scholars and professionals who contribute to the Commonwealth, the nation, and the world through their research and discovery, creative endeavors, teaching, and service.
- **Diversity and Inclusivity** – Enhance the diversity and inclusivity of our University community through recruitment, promotion, and retention of an increasingly diverse population of faculty, administrators, staff, and students, and by implementing initiatives that provide rich diversity-related experiences for all, to help ensure their success in an interconnected world.
- **Research and Scholarly Work** – Expand our scholarship, creative endeavors, and research across the full range of disciplines to focus on the most important challenges of the Commonwealth, our nation, and the world.
- **Outreach and Community Engagement** – Leverage leading-edge technology, scholarship, and research in innovative ways to advance the public good and to foster the development of citizen-scholars.

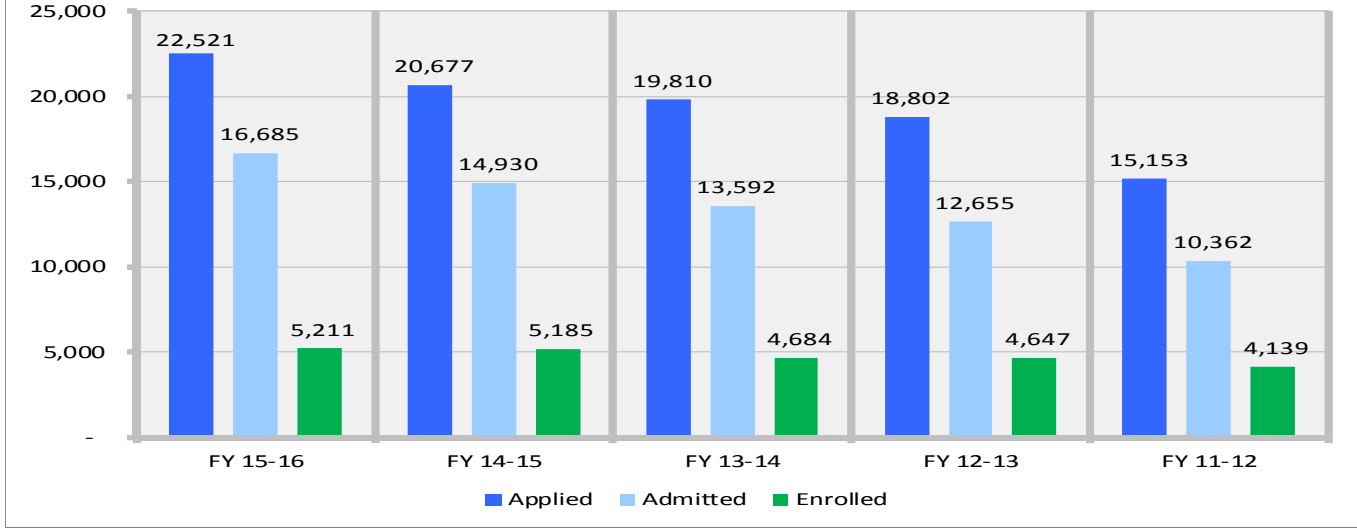
Under the leadership of Provost Timothy Tracy, progress on these objectives will be reported on an annual basis and presented to the UK Board of Trustees.

The University is identified as a “Research University (highest research activity)” by the Carnegie Commission on Higher Education. There are 115 such institutions in the United States (out of approximately 3,600 colleges and universities).

The University is accredited by the Commission on Colleges (CoC) of the Southern Association of Colleges and Schools (SACS). This has been re-affirmed at approximately 10-year intervals since 1915, with the next accreditation review scheduled for 2022. In addition, several degree programs and individual units are accredited by agencies appropriate to specific professions or fields.

**Students.** In Fall 2015, the University had 30,720 undergraduate, graduate, and professional students. They represent all 120 Kentucky counties, every state in the U.S. and over 100 countries. Enrollment has increased by 4,281 students (16%) since Fall 2006.

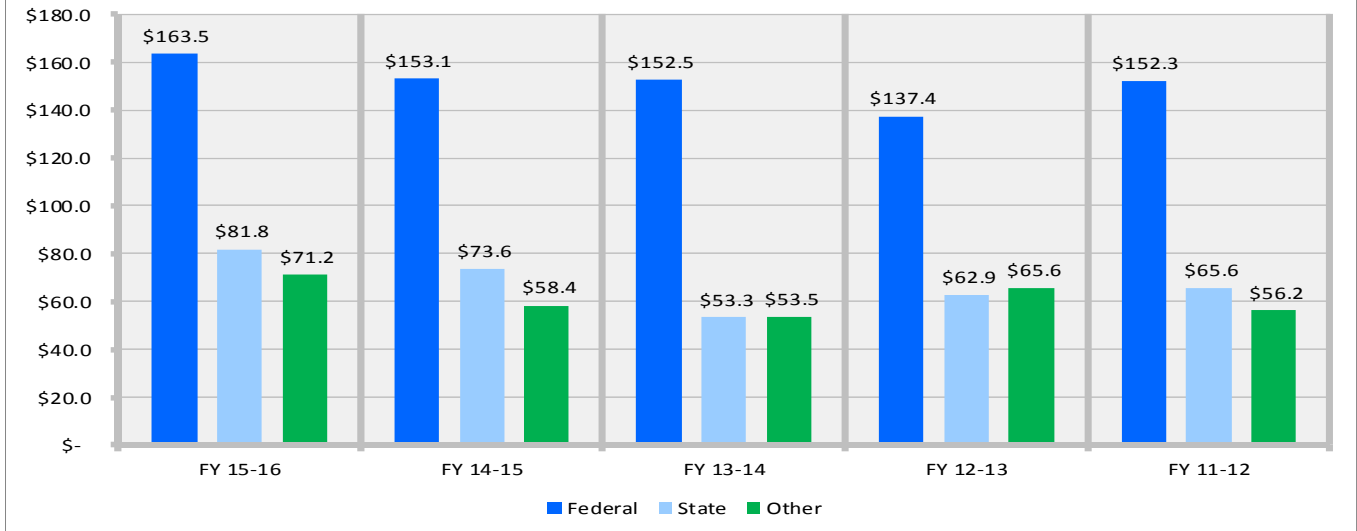
### First Year Students Applied, Admitted and Enrolled (Fall Term)



**Programs.** The University offers more than 200 majors and degree programs in 17 academic and professional colleges that are supported by a comprehensive research library system. UK is one of only eight public universities nationally with colleges of Agriculture, Engineering, Medicine and Pharmacy on a single contiguous campus.

**Research.** Total research expenditures, as reported to the National Science Foundation, totaled \$331.7 million for fiscal year 2014-15, compared to \$328.2 million in 2013-14. Research awards received during fiscal year 2015-16 total \$316.5 million, an 11% increase from the prior year amount of \$285.1 million.

### Grant and Contract Awards (in millions)



**Outreach.** As Kentucky's flagship, land-grant university, UK engages citizens and communities across the state in a myriad of ways, including extension offices in all 120 Kentucky counties; continuing education opportunities for teachers, lawyers and health care providers; clinics providing legal, pharmaceutical and health care assistance; and a multitude of research efforts aimed at Kentucky's most difficult problems in economic development, health care, infrastructure and education.

**Medical Centers.** UK HealthCare, a trademarked brand used by the University for its healthcare services, is uniquely equipped to provide advanced subspecialty care to the people of Kentucky. The academic medical center and health system provides patient care on par – in terms of both volume and complexity – with the nation’s top 25% of academic medical centers. In August 2016, UK HealthCare was named number one in Kentucky in the latest U.S. News Best Hospital ranking. To be recognized as a Best Hospital, UK HealthCare had to rank high nationally on a stringent data-driven ratings system that gauges performance. The analysis includes multiple clinical specialties, procedures and conditions. Scores are based on a variety of patient outcome and care-related factors such as mortality and patient safety, as well as reputation. This and other notable achievements are listed at <http://ukhealthcare.uky.edu/quality/awards/>.

UK HealthCare Hospital System (the System) operates two hospital units under one Joint Commission Accreditation and two licenses in addition to ambulatory services. The major service units include Albert B. Chandler Hospital, Good Samaritan Hospital and the Kentucky Clinic. The System has a combined total of 825 licensed beds with an average daily census of 709 patients. On a monthly basis, the system provides over 1,222 inpatient surgeries, 1,388 outpatient surgeries, 32,638 radiology procedures, 9,035 emergency department visits and 125,428 hospital based outpatient clinic visits.

Under a management contract entered into with the Kentucky Cabinet for Health and Family Services, the System also operates and manages Eastern State Hospital, a 300,000 square-foot facility located on the University’s Coldstream Research Campus. Eastern State Hospital provides a modern setting for both acute and long-term inpatient psychiatric treatment for adults living within Fayette County and the 50 surrounding counties.

UK HealthCare’s Markey Cancer Center remains the state’s only cancer center designated by the National Cancer Institute (NCI), which reflects UK’s position as a frontrunner in cancer treatment and research. UK HealthCare is one of an elite group of only 22 medical centers in the United States that have NCI designation, a federally funded Center on Aging, and a highly prized Clinical and Translational Science Award grant.

UK HealthCare’s dramatic growth within the last decade is in large part the result of a commitment to support the state’s overall system of care by working hand-in-hand with local community providers to bring specialty care closer to the patient. These relationships take on different dimensions in each locality (management agreements, affiliate networks, outreach, etc.) and support keeping less acute care in the local community and smoothing the process for more complex, serious cases to be treated in UK HealthCare’s Lexington facilities. The goal is better care at all points of the continuum.

**Libraries.** UK operates a nationally recognized research library system, with the capstone being the world-class William T. Young Library. UK’s book endowment is the largest among public universities. Its library network and technology provide extraordinary service to students in the colleges of Medicine, Law, Engineering, Fine Arts and other programs. Meanwhile, students, faculty and Kentucky residents can use UK Libraries’ advanced technology to access the most up-to-date information from online journals, government publications and private studies.

### **Financial Highlights**

The University’s overall financial position remains fiscally sound with assets of \$6.02 billion, deferred outflows of resources of \$12.2 million, liabilities of \$1.93 billion and deferred inflows of resources of \$366.7 million as of June 30, 2016. Net position, which represents the University’s residual interest in assets and deferred outflows of resources after liabilities and deferred inflows of resources are deducted, was \$3.73 billion (62% of total assets).

- Total assets increased \$534.6 million (10%), primarily due to increases in cash and cash equivalents, other long-term investments and capital assets, net.
- Deferred outflows of resources decreased \$1.6 million (12%) due to the amortization of the difference between the reacquisition price and the net carrying amount of refunded debt.
- Total liabilities increased \$138.1 million (eight percent), primarily due to increases in bonds and capital lease obligations and accounts payable and accrued liabilities.
- Deferred inflows of resources increased \$125.6 million (52%) due to increases in the service concession arrangements with Education Realty Trust (EdR) and Aramark Educational Services, LLC (Aramark).

- Total net position increased \$269.3 million (eight percent). Unrestricted net position increased \$106.0 million and net investment in capital assets increased \$104.5 million. Restricted net position increased \$58.8 million mainly due to capital projects including the new research building, student center and academic science building.
- Operating revenues were \$2.60 billion and operating expenses were \$2.89 billion, resulting in a loss from operations of \$284.3 million. Nonoperating and other revenues, net of nonoperating expenses, were \$553.5 million, including \$279.6 million in state appropriations.

### **Using the Financial Statements**

The University presents its financial reports in a “business type activity” format, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements and Management’s Discussion and Analysis for State and Local Governments*, and GASB Statement No. 35, *Basic Financial Statements and Management’s Discussion and Analysis for Public Colleges and Universities – an amendment of GASB Statement No. 34*. GASB requires that statements be presented on a comprehensive, entity-wide basis. In addition to this MD&A section, the financial report includes:

- Statement of Net Position
- Statement of Revenues, Expenses, and Changes in Net Position
- Statement of Cash Flows
- Notes to the Financial Statements

### **Reporting Entity**

The University is a component unit of the Commonwealth. The financial statements of the University include the operations of the University and the following entities:

- University of Kentucky Research Foundation, its for-profit subsidiary, Kentucky Technology, Inc. and formerly owned for-profit subsidiary, Coldstream Laboratories, Inc.
- The Fund for Advancement of Education and Research in the University of Kentucky Medical Center
- University of Kentucky Gluck Equine Research Foundation, Inc.
- University of Kentucky Humanities Foundation, Inc.
- University of Kentucky Mining Engineering Foundation, Inc.
- University of Kentucky Center on Aging Foundation, Inc.
- Central Kentucky Management Services, Inc.
- Kentucky Medical Services Foundation, Inc.

### **Statement of Net Position**

The Statement of Net Position is the University’s balance sheet. It reflects the total assets, liabilities, net position (equity), and deferred outflows and inflows of resources of the University as of June 30, 2016, with comparative information as of June 30, 2015. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as noncurrent. Net position (i.e. the difference between total assets and total liabilities and deferred inflows and outflows of resources) are an important indicator of the University’s current financial condition, while the change in net position is an indicator of whether the overall financial position has improved or worsened during the year. Generally, assets and liabilities and deferred inflows and outflows of resources are reported using current values. A major exception is capital assets, which are stated at historical cost less accumulated depreciation.

A summarized comparison of the University's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position as of June 30, 2016, 2015 and 2014 are as follows:

**Condensed Statements of Net Position (in thousands)**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
<b>ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>			
Current assets	\$ 1,058,800	\$ 983,253	\$ 694,839
Capital assets, net	2,709,638	2,336,640	1,979,404
Other noncurrent assets	2,247,372	2,161,316	1,816,476
Deferred outflows of resources	12,164	13,755	-
Total assets and deferred outflows of resources	<u>6,027,974</u>	<u>5,494,964</u>	<u>4,490,719</u>
<b>LIABILITIES AND DEFERRED INFLOWS OF RESOURCES</b>			
Current liabilities	508,534	472,487	358,671
Noncurrent liabilities	1,426,167	1,324,095	988,196
Deferred inflows of resources	366,746	241,124	-
Total liabilities and deferred inflows of resources	<u>2,301,447</u>	<u>2,037,706</u>	<u>1,346,867</u>
<b>NET POSITION</b>			
Net investment in capital assets	1,527,034	1,422,560	1,347,778
Restricted			
Nonexpendable	601,703	585,074	576,265
Expendable	494,154	451,990	425,775
Unrestricted	<u>1,103,636</u>	<u>997,634</u>	<u>794,034</u>
Total net position	<u>\$ 3,726,527</u>	<u>\$ 3,457,258</u>	<u>\$ 3,143,852</u>

**Assets.** As of June 30, 2016, total assets amounted to \$6.02 billion. The largest asset class was capital assets, net, that totaled \$2.71 billion or 45% of total assets. Endowment investments were \$1.22 billion, or 20% of total assets and cash and cash equivalents totaled \$1.09 billion, or 18% of total assets. During the year, total assets increased by a net \$534.6 million primarily due to an increase in capital assets, net of \$373.0 million, cash and cash equivalents of \$154.8 million and other long-term investments of \$24.4 million offset by a decrease in endowment investments of \$10.0 million and notes, loans and accounts receivable, net of \$6.7 million.

**Deferred Outflows of Resources.** The University's deferred outflows of resources totaled \$12.2 million, a decrease of \$1.6 million, which represents the unamortized difference between the reacquisition price and the net carrying amount of refunded debt.

**Liabilities.** As of June 30, 2016, total liabilities amounted to \$1.93 billion. Bonds and notes payable, capital leases and other long-term obligations issued for educational buildings, housing, the UK HealthCare Hospital System, athletics football stadium, and equipment totaled \$1.04 billion, or 54% of total liabilities. During the year, total liabilities increased by \$138.1 million primarily in the issuance of new debt comprised of \$155.8 million in general receipts bonds and \$7.2 million in capital leases offset by principal payments of \$49.8 million as well as an increase in other long-term liabilities of \$22.8 million with the largest increase in the retiree health benefits trust. Accounts payable and accrued liabilities also increased \$15.5 million offset by a decrease in unearned revenue of \$13.4 million.

**Deferred Inflows of Resources.** The University's deferred inflows of resources totaled \$366.7 million that represents service concession arrangements with EdR of \$222.3 million, Aramark of \$140.3 million and Barnes and Noble of \$4.1 million. During the year, deferred inflows of resources increased \$125.6 million primarily due to an increase in EdR of \$92.1 million and Aramark of \$34.4 million due to the completion of three new residence halls, a new dining facility and six dining facility renovations.



**Net Position.** The University's equity of \$3.73 billion as of June 30, 2016 is reported on the Statement of Net Position in three net position categories: net investment in capital assets, \$1.53 billion (41%); restricted nonexpendable, \$601.7 million (16%) and restricted expendable, \$494.2 million (13%); and unrestricted, \$1.10 billion (30%).

Restricted net position is subject to externally imposed restrictions governing its use. Although unrestricted net position is not subject to externally imposed stipulations, most of the unrestricted net position has been internally designated for support of academic and research programs and initiatives, capital projects and working capital requirements.

Total net position increased \$269.3 million during the year ended June 30, 2016. Net investment in capital assets increased \$104.5 million due to excess of additions of capital assets and principal payments of capital debt offset by depreciation expense. Restricted net position increased \$58.8 million principally due to state funding for the new research building construction project. Unrestricted net position increased \$106.0 million, primarily due to an increase in the net increase in operating revenues in excess of operating expenses for the UK HealthCare Hospital System.

**2015 Versus 2014.** During the year ended June 30, 2015:

- Total assets increased by a net \$990.5 million primarily due to an increase in cash and cash equivalents of \$256.6 million, endowment investments of \$16.3 million, other long-term investments of \$26.9 million, capital assets, net of \$357.2 million and notes, loans and accounts receivable, net of \$332.2 million.
- Deferred outflows of resources increased \$13.8 million due to the unamortized difference between the reacquisition price and the net carrying amount of refunded debt.
- Liabilities increased \$449.7 million primarily as the result of an increase in unearned revenue of \$212.8 million due to the new multimedia rights contract with JMI sports for Athletics, issuance of new debt of \$142.7 million offset by principal payments and an increase in accounts payable and accrued liabilities of \$83.7 million.
- Deferred inflows of resources increased \$241.1 million due to the service concession arrangements with EdR, Aramark and Barnes and Noble.
- Total net position increased \$313.4 million. Net investment in capital assets increased \$74.8 million due to excess of additions of capital assets and principal payments of capital debt offset by depreciation expense. Restricted net position increased \$35.0 million principally due to gifts for construction projects including the Gatton College of Business and Economics renovation/expansion and Athletics' new football training facility. Unrestricted net position increased \$203.6 million primarily due to an increase in operating revenues of \$313.0 million offset by an increase in operating expenses of \$167.7 million.

### **Statement of Revenues, Expenses and Changes in Net Position**

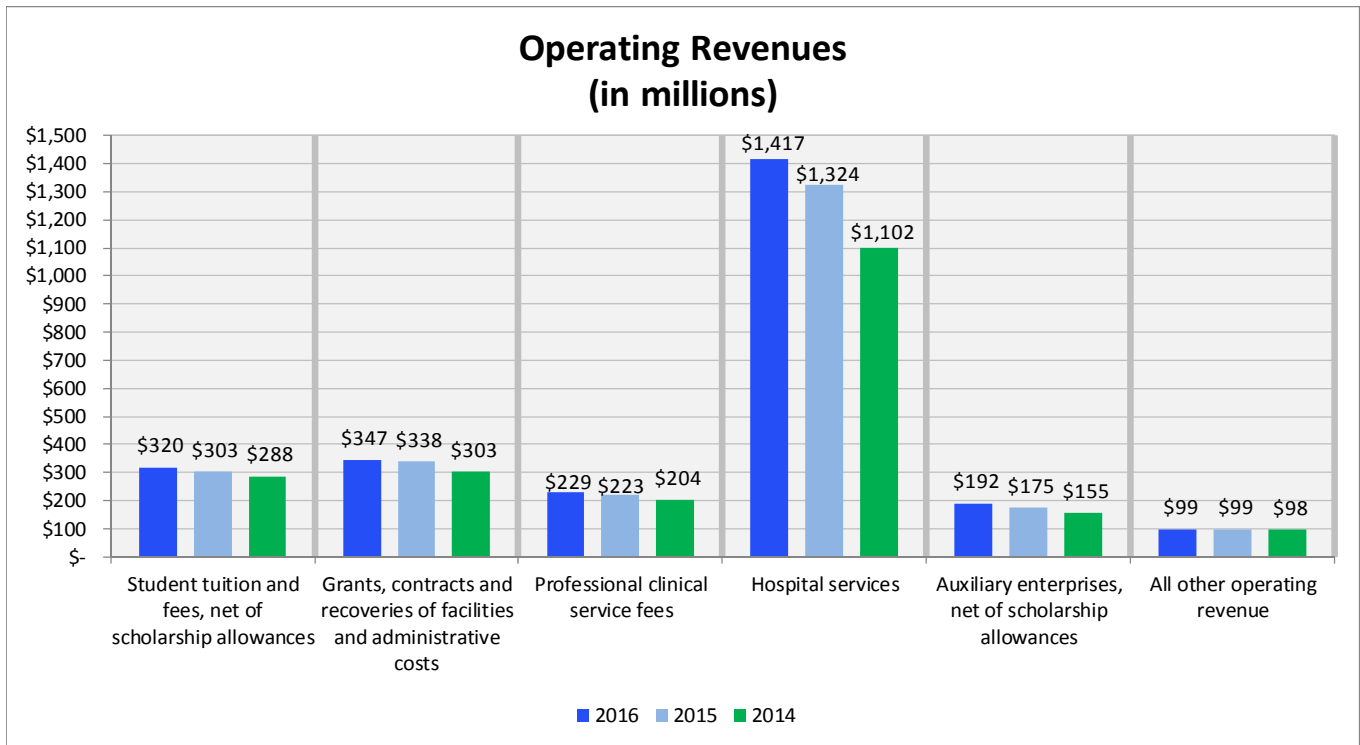
The Statement of Revenues, Expenses and Changes in Net Position is the University's income statement. It details how net position has changed during the year ended June 30, 2016, with comparative information for the year ended June 30, 2015. This statement is prepared on the accrual basis of accounting whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. Items that increase or decrease net position appear on the Statement of Revenues, Expenses and Changes in Net Position as revenues, expenses, gains or losses.

Financial activities are reported as either operating or nonoperating. GASB Statement No. 35 requires state appropriations, gifts and investment income to be classified as nonoperating revenues. Accordingly, the University reports a net operating loss prior to the addition of nonoperating revenues. The utilization of long-lived capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life. Tuition revenue is reduced by external scholarships and institutional aid and is reported net of the scholarship allowance.

A summarized comparison of the University's revenues, expenses and changes in net position for the years ended June 30, 2016, 2015 and 2014 are as follows:

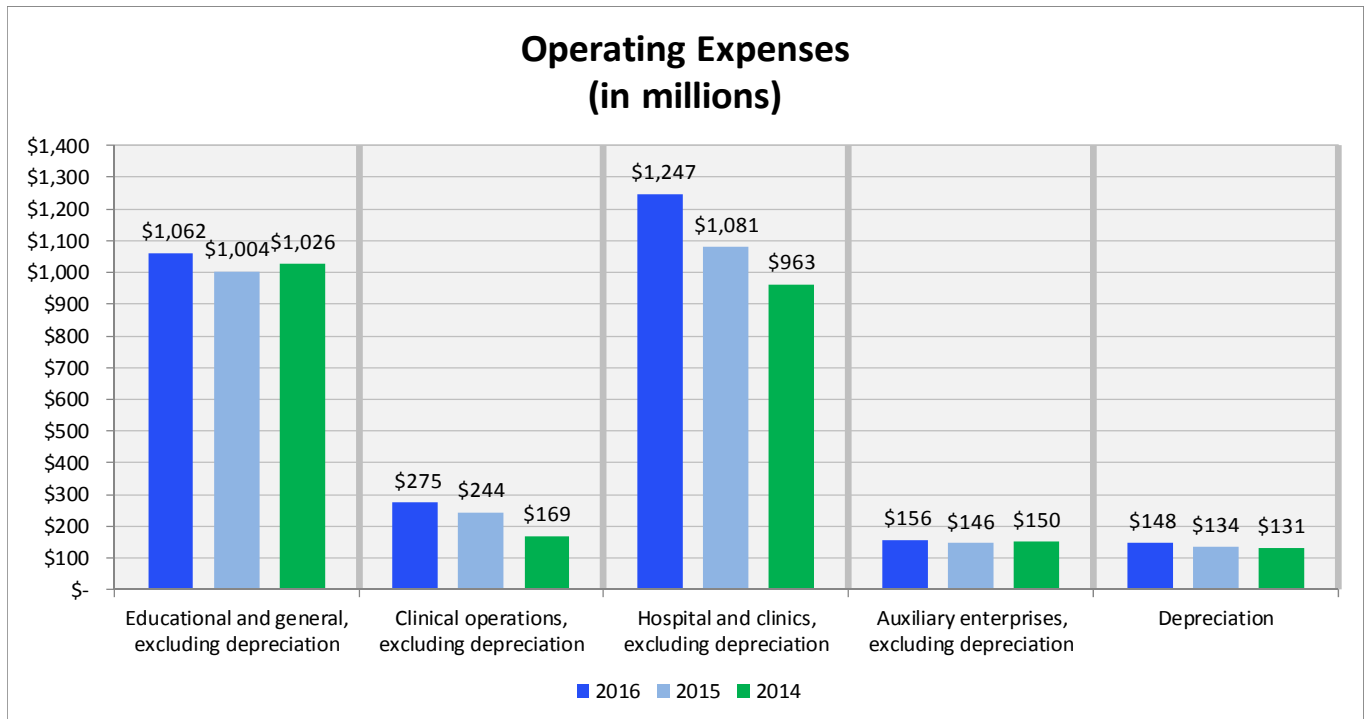
**Condensed Statements of Revenues, Expenses and Changes in Net Position (in thousands)**

	<u>2016</u>	<u>2015</u>	<u>2014</u>
<b>OPERATING REVENUES</b>			
Student tuition and fees, net of scholarship allowances	\$ 319,627	\$ 302,936	\$ 287,517
Grants and contracts	295,486	290,199	256,179
Recoveries of facilities and administrative costs	51,088	48,154	47,159
Sales and services	48,823	54,112	54,765
Federal and county appropriations	42,983	39,510	38,259
Professional clinical service fees	229,075	223,291	203,721
Hospital services	1,417,243	1,323,652	1,101,662
Auxiliary enterprises, net of scholarship allowances	191,532	175,232	155,393
Other operating revenues	7,931	5,059	4,516
Total operating revenues	<u>2,603,788</u>	<u>2,462,145</u>	<u>2,149,171</u>
<b>OPERATING EXPENSES</b>			
Educational and general, excluding depreciation	1,061,924	1,003,856	1,026,280
Clinical operations, excluding depreciation	274,984	243,688	168,934
Hospital and clinics, excluding depreciation	1,246,994	1,080,956	963,272
Auxiliary enterprises, excluding depreciation	155,458	145,739	150,451
Depreciation	148,109	134,374	131,262
Other operating expenses	570	640	1,384
Total operating expenses	<u>2,888,039</u>	<u>2,609,253</u>	<u>2,441,583</u>
<b>NET LOSS FROM OPERATIONS</b>	<u>(284,251)</u>	<u>(147,108)</u>	<u>(292,412)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>			
State appropriations	279,611	279,611	283,869
Gifts and non-exchange grants	127,796	105,506	96,771
Investment income (loss)	(2,665)	45,188	155,547
Interest on capital asset-related debt	(28,444)	(27,691)	(30,288)
Capital grants and gifts	165,896	45,341	54,068
Additions to permanent endowments	13,052	7,758	7,578
Other, net	(1,726)	4,801	6,213
Total nonoperating revenues (expenses)	<u>553,520</u>	<u>460,514</u>	<u>573,758</u>
Total increase in net position	269,269	313,406	281,346
Net position, beginning of year	<u>3,457,258</u>	<u>3,143,852</u>	<u>2,862,506</u>
Net position, end of year	<u>\$ 3,726,527</u>	<u>\$ 3,457,258</u>	<u>\$ 3,143,852</u>



Total operating revenues were \$2.60 billion for the year ended June 30, 2016, an increase of \$141.6 million (six percent). The primary components of operating revenues were student tuition and fees of \$319.6 million; grants, contracts and recoveries of facilities and administrative costs of \$346.6 million; professional clinical service fees of \$229.1 million; and hospital services of \$1.42 billion.

The major increase was in hospital service revenue of \$93.6 million attributable to an increase in rates, partially driven by patient acuity, and improved payer mix as a result of the Medicaid expansion program. Other significant increases in operating revenues related to net student tuition and fees of \$16.7 million due to tuition and fee rate increases as well as increased enrollment; grants, contracts and recoveries of facilities and administrative costs of \$8.2 million due to increases in federal and nongovernmental grants and contracts; professional clinical service fees of \$5.8 million; and auxiliary enterprises of \$16.3 million.



Operating expenses totaled \$2.89 billion, an increase of \$278.8 million (11%). Of this amount, \$1.06 billion, excluding depreciation, was expended for educational and general programs, including instruction, research and public service. Clinical operations expenses, excluding depreciation, were \$275.0 million; hospital and clinics expenses, excluding depreciation, amounted to \$1.25 billion; and auxiliary enterprise expenses, excluding depreciation, were \$155.5 million. Depreciation expense for the year amounted to \$148.1 million.

Education and general programs expenses, excluding depreciation, increased \$58.1 million due primarily to increases in instruction of \$15.1 million, research of \$12.5 million, student services of \$5.9 million, operations and maintenance of plant of \$12.3 million and student financial aid of \$3.9 million. Clinical operations expenses, excluding depreciation, increased \$31.3 million primarily due to increased staffing and market adjustments for clinical faculty and staff. Hospital and clinics expenses, excluding depreciation, increased \$166.0 million primarily due to additional staffing and supplies required for increased patient volume and market adjustments for clinical staff. Auxiliary enterprise expenses, excluding depreciation, increased \$9.7 million primarily in Athletics due to contractual increases in coaches' salaries and minor renovation and maintenance costs at Commonwealth Stadium. Depreciation expense increased \$13.7 million due to new buildings, renovations and equipment depreciation.

The net loss from operations for the year was \$284.3 million. Nonoperating and other revenues, net of expenses, totaled \$553.5 million and included state appropriations of \$279.6 million. Capital grants and gifts totaled \$165.9 million, an increase of \$120.6 million; gifts and non-exchange grants totaled \$127.8 million, an increase of \$22.3 million; additions to permanent endowments totaled \$13.1 million, an increase of \$5.3 million and investment loss totaled \$2.7 million, a decrease of \$47.9 million.

**2015 Versus 2014.** Total operating revenues were \$2.46 billion for the year ended June 30, 2015, including: student tuition and fees of \$302.9 million (12%); grants, contracts, and recoveries of facilities and administrative costs of \$338.4 million (14%); professional clinical service fees of \$223.3 million (nine percent); and hospital services of \$1.32 billion (54%). Operating revenues for fiscal year 2015 increased \$313.0 million (15%) over fiscal year 2014, primarily due to increases in hospital services revenue of \$222.0 million resulting from an increase in rates and overall case mix as well as an increase in retail and contract pharmacy sales; student tuition and fees of \$15.4 million due to tuition and fees rate increases as well as increased enrollment; grants and contracts of \$34.0 million due to increases in professional supplemental payments from state and federal grants and contracts; professional clinical service fees of \$19.6 million due to increased patient activity and improved reimbursements

associated with the decline in the uninsured self-pay population due to Medicaid expansion; and auxiliary enterprises net of scholarship allowances of \$19.8 million.

Operating expenses totaled \$2.61 billion in fiscal year 2015. Of this amount, \$1.00 billion (38%), excluding depreciation, was expended for educational and general programs, including instruction, research and public service. Hospital and clinics expenses, excluding depreciation, totaled \$1.08 billion (41%) of the total expenses, and clinical operations expenses, excluding depreciation, were \$243.7 million (nine percent). Depreciation amounted to \$134.4 million (five percent). Operating expenses for fiscal year 2015 increased \$167.7 million (seven percent) compared to fiscal year 2014 primarily due to an increase in hospital and clinics expenses, excluding depreciation, of \$117.7 million (12%); clinical operations expenses, excluding depreciation, of \$74.8 million (44%) and depreciation expense of \$3.1 million (two percent). Offsetting decreases were in education and general programs expenses, excluding depreciation, of \$22.4 million (two percent) and auxiliary enterprises expenses, excluding depreciation, of \$4.7 million (three percent).

The net loss from operations for the 2015 fiscal year totaled \$147.1 million. Nonoperating and other revenues, net of expenses, totaled \$460.5 million, resulting in an increase in net position of \$313.4 million for the year. Nonoperating revenue included state appropriations of \$279.6 million and \$283.9 million for June 30, 2015 and June 30, 2014, respectively.

### **Statement of Cash Flows**

The Statement of Cash Flows details how cash has increased or decreased during the fiscal year ended June 30, 2016, with comparative financial information for the fiscal year ended June 30, 2015. The sources and uses of cash are arranged in the following categories:

- Operating activities
- Noncapital financing activities
- Capital and related financing activities
- Investing activities

Cash flows associated with the University's expendable net position appear in the operating and noncapital financing categories. Capital financing activities include payments for capital assets, proceeds from long-term debt, and debt repayments. Purchases and sales of investments are reflected in investing activities.

The primary purpose of the Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the University during the year that will allow financial statement readers to assess the University's ability to generate future net cash flows and to meet obligations as they become due, and to assess the possible need for external financing.



A comparative summary of the University's statement of cash flows for the years ended June 30, 2016, 2015 and 2014 are as follows:

**Condensed Statements of Cash Flows (in thousands)**

	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>CASH PROVIDED (USED) BY:</b>			
Operating activities	\$ (90,450)	\$ 11,738	\$ (150,202)
Noncapital financing activities	434,004	416,732	409,650
Capital and related financing activities	(176,131)	(178,778)	81,163
Investing activities	(12,594)	6,900	(111,587)
Net increase (decrease) in cash and cash equivalents	154,829	256,592	229,024
<b>Cash and cash equivalents, beginning of year</b>	<b>937,483</b>	<b>680,891</b>	<b>451,867</b>
<b>Cash and cash equivalents, end of year</b>	<b>\$1,092,312</b>	<b>\$ 937,483</b>	<b>\$ 680,891</b>

The University's cash and cash equivalents increased \$154.8 million in fiscal year 2016. Total cash provided by noncapital financing activities was \$434.0 million, an increase of \$17.3 million compared to fiscal year 2015. Total cash used by operating activities was \$90.5 million, an increase of \$102.2 million; cash used by capital and related financing activities was \$176.1 million, reflecting both capital funding sources (debt proceeds) and uses (purchases of capital assets and debt service). Total cash used by investing activities was \$12.6 million, an increase of \$19.5 million.

Major sources of cash received from operating activities were hospital services of \$1.42 billion; student tuition and fees of \$320.1 million; grants, contracts, and recoveries of facilities and administrative costs of \$351.5 million; and professional clinical service fees of \$223.7 million. Major uses of cash for operating activities were payments to employees for salaries and benefits of \$1.76 billion and to vendors and contractors of \$924.0 million.

Noncapital financing activities include state appropriations from the Commonwealth of \$274.0 million, gifts of \$127.0 million and other noncapital financing receipts of \$33.0 million.

Capital and related financing activities include proceeds of capital debt of \$159.5 million and capital grants and gifts of \$164.2 million. Cash of \$416.8 million was expended for construction and acquisition of capital assets and \$88.5 million was expended for principal and interest payments on debt.

Investing activities include proceeds from sales and maturities of investments of \$649.7 million and interest and dividends on investments of \$26.0 million. Cash of \$688.3 million was used to purchase investments.

**2015 Versus 2014.** Cash balances were higher when comparing fiscal year 2015 to fiscal year 2014. The \$256.6 million net increase in cash was created from more cash provided by operating activities, noncapital financing activities and investing activities offset by more cash used for capital and related financing activities.

## Capital Asset and Debt Administration

### Capital Assets

Capital assets, net of accumulated depreciation, totaled \$2.71 billion at June 30, 2016, an increase of \$373.0 million. Capital assets as of June 30, 2016, 2015 and 2014, and significant changes in capital assets during the years ended June 30, 2015 and 2016 are as follows (in millions):

	Balance June 30, 2014	Net Additions (Deletions) FY 14-15	Balance June 30, 2015	Net Additions (Deletions) FY 15-16	Balance June 30, 2016
Land and land improvements	\$ 185	\$ 9	\$ 194	\$ 27	\$ 221
Buildings, fixed equipment and infrastructure	2,401	231	2,632	436	3,068
Equipment, vehicles and capitalized software	735	22	757	(40)	717
Library materials and art	162	2	164	3	167
Certificate of need license	12	-	12	-	12
Construction in progress	92	175	267	(8)	259
Accumulated depreciation	(1,608)	(81)	(1,689)	(45)	(1,734)
<b>Total</b>	<b>\$ 1,979</b>	<b>\$ 358</b>	<b>\$ 2,337</b>	<b>\$ 373</b>	<b>\$ 2,710</b>

At June 30, 2016, the University had capital construction projects in progress totaling approximately \$957.9 million in scope. Major projects include the construction of the new research building, student center and academic science building. The estimated cost to complete the projects in progress was approximately \$699.5 million.

Net additions also include EdR Phase II construction totaling \$97.0 million and Aramark capital construction and renovation projects of \$44.7 million.

### Debt

At June 30, 2016, capital debt amounted to \$1.04 billion, summarized by trust indenture and type, is as follows (in millions):

	2016	2015	2014
General Receipts bonds and notes	\$ 946	\$ 821	\$ 698
Consolidated Educational Buildings Revenue Bonds	-	-	33
Capital lease obligations	79	90	86
Notes payable	19	19	21
<b>Total</b>	<b>\$ 1,044</b>	<b>\$ 930</b>	<b>\$ 838</b>

Debt increased \$113.2 million during the year primarily due to the issuance of General Receipts Bonds 2016 Series A and B for \$155.8 million and additional capital leases of \$7.2 million, offset by a net decrease from principal payments of the University's debt obligations of \$49.8 million.

## **Economic and Other Factors That Will Affect the Future**

Senior leadership continues to believe that the University is well-positioned to maintain its strong financial condition and to continue providing excellent service to students, patients, the community, and the citizens of the Commonwealth. This position, along with ongoing efforts toward revenue diversification and cost containment, will enable the University to obtain the necessary resources to sustain improving excellence. The following are known facts and circumstances that will affect future financial results:

- The national and state economies are finally recovering from the most devastating recession of the post-war era. After depositing \$26.4 million of the Commonwealth's General Fund surplus for fiscal year 2015-16, the Commonwealth's Budget Reserve Trust Fund is estimated to total \$235.8 million, the largest balance since the fiscal year ended June 30, 2001. State economists predict Kentucky will experience modest growth in tax collections in 2016-18.
- Matt Bevin was elected Governor in November 2015 and has frequently expressed his commitment to addressing the state's pension programs, which in 2015 ranked second highest in the nation, on an adjusted net pension liability basis, with the Commonwealth's two largest plans funded just 55% (KTRS) and 19% (KERS non-hazardous). While the University does not participate in the state's pension programs, the amount of available state funds for public postsecondary education is expected to be negatively impacted by the programs' financial condition.
- The enacted 2016-18 state budget includes a 4.5% reduction in state appropriations for fiscal year 2016-17 and reallocates five percent of the remaining state funds for a performance funding model for fiscal year 2017-18. The funds will be distributed to the institutions based on achievement of performance goals and metrics enacted by the General Assembly as recommended by the Postsecondary Education Working Group.
- Student demand is expected to remain high in the coming years. Applications for the Fall 2016 incoming class have exceeded 24,300 for the first time in the University's history. Preliminary numbers indicate that the Fall 2016 entering freshmen class will reach over 5,150 students, meeting the University's strategic enrollment budget.
- The number of patients served by UK HealthCare has grown more than 95% since fiscal year 2003 with 37,333 patients in our hospitals and 1.4 million visits to our clinics last year alone. Part of this growth is related to the Affordable Care Act (ACA) which initiated significant changes to the United States healthcare system including material changes to the delivery of healthcare services and the reimbursement paid for such services by governments or other third-party payers. As a result of the ACA, Kentucky has experienced one of the largest increases in Medicaid enrollment in the country. The average increase in enrollment for the United States is 23% compared to Kentucky's 90%. (Source: Kaiser Family Foundation, UK CEBR Annual Report). While the long-term impact of the ACA and its status in Kentucky is unknown, UK HealthCare will develop and execute strategies in an effort to mitigate negative impacts and leverage opportunities.
- As of June 30, 2016, grants and contracts of approximately \$201.4 million, an increase of approximately \$12.2 million from the previous year, have been awarded to the University but not expended. The growth in available governmental awards will result in increased grant revenue in future periods.
- The University is undergoing a momentous physical transformation including the following academic, research, healthcare and athletic projects:
  - A \$65.0 million renovation and expansion of the Gatton College of Business and Economics, financed by the University which opened in August 2016.
  - A new \$112.0 million academic science building financed by the University with Athletics funding \$65.0 million of the project cost. The building opened in August 2016.
  - A \$45.0 million football training facility and practice field construction project, financed completely by Athletics which opened in August 2016.
  - A \$201.3 million renovation and expansion of the student center financed by the University that is expected to open in January 2018.
  - A new \$265.0 million research building financed by the University and state bonds (\$132.5 million each). The new facility is expected to open in June 2018.
  - A \$65.0 million renovation and expansion of the College of Law building financed by \$35.0 million of state bonds and up to \$30.0 million by the University. The renovated and expanded facility is expected to be completed in April 2019.
  - A \$412.6 million multiphase renovation and upgrade of UK HealthCare facilities, including the Kentucky's Children Hospital, will increase the licensed bed capacity to 945 beds. The

renovation and upgrade will be financed by UK HealthCare and is expected to be fully completed by November 2019.

- A major component of the University's physical transformation involves revitalization of on-campus housing and dining using comprehensive public/private partnerships (P3) with EdR and Aramark. The multiphase housing P3 with EdR is the first of its kind in the nation, entailing a substantial increase in the quantity and quality of student housing while allowing the University to reserve its debt capacity for other capital needs. From August 2013 to August 2016, 12 new residence halls have opened with 5,733 total beds. Construction is underway for two more halls with 1,117 beds that are slated to open in August 2017 bringing the total new beds to 6,850. Discussions are ongoing regarding future projects. In July 2014, the University entered into a P3 with Aramark for transformation of dining services for students, faculty, staff, and the community. The 15 year partnership provides for \$70.0 million in facilities investments by Aramark. Through June 30, 2016, over \$60.0 million has been used to build a new 1,000 seat residential dining facility and to develop dining spaces in our new residence halls, academic buildings, and to renovate existing dining venues. A 750 seat residential dining unit is slated to open in the new student center in January 2018.

Economic challenges will continue to have an impact on the future. However, senior leadership believes the University will be able to sustain its sound financial position and continue its progress toward enhancing student success and becoming a nationally recognized public research institution.

**UNIVERSITY OF KENTUCKY**  
**A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY**  
**STATEMENTS OF NET POSITION (in thousands)**  
**JUNE 30, 2016 AND 2015**

	2016	2015
<b>ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 693,743	\$ 621,961
Notes, loans and accounts receivable, net	297,620	292,776
Investments	16,977	21,702
Inventories and other assets	50,460	46,814
Total current assets	<u>1,058,800</u>	<u>983,253</u>
<b>Noncurrent Assets</b>		
Restricted cash and cash equivalents	398,569	315,522
Endowment investments	1,221,579	1,231,557
Other long-term investments	299,417	275,001
Notes, loans and accounts receivable, net	327,366	338,953
Other noncurrent assets	441	283
Capital assets, net	2,709,638	2,336,640
Total noncurrent assets	<u>4,957,010</u>	<u>4,497,956</u>
Total assets	<u>6,015,810</u>	<u>5,481,209</u>
<b>Deferred Outflows of Resources</b>		
Total assets and deferred outflows of resources	<u>6,027,974</u>	<u>5,494,964</u>
<b>LIABILITIES AND DEFERRED INFLOWS OF RESOURCES</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued liabilities	326,817	311,308
Unearned revenue	79,648	79,776
Long-term liabilities - current portion	102,069	81,403
Total current liabilities	<u>508,534</u>	<u>472,487</u>
<b>Noncurrent Liabilities</b>		
Unearned revenue	179,853	193,094
Long-term liabilities	1,246,314	1,131,001
Total noncurrent liabilities	<u>1,426,167</u>	<u>1,324,095</u>
Total liabilities	<u>1,934,701</u>	<u>1,796,582</u>
<b>Deferred Inflows of Resources</b>		
Total liabilities and deferred inflows of resources	<u>2,301,447</u>	<u>2,037,706</u>
<b>NET POSITION</b>		
<b>Net investment in capital assets</b>	<u>1,527,034</u>	<u>1,422,560</u>
<b>Restricted</b>		
Nonexpendable		
Scholarships and fellowships	150,458	140,739
Research	273,161	271,579
Instruction	82,455	80,062
Academic support	85,183	84,083
Other	10,446	8,611
Total restricted nonexpendable	<u>601,703</u>	<u>585,074</u>
Expendable		
Scholarships and fellowships	65,097	75,608
Research	77,082	92,833
Instruction	49,620	54,951
Academic support	59,790	59,860
Loans	11,455	10,908
Capital projects	186,168	128,734
Debt service	17	724
Auxiliary	14,631	15,523
Other	30,294	12,849
Total restricted expendable	<u>494,154</u>	<u>451,990</u>
Total restricted	<u>1,095,857</u>	<u>1,037,064</u>
<b>Unrestricted</b>		
Total net position	<u>\$ 3,726,527</u>	<u>\$ 3,457,258</u>

See notes to financial statements.



**UNIVERSITY OF KENTUCKY**  
**A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY**  
**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION (in thousands)**  
**FOR THE YEARS ENDED JUNE 30, 2016 AND 2015**

	2016	2015
<b>OPERATING REVENUES</b>		
Student tuition and fees	\$ 457,893	\$ 425,805
Less: Scholarship allowances	(138,266)	(122,869)
Net tuition and fees	319,627	302,936
Federal grants and contracts	169,291	168,125
State and local grants and contracts	91,216	92,269
Nongovernmental grants and contracts	34,979	29,805
Recoveries of facilities and administrative costs	51,088	48,154
Sales and services	48,823	54,112
Federal appropriations	19,266	17,535
County appropriations	23,717	21,975
Professional clinical service fees	229,075	223,291
Hospital services	1,417,243	1,323,652
Auxiliary enterprises:		
Housing and dining	41,041	41,960
Less: Scholarship allowances	(1,938)	(2,695)
Net housing and dining	39,103	39,265
Athletics	102,995	88,928
Other auxiliaries	49,434	47,039
Other operating revenues	7,931	5,059
Total operating revenues	2,603,788	2,462,145
<b>OPERATING EXPENSES</b>		
Educational and general:		
Instruction	301,463	286,377
Research	256,021	243,511
Public service	184,214	181,537
Libraries	22,198	21,084
Academic support	74,600	73,078
Student services	44,570	38,648
Institutional support	58,643	55,623
Operations and maintenance of plant	83,420	71,104
Student financial aid	36,795	32,894
Depreciation	65,188	65,548
Total educational and general	1,127,112	1,069,404
Clinical operations (including depreciation of \$8,390 in 2016 and \$2,743 in 2015)	283,374	246,431
Hospital and clinics (including depreciation of \$53,603 in 2016 and \$53,167 in 2015)	1,300,597	1,134,123
Auxiliary enterprises:		
Housing and dining (including depreciation of \$6,259 in 2016 and \$5,279 in 2015)	27,227	30,961
Athletics (including depreciation of \$13,071 in 2016 and \$6,031 in 2015)	121,859	101,696
Other auxiliaries (including depreciation of \$1,598 in 2016 and \$1,606 in 2015)	27,300	25,998
Other operating expenses	570	640
Total operating expenses	2,888,039	2,609,253
Net loss from operations	(284,251)	(147,108)
<b>NONOPERATING REVENUES (EXPENSES)</b>		
State appropriations	279,611	279,611
Gifts and non-exchange grants	127,796	105,506
Investment income (loss)	(2,665)	45,188
Interest on capital asset-related debt	(28,444)	(27,691)
Other nonoperating revenues and expenses, net	16,653	8,988
Net nonoperating revenues (expenses)	392,951	411,602
Net income (loss) before other revenues, expenses, gains or losses	108,700	264,494
Capital grants and gifts	165,896	45,341
Additions to permanent endowments	13,052	7,758
Other, net	(18,379)	(4,187)
Total other revenues (expenses)	160,569	48,912
<b>INCREASE IN NET POSITION</b>	269,269	313,406
<b>NET POSITION, beginning of year</b>	3,457,258	3,143,852
<b>NET POSITION, end of year</b>	\$ 3,726,527	\$ 3,457,258

See notes to financial statements.

**UNIVERSITY OF KENTUCKY**  
**A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY**  
**STATEMENTS OF CASH FLOWS (in thousands)**  
**FOR THE YEARS ENDED JUNE 30, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Student tuition and fees	\$ 320,092	\$ 301,454
Grants and contracts	299,217	284,664
Recoveries of facilities and administrative costs	52,313	48,457
Sales and services	51,168	53,465
Federal appropriations	18,630	18,749
County appropriations	22,869	22,640
Payments to vendors and contractors	(923,966)	(827,529)
Student financial aid	(36,794)	(32,896)
Salaries, wages and benefits	(1,755,876)	(1,598,279)
Professional clinic service fees	223,744	221,728
Hospital services	1,417,430	1,338,659
Auxiliary enterprise receipts	208,425	171,385
Loans issued to students	(5,915)	(18,231)
Collection of loans to students	7,529	18,425
Self insurance receipts	67,275	61,352
Self insurance payments	(64,860)	(56,750)
Other operating receipts (payments), net	8,269	4,445
Net cash provided (used) by operating activities	<u>(90,450)</u>	<u>11,738</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
State appropriations	274,019	279,611
Gifts and grants received for other than capital purposes:		
Gifts received for endowment purposes	13,052	7,782
Gifts received for other purposes	113,956	113,225
Agency and loan program receipts	232,673	227,347
Agency and loan program payments	(229,244)	(229,398)
Other noncapital financing receipts (payments), net	29,548	18,165
Net cash provided (used) by noncapital financing activities	<u>434,004</u>	<u>416,732</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Capital grants and gifts	164,154	30,974
Purchases of capital assets	(416,832)	(284,031)
Proceeds from capital debt	159,541	392,077
Payments to refunding bond agents	-	(248,642)
Proceeds from sales of capital assets	-	10,180
Principal paid on capital debt and leases	(49,753)	(49,872)
Interest paid on capital debt and leases	(38,782)	(34,849)
Other capital and related financing receipts (payments), net	5,541	5,385
Net cash provided (used) by capital and related financing activities	<u>(176,131)</u>	<u>(178,778)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sales and maturities of investments	649,728	312,958
Interest and dividends on investments	26,017	19,850
Purchase of investments	(688,339)	(342,511)
Net proceeds from sale of CLI stock, net of cash acquired	-	19,877
Repayment of debt and other related to sale of CLI stock	-	(3,274)
Net cash provided (used) by investing activities	<u>(12,594)</u>	<u>6,900</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<u>154,829</u>	<u>256,592</u>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<u>937,483</u>	<u>680,891</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<u>\$ 1,092,312</u>	<u>\$ 937,483</u>
<b>Reconciliation of net loss from operations</b>		
<b>to net cash provided (used) by operating activities:</b>		
Net loss from operations	\$ (284,251)	\$ (147,108)
Adjustments to reconcile net loss from operations		
<b>to net cash provided (used) by operating activities:</b>		
Depreciation expense	148,109	134,374
Change in assets and liabilities:		
Notes, loans and accounts receivable, net	16,775	(327,943)
Inventories and other assets	(3,229)	(5,800)
Accounts payable and accrued liabilities	36,070	22,358
Unearned revenue	(13,337)	230,882
Long-term liabilities	8,018	13,959
Deferred inflows of resources	1,395	91,016
<b>Net cash provided (used) by operating activities</b>	<u>\$ (90,450)</u>	<u>\$ 11,738</u>

See notes to financial statements.

**UNIVERSITY OF KENTUCKY**  
**A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY**  
**NOTES TO FINANCIAL STATEMENTS**  
**June 30, 2016 and 2015**

**1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Reporting Entity**

The University of Kentucky (the University) is a component unit of the Commonwealth of Kentucky (the Commonwealth) and is included in the basic financial statements of the Commonwealth. The financial statements of the University include the operations of the University and its affiliated non-profit corporations (entities for which the University is financially accountable as defined by Statement No. 14 and amended by Statements No. 39 and No. 61 of the Governmental Accounting Standards Board (GASB), and which meet the definition of an affiliated corporation under Kentucky Revised Statutes (KRS) section 164A.550) as follows: the University of Kentucky Research Foundation and its for-profit subsidiary, Kentucky Technology, Inc. (KTI); The Fund for Advancement of Education and Research in the University of Kentucky Medical Center (The Fund); University of Kentucky Gluck Equine Research Foundation, Inc.; University of Kentucky Humanities Foundation, Inc.; University of Kentucky Mining Engineering Foundation, Inc.; University of Kentucky Center on Aging Foundation, Inc.; and Central Kentucky Management Services, Inc. The affiliates are presented as blended component units since University management has operational responsibility for each affiliated corporation. The financial statements also include the operations of Kentucky Medical Services Foundation, Inc. (KMSF) a non-profit entity for which the University is financially accountable as defined by GASB, but which is not an affiliated corporation under KRS. KMSF is included within the University reporting entity as a blended component unit as KMSF provides its services entirely to the University. The financial statements also include the operations of organizational units of the University: the UK HealthCare Hospital System (the System), the Department of Intercollegiate Athletics (Athletics), the Kentucky Tobacco Research and Development Center (KTRDC), and WUKY Radio. The separate financial statements for the above entities can be found at: [www.uky.edu/evpfa/controller/finst](http://www.uky.edu/evpfa/controller/finst).

**Basis of Presentation**

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the GASB. GASB establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and financial reporting purposes into the following net position categories:

- Net investment in capital assets: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- Restricted:
  - Nonexpendable* – Net position subject to externally imposed stipulations that they be maintained permanently by the University. Such assets include the principal of the University's permanent endowment funds.
  - Expendable* – Net position whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time.
- Unrestricted: Net position whose use by the University is not subject to externally imposed stipulations. Unrestricted net position may be designated for specific purposes by action of management or the Board of Trustees (the Board) or may otherwise be limited by contractual agreements with outside parties.

The financial statement presentation is intended to provide a comprehensive, entity-wide perspective of the University's assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues, expenses, changes in net position and cash flows.

## **Summary of Significant Accounting Policies**

Accrual Basis. The financial statements have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation has been incurred. The University reports as a Business Type Activity (BTA) as defined by GASB Statement No. 35. BTAs are those activities that are financed in whole or part by fees charged to external parties for goods and services.

Cash and Investments. The University considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Noncurrent cash and cash equivalents include plant funds allocated for capital projects, debt service reserves and endowment fund cash pending transfer to the custodian for investment. Cash and cash equivalents held by bond trustees and the University's endowment fund managers are included in investments.

Investments in marketable debt and equity securities are carried at fair value, as determined by the major securities markets. See footnote 2 for more information on the fair value determination. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the Statement of Revenues, Expenses and Changes in Net Position.

Notes, Loans and Accounts Receivable. This classification consists of tuition and fee charges to students; charges for auxiliary enterprise services provided to students, faculty and staff; and loans to students. Also included are patient accounts receivable, amounts due from sponsors for reimbursement of expenses made pursuant to contracts and grants, amounts due under multimedia rights contract and service concession arrangements, and pledges that are verifiable, measurable and expected to be collected. Accounts receivable are recorded net of estimated uncollectible amounts based upon a review of outstanding receivables, historical collection information, and existing economic conditions.

Inventories. Inventories are stated principally at the lower of average cost or market value.

Pooled Endowment Funds. All endowments are managed in a consolidated investment pool, which consists of more than 2,100 named funds. All contributing endowments participate in the income and appreciation of the pool on a per unit basis commensurate with their contribution to the pool. New endowments purchase units in the pool at the current unit value, which is calculated each month based on the fair value of the pool investments divided by the number of pool units outstanding. The market value method of accounting for pooled endowment funds is employed to ensure proper distribution of market price changes, realized gains (losses) on sales, accrued income earned, and distribution of investment earnings for expenditure by participating funds.

In accordance with the Kentucky Uniform Prudent Management of Institutional Funds Act (UPMIFA), as adopted by the Commonwealth in July 2010, the University employs a total return method for establishing investment objectives and spending policies designed to achieve financial equilibrium for endowment funds over the long-term. The University makes expenditure decisions in accordance with UPMIFA and donor gift agreements. UPMIFA prescribes guidelines for expenditure of a donor-restricted endowment fund (in the absence of overriding, explicit donor stipulations) and focuses on the entirety of a donor-restricted endowment fund, that is, both the original gift amount(s) and net appreciation. In accordance with the standard of prudence prescribed by UPMIFA and consistent with industry standards, the University has adopted a spending policy with the long-term objective to maintain the purchasing power of each endowment and provide a predictable and sustainable level of income to support current operations.

The adopted spending policy is a "hybrid" policy, which includes both the market value of the endowment and the current level of inflation in determining spending each year. Annual spending is calculated by taking a weighted average comprising 60% of the prior year's spending, adjusted for inflation, and 40% of the amount that results when the target annual spending rate of four percent is applied to the average market value of the endowment over the preceding 36 months. The spending amount determined by the formula is constrained so that the calculated rate is at least three percent, and not more than six percent, of the current endowment market value.

The University also utilizes an endowment management fee to support internal management and fundraising costs related to the endowment. For the years ended June 30, 2016 and 2015, the University's annual endowment management fee was 0.50% and 0.25%, respectively.

To protect endowment funds from permanent impairment of value, spending and management fee withdrawals are suspended on endowments with a market value less than the contributed value by more than 20%. Additionally, endowments with a market value less than the contributed value by more than 10% undergo a formal review to determine the appropriate level of spending in accordance with various factors set forth in UPMIFA. All donor restrictions and stipulations prevail in decisions regarding preservation and spending of endowment funds.

The components of the University's spending policy distribution and management fee for the years ended June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Gross spending policy distribution	\$ 40,791	\$ 38,340
Reinvested spending policy distribution	(18,661)	(17,903)
Net spending policy distribution	\$ 22,130	\$ 20,437
Management fee	\$ 5,375	\$ 2,718

Capital Assets. Capital assets are stated at cost at date of acquisition or, in the case of gifts, at fair market value at date of gift.

The University capitalizes interest costs as a component of construction in progress based on the interest cost of borrowing specifically for a currently active project, net of interest earned on investments acquired with the proceeds of the borrowing. The University also capitalizes interest costs as a component of construction in progress on projects funded by unrestricted funds based on the interest costs of borrowings no longer associated with a specific project. The calculation is based on a project's average expenditures times the weighted average interest rate on borrowings.

Effective July 1, 2015, equipment with a unit cost of \$5,000 or more (\$2,000 or more for KMSF, \$2,500 or more for KTI) and having an estimated useful life of greater than one year is capitalized. Institutional software costing more than \$400,000 is capitalized. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred.

Depreciation of capital assets is computed on a straight-line basis over the estimated useful lives of the respective assets, generally 75 years for new student housing buildings, 40 years for other buildings, 10 – 25 years for land improvements, building improvements and infrastructure, 10 years for library books and capitalized software (capitalized software is depreciated over 3 years by KMSF), and 5 – 20 years for equipment and vehicles.

The University capitalizes, but does not depreciate, works of art, historical treasures and certain library materials that are held for exhibition, education, research and public service.

Deferred Outflows of Resources. A deferred outflow of resources is a loss in net position by the University that is applicable to a future reporting period. Deferred outflows of resources are reported in the Statement of Net Position, but are not recognized in the financial statements as expense until in the related period. Deferred outflows of resources of \$12.2 million and \$13.8 million as of June 30, 2016 and 2015, respectively, consisted of the unamortized difference between the reacquisition price and net carrying amount of refunded debt.

Unearned Revenue. Unearned revenue consists primarily of amounts received from grant and contract sponsors that have not yet been earned under the terms of the agreement. Unearned revenue also includes amounts received from multimedia rights pursuant to contract agreement and amounts received in advance of an event, such as athletic ticket sales relating to future fiscal years and unearned summer school revenue. Unearned revenue is recognized in the period to which the grant, event or semester relates.



Compensated Absences. The amount of vacation leave earned but not taken by employees at June 30, 2016 is recorded as a liability by the University. Temporary disability leave payable upon termination under the University's payout policy is also recorded as a liability. Compensated absence liabilities are computed using the pay rates in effect at the Statement of Net Position date plus an additional amount for compensation-related payments such as Social Security and Medicare taxes computed using rates in effect at that date.

Deferred Inflows of Resources. A deferred inflow of resources is a gain in net position by the University that is applicable to a future reporting period. Deferred inflows of resources are reported in the Statement of Net Position but are not recognized in the financial statements as revenue until in the related period.

Scholarship Allowances. Student tuition and fees are presented net of scholarship allowances applied to student accounts. Stipends and other payments made directly to students are presented as student financial aid expenses. Scholarship allowances are the difference between the stated charge for goods and services provided by the University and the amount that is paid by students and/or third parties making payments on the students' behalves. Certain governmental grants, such as Pell grants and other federal and state programs similar to Pell, are recorded as nonoperating revenues; other governmental and nongovernmental grants are recorded as operating revenues in the University's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the University has recorded a scholarship allowance.

Hospital and Clinical Services Revenues. Hospital and clinical services revenues are reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered, including contractual allowances and estimated retroactive adjustments under reimbursement programs with third-party payers, less a provision for doubtful accounts. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Inpatient acute care services and substantially all outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient skilled nursing services are paid at prospectively determined per diem rates that are based on the patients' acuity. Certain inpatient nonacute services and defined medical education costs are paid based on a cost reimbursement methodology. The System is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare fiscal intermediary.

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement methodology for certain services and at prospectively determined rates for all other services. The System is reimbursed for cost reimbursable services at tentative rates with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicaid fiscal intermediary.

Revenue from the Medicare and Medicaid programs accounted for approximately 24% and 31%, respectively, of the System's net patient services revenues before the provision for doubtful accounts for the year ended June 30, 2016 and approximately 28% and 27%, respectively for the year ended June 30, 2015. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

The System also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the System under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

The System provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Since the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Electronic Health Records Incentive Program. The Electronic Health Records Incentive Program, enacted as part of the American Recovery and Reinvestment Act of 2009, provides for incentive payments under both the Medicare and Medicaid programs to eligible physicians, dentists and hospitals that demonstrate meaningful use of certified electronic health records technology. Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, as determined by the state, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs is contingent on the System, The Fund and KMSF continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the fiscal intermediary. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The System recognizes revenue when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

In fiscal year 2016, the System was in the fifth year under the Medicare programs and recorded \$550,000, which is included in hospital services revenue within operating revenues in the Statement of Revenues, Expenses, and Changes in Net Position. In fiscal year 2015, the System was in the fourth year of the programs and recorded \$1.1 million.

In addition, during the years ended June 30, 2016 and 2015, KMSF applied for and received \$587,000 and \$366,000, respectively, in Medicaid Health Information Technology (HIT) funds and \$923,000 and \$1.3 million, respectively, in Medicare HIT funds, which is included in professional clinical service fees in the Statement of Revenues, Expenses and Changes in Net Position.

The Fund completed the second-year requirements under the Medicaid program and recorded \$128,000 and \$298,000 for the years ended June 30, 2016 and 2015, respectively, in state and local grants and contracts within operating revenues in the Statement of Revenues, Expenses and Changes in Net Position.

Income Taxes. The University is an agency and instrumentality of the Commonwealth, pursuant to Kentucky Revised Statutes sections 164.100 through 164.280. Accordingly, the University is excluded from federal income taxes as an organization described in section 115 of the Internal Revenue Code of 1986, as amended. Each of the University's affiliated non-profit organizations has received a determination from the Internal Revenue Service granting exemption from federal income taxation pursuant to the provisions of Internal Revenue Code section 501(c)(3). KMSF is a not-for-profit corporation as described in section 501(c)(3) of the Internal Revenue Code.

Restricted Asset Spending Policy. The University's policy is that restrictions on assets cannot be fulfilled by the expenditure of unrestricted funds for similar purposes. The determination on whether restricted or unrestricted funds are expended for a particular purpose is made on a case-by-case basis. Restricted funds remain restricted until spent for the intended purpose.

Operating Activities. The University defines operating activities, as reported on the Statement of Revenues, Expenses and Changes in Net Position, as those that generally result from exchange transactions, such as payments received for providing goods and services and payments made for goods and services received. Nearly all of the University's expenses are from exchange transactions. Certain significant revenues relied upon for operations, such as state appropriations, gifts and investment income, are recorded as nonoperating revenues in accordance with GASB Statement No. 35.

The University has classified operating expenses based upon their functional classifications. Operating expenses by natural classification are presented in Note 23. During fiscal years 2016 and 2015, departmental research in nonsponsored accounts of approximately \$67.9 million and \$61.6 million, respectively, was recorded as research expense in the Statements of Revenues, Expenses and Changes in Net Position.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to use estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The accompanying financial statements include estimates for items such as bad debt and

contractual allowances, estimated third-party payer settlements, self-insurance reserves, accrued expenses and other liability accounts.

Recent Accounting Pronouncements. As of June 30, 2016, the GASB has issued the following applicable statements to the University but are not yet implemented.

- GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement No. 68, and Amendments to Certain Provisions of GASB Statements No. 67 and 68*, issued June 2015. The provisions of this Statement are effective for fiscal years beginning after June 15, 2016 (fiscal year 2017). This statement establishes requirements for defined contribution pension plans not administered through trusts that meet certain criteria. The University has certain employees who were age 40 or older prior to the establishment of each group retirement plan that qualify for minimum annual retirement benefits (see Note 16). The University is currently evaluating the effect statement No. 73 will have on its financial statements.
- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, issued June 2015. The provisions of this Statement are effective for fiscal years beginning after June 15, 2017 (fiscal year 2018). This statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expenses. This statement addresses employers whose employees are provided defined contribution other post-employment benefits. The University is working with an actuary to determine the impact of the pronouncement. Although specific amounts are not yet known, this is expected to result in a significant liability for the unfunded portion being recorded on the University's financial statements.
- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, issued March 2016. The provisions of this Statement are effective for fiscal years beginning after December 15, 2016 (fiscal year 2018). This statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement recognizes assets, liabilities, and deferred inflows of resources at the inception of the agreement. Furthermore, this Statement requires that a government recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party, if the government controls the present service capacity of the beneficial interests. This Statement requires that a government recognize revenue when the resources become applicable to the reporting period. The University is currently assessing the impact statement No. 81 will have on its financial statements.

Reclassifications. Certain reclassifications have been made to the fiscal year 2015 financial statements to conform to the fiscal year 2016 financial statement presentation. These reclassifications had no effect on change in net position.

## **2. DEPOSITS AND INVESTMENTS**

The University's deposits and investments can be grouped into five significant categories, as follows:

- Overnight investments include deposits, money market funds and repurchase agreements with local banks, the Commonwealth and other financial institutions.
- Bond revenue fund investments held by the Treasurer of the Commonwealth as required by the University's bond trust indentures and invested in pooled fixed income funds managed by the Commonwealth.
- Short-term and intermediate-term investments:
  - managed by the University, including individual securities purchased and held by the University,
  - managed by the Commonwealth in pooled fixed income funds, and
  - managed by an external manager in a low duration strategy.
- Debt service sinking fund investments required by the University's bond trust indentures and held by the bond trustees.
- Endowment investments administered by the University and managed using external investment managers.

Deposit and Investment Policies. The Board is responsible for establishing deposit and investment policies. Once established, the Board has delegated day-to-day management to the Treasurer of the University. Deposit and investment policies are developed to ensure compliance with state laws and regulations as well as to establish and maintain sound financial management practices.

The University follows KRS 42.500 for the investment of public funds, which lists allowable investment instruments including: obligations backed by the United States or a United States government agency; obligations of any corporation of the United States government or government-sponsored enterprise; various highly rated fixed income securities including collateralized and uncollateralized certificates of deposit, bankers acceptances, commercial paper, state or local government securities, United States denominated corporate, Yankee and Eurodollar securities; asset-backed securities; highly rated mutual funds comprised of any of the above allowable investments; and state and local property tax certificates of delinquency secured by interests in real property.

The Treasurer of the University manages overnight, short-term and intermediate-term investments based on the Operating Fund Investment Policy. The University's policy for the investment of bond revenue and debt service reserve funds is governed by each respective bond's trust indenture. The Investment Committee of the Board establishes and maintains the University's Endowment Investment Policy.

The fair value of deposits and investments, by Statement of Net Position classification, at June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Statement of Net Position classification		
Current cash and cash equivalents	\$ 693,743	\$ 621,961
Current investments	16,977	21,702
Restricted cash and cash equivalents	398,569	315,522
Endowment investments	1,221,579	1,231,557
Other long-term investments	299,417	275,001
Total	\$ 2,630,285	\$ 2,465,743

**Fair Value.** Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at a measurement date. The framework for measuring fair value established by GAAP provides a fair value hierarchy as follows:

- Level 1 Quoted prices in active markets for identical assets or liabilities.
- Level 2 Observable inputs other than level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities.

The University categorizes its fair value measurements within the fair value hierarchy. Certain investments are measured at fair value using net asset value per share (or its equivalent) practical expedient, amortized costs, or historical costs and therefore have not been classified in the fair value hierarchy. These investments have been included in the table below to permit reconciliation of the fair value hierarchy to the amounts presented in the Statement of Net Position.

The University has the following valuation measurements, by type, at June 30, 2016 (in thousands):

	2016						
	Fair Value Measurement Using				Total Measured at Fair Value	Net Asset Value (NAV)	Amortized or Historical cost
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Value			
<u>Non-endowed deposits and investments</u>							
Cash and cash equivalents	\$ 223,067	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 223,067
Certificates of deposit	30,394	-	-	-	-	-	30,394
Common and preferred stock	7,011	6,564	-	-	6,564	-	447
Corporate fixed income securities	64,396	-	64,396	-	64,396	-	-
Deposits with banks and the Commonwealth of Kentucky	225,144	-	-	-	-	-	225,144
Government agency fixed income securities	128,165	-	128,165	-	128,165	-	-
Guaranteed investment contracts	4,722	-	-	-	-	-	4,722
Other	3,387	-	-	-	-	-	3,387
Pooled equity funds	3,323	3,323	-	-	3,323	-	-
Pooled fixed income funds (1)	673,067	1,899	287,927	-	289,826	-	383,241
Pooled private equity funds	222	-	-	-	-	-	222
Pooled real estate funds	1,085	1,085	-	-	1,085	-	-
State and municipal fixed income securities	11,845	-	11,845	-	11,845	-	-
U.S. Treasury fixed income securities	32,878	-	32,878	-	32,878	-	-
Total non-endowed deposits and investments	1,408,706	12,871	525,211	-	538,082	-	870,624
<u>Endowed deposits and investments</u>							
Cash and cash equivalents	9,292	-	-	-	-	-	9,292
Common and preferred stock	37,228	36,420	-	808	37,228	-	-
Corporate fixed income securities	5,673	-	5,651	22	5,673	-	-
Government agency fixed income securities	2,993	-	2,993	-	2,993	-	-
Other	28	-	28	-	28	-	-
Pooled absolute return funds	138,864	-	-	-	-	138,864	-
Pooled equity funds	301,536	5,120	2,124	-	7,244	294,292	-
Pooled fixed income funds	73,795	-	4,189	-	4,189	69,606	-
Pooled global tactical allocation funds	82,653	-	-	-	-	82,653	-
Pooled long/short equity funds	165,032	-	-	-	-	165,032	-
Pooled private equity funds	173,991	-	-	-	-	173,991	-
Pooled real estate funds	128,858	-	-	-	-	128,858	-
Pooled diversified inflation strategy funds	90,450	-	-	-	-	90,450	-
U.S. Treasury fixed income securities	11,186	-	11,186	-	11,186	-	-
Total endowed deposits and investments	1,221,579	41,540	26,171	830	68,541	1,143,746	9,292
Total deposits and investments	\$ 2,630,285	\$ 54,411	\$ 551,382	\$ 830	\$ 606,623	\$ 1,143,746	\$ 879,916

- 1) Non-endowed pooled fixed income funds include deposits and investments in the Commonwealth's limited pool and intermediate pool funds. As of June 30, 2016, \$383.2 million was held in the Commonwealth's limited-term investment pool and \$287.9 million was held in the intermediate-term pool. The limited-term pool fund's fair value is measured at amortized cost and the intermediate-term pool fund's fair value is measured using level 2 observable inputs. Both investment pools provide same day liquidity with no limitations, fees or restrictions on withdrawals.

The University had the following valuation measurements, by type, at June 30, 2015 (in thousands):

	2015						
	Total Value	Fair Value Measurement Using			Total Measured at Fair Value	Net Asset Value (NAV)	Amortized or Historical cost
Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)				
<u>Non-endowed deposits and investments</u>							
Cash and cash equivalents	\$ 222,720	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 222,720
Certificates of deposit	36,729	-	-	-	-	-	36,729
Common and preferred stock	8,764	8,209	-	-	8,209	-	555
Corporate fixed income securities	52,745	-	52,745	-	52,745	-	-
Deposits with banks and the Commonwealth of Kentucky	68,030	-	-	-	-	-	68,030
Government agency fixed income securities	89,368	-	89,368	-	89,368	-	-
Guaranteed investment contracts	3,786	-	-	-	-	-	3,786
Other	3	-	-	-	-	-	3
Pooled equity funds	6,459	6,459	-	-	6,459	-	-
Pooled fixed income funds (1)	730,798	1,833	110,495	-	112,328	-	618,470
Pooled private equity funds	235	-	-	-	-	-	235
Pooled real estate funds	1,095	1,095	-	-	1,095	-	-
Repurchase agreements	487	-	487	-	487	-	-
State and municipal fixed income securities	12,967	-	12,967	-	12,967	-	-
Total non-endowed deposits and investments	<u>1,234,186</u>	<u>17,596</u>	<u>266,062</u>	<u>-</u>	<u>283,658</u>	<u>-</u>	<u>950,528</u>
<u>Endowed deposits and investments</u>							
Cash and cash equivalents	4,896	-	7	-	7	-	4,889
Common and preferred stock	42,977	42,145	24	808	42,977	-	-
Corporate fixed income securities	8,072	-	8,050	22	8,072	-	-
Government agency fixed income securities	2,558	-	2,558	-	2,558	-	-
Other	145	-	-	-	-	-	145
Pooled absolute return funds	122,347	-	-	-	-	122,347	-
Pooled equity funds	325,799	2,670	2,028	-	4,698	321,101	-
Pooled fixed income funds	91,151	234	1,915	-	2,149	89,002	-
Pooled global tactical allocation funds	88,047	-	-	-	-	88,047	-
Pooled long/short equity funds	173,669	-	-	-	-	173,669	-
Pooled private equity funds	157,027	-	-	-	-	157,027	-
Pooled real estate funds	104,613	292	66	-	358	104,255	-
Pooled diversified inflation strategy funds	101,210	-	-	-	-	101,210	-
U.S. Treasury fixed income securities	9,046	-	9,046	-	9,046	-	-
Total endowed deposits and investments	<u>1,231,557</u>	<u>45,341</u>	<u>23,694</u>	<u>830</u>	<u>69,865</u>	<u>1,156,658</u>	<u>5,034</u>
Total deposits and investments	<u>\$ 2,465,743</u>	<u>\$ 62,937</u>	<u>\$ 289,756</u>	<u>\$ 830</u>	<u>\$ 353,523</u>	<u>\$ 1,156,658</u>	<u>\$ 955,562</u>

- 1) Non-endowed pooled fixed income funds include deposits and investments in the Commonwealth's limited pool and intermediate pool funds. As of June 30, 2015, \$618.5 million was held in the Commonwealth's limited-term investment pool and \$110.5 million was held in the intermediate-term pool. The limited-term pool fund's fair value is measured at amortized cost and the intermediate-term pool fund's fair value is measured using level 2 observable inputs. Both investment pools provide same day liquidity with no limitations, fees or restrictions on withdrawals.

Where quoted market prices are available in an active market, securities are classified within level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in level 2 of the valuation hierarchy. In certain cases, where level 1 or level 2 inputs are not available, securities are classified within level 3 of the hierarchy.

The following describes how the valuation was measured for each category of investment with a level 3 valuation:

- Common and preferred stock investments are valued using either discounted cash flow or market comparable companies technique.
- Corporate fixed income securities are valued using discounted cash flow.

Investments valued using the net asset value (NAV) per share (or its equivalent) as of June 30, 2016 and 2015 are as follows (in thousands):

	2016			
	Net asset value (NAV)	Unfunded commitments	Redemption frequency	Redemption notice period
Pooled absolute return funds (1)	\$ 138,864	\$ 5,144	Quarterly	45 - 90 days
Pooled equity funds (5)	294,292	\$ -	Daily, Monthly	1 - 30 days
Pooled fixed income funds (5)	69,606	\$ -	Daily, Weekly	1 - 3 days
Pooled global tactical allocation funds (5)	82,653	\$ -	Daily	1 day
Pooled long/short equity funds (3)	165,032	\$ -	Monthly, Quarterly	45 - 90 days
Pooled private equity funds (2)	173,991	\$ 118,230	End of term	7 to 10 years
Pooled real estate funds (4)	128,858	\$ 39,393	End of term	7 to 10 years
Pooled diversified inflation strategy funds (2)	90,450	\$ 36,691	Daily	1 day
Total measured at net asset value	<u>\$ 1,143,746</u>			

	2015			
	Net asset value (NAV)	Unfunded commitments	Redemption frequency	Redemption notice period
Pooled absolute return funds (1)	\$ 122,347	\$ -	Quarterly	45 - 90 days
Pooled equity funds (5)	321,101	\$ -	Daily, Monthly	1 - 30 days
Pooled fixed income funds (5)	89,002	\$ -	Daily, Weekly	1 - 3 days
Pooled global tactical allocation funds (5)	88,047	\$ -	Daily	1 day
Pooled long/short equity funds (3)	173,669	\$ -	Monthly, Quarterly	45 - 90 days
Pooled private equity funds (2)	157,027	\$ 138,303	End of term	7 to 10 years
Pooled real estate funds (4)	104,255	\$ 57,093	End of term	7 to 10 years
Pooled diversified inflation strategy funds (2)	101,210	\$ -	Daily, Monthly	1-30 days
Total measured at net asset value	<u>\$ 1,156,658</u>			

- 1) Pooled absolute return funds include several investments in hedge funds that pursue multiple strategies across asset classes globally. As of June 30, 2016, one investment which made up 17% of this investment group is less liquid and has a structure more similar to a private equity fund. That investment does not allow redemptions during its seven-year term.
- 2) Pooled private equity and pooled diversified inflation strategy funds include illiquid investments in private equity and diversified inflation strategies funds that pursue multiple strategies. As of June 30, 2016, total illiquid investments represents one percent of the total and these investments do not offer redemptions prior to the end of the fund's term.



- 3) Pooled long/short equity funds include investments in hedge funds that take both long and short positions in global stocks. The pool includes one investment which made up 25% of the investment group as of June 30, 2016 and 26% as of June 30, 2015, which is less liquid. That investment offers annual redemption beginning January 1, 2017, with 90 day notice.
- 4) Pooled real estate funds include funds that invest in real estate assets globally. These are illiquid investments that do not offer redemptions prior to the end of the fund's term, which can range from seven to 10 years or longer. The pool includes one investment which made up 42% of the investment group as of June 30, 2016 and 48% as of June 30, 2015, which offers more frequent (quarterly) redemptions, with 60 day notice subject to cash availability.
- 5) Pooled equity, pooled fixed income, and pooled global tactical allocation funds include investments in diversified portfolios of stocks and bonds.

The University also holds an alternative investment in a limited partnership whose fair market value is measured using its cost basis of \$222,000 and \$235,000 as of December 31, 2015 and 2014, respectively.

Deposit and Investment Risks. The University's deposits and investments are exposed to various risks, including credit, interest rate and foreign currency risk. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could affect the investment amounts in the Statements of Net Position.

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligation, causing the University to experience a loss of principal.

As a means of limiting its exposure to losses arising from credit risk, the University's investment policies limit the exposure of its various investment types as follows:

- Overnight investment (deposits, money market funds and repurchase agreements) policies minimize credit risk in several ways. Deposits are governed by state law which requires full collateralization for balances exceeding amounts covered by the Federal Deposit Insurance Corporation (FDIC). The University's deposits are insured up to \$250,000 at each FDIC insured institution. Credit risk on deposits in excess of FDIC coverage and on repurchase agreements with local banks is mitigated by the issuing financial institution's pledge of specific U.S. Treasury or agency securities, held in the name of the University by the Federal Reserve Bank. Credit risk on repurchase agreements with the Commonwealth is mitigated by the Commonwealth's requirement that providers of overnight repurchase agreements collateralize these investments at 102% of face value with U.S. Treasury or agency securities, pledged in the name of the Commonwealth. Money market fund portfolios consist of securities eligible for short-term investments.
- Bond revenue fund investments held in the Commonwealth's investment pools can invest in U.S. Treasury and agency securities; commercial paper, asset-backed securities or qualified mutual funds rated in the highest category by a nationally recognized statistical rating organization; certificates of deposit, bankers acceptances, state or local government securities and corporate, Yankee and Eurodollar securities rated in one of the three highest categories by a nationally recognized statistical rating organization; and state and local property tax certificates of delinquency secured by interests in real property.
- Short-term and intermediate-term investments managed by the University and those held in the Commonwealth's investment pools are subject to the same credit quality restrictions as denoted above for bond revenue fund investments. The investment guidelines for the low duration strategy managed by an external manager require that a minimum of 85% of the portfolio holdings are investment grade and a minimum A- portfolio average quality is maintained, with no single credit industry exceeding 15% of the portfolio.
- Investment securities held in bond debt service reserve funds may be invested and reinvested solely in bonds or interest bearing notes of the United States government.
- Endowment managers are permitted to use derivative instruments to limit credit risk.

At June 30, 2016 and 2015, respectively, the credit quality of the University's fixed income investments is summarized below (in thousands):

	2016							Total
	S&P/Moody's Credit Ratings							
	AAA/Aaa	AA/Aa	A	BBB/Baa	Below BBB/Baa	Not rated	Rating not applicable	
<u>Non-ended deposits and investments</u>								
Cash and cash equivalents	\$ 196,057	\$ -	\$ -	\$ -	\$ -	\$ 27,010	\$ -	\$ 223,067
Certificates of deposit	-	-	-	-	-	30,394	-	30,394
Corporate fixed income securities	3,890	4,749	16,777	24,994	13,697	289	-	64,396
Government agency fixed income securities	119,762	8,403	-	-	-	-	-	128,165
Guaranteed investment contracts	-	34	-	-	-	4,688	-	4,722
Pooled fixed income funds	-	-	-	-	-	673,067	-	673,067
State and municipal fixed income securities	7,442	259	4,144	-	-	-	-	11,845
U.S. Treasury fixed income securities	-	-	-	-	-	-	32,878	32,878
Total non-ended fixed income investments	327,151	13,445	20,921	24,994	13,697	735,448	32,878	1,168,534
<u>Endowed deposits and investments</u>								
Cash and cash equivalents	-	-	-	-	-	9,292	-	9,292
Corporate fixed income securities	937	154	1,797	2,006	757	22	-	5,673
Government agency fixed income securities	-	2,993	-	-	-	-	-	2,993
Other	-	-	-	-	-	28	-	28
Pooled fixed income funds	428	69	204	422	827	71,845	-	73,795
U.S. Treasury fixed income securities	-	-	-	-	-	-	11,186	11,186
Total endowed fixed income investments	1,365	3,216	2,001	2,428	1,584	81,187	11,186	102,967
Total fixed income investments	\$ 328,516	\$ 16,661	\$ 22,922	\$ 27,422	\$ 15,281	\$ 816,635	\$ 44,064	\$ 1,271,501

	2015							Total
	S&P/Moody's Credit Ratings							
	AAA/Aaa	AA/Aa	A	BBB/Baa	Below BBB/Baa	Not rated	Rating not applicable	
<u>Non-ended deposits and investments</u>								
Cash and cash equivalents	\$ 213,921	\$ -	\$ -	\$ -	\$ -	\$ 8,799	\$ -	\$ 222,720
Certificates of deposit	-	-	-	-	-	36,729	-	36,729
Corporate fixed income securities	7,565	2,809	15,842	18,578	7,761	190	-	52,745
Government agency fixed income securities	-	88,671	-	-	697	-	-	89,368
Guaranteed investment contracts	-	159	-	-	-	3,627	-	3,786
Pooled fixed income funds	-	-	-	-	-	730,798	-	730,798
Repurchase agreements	-	-	-	-	-	487	-	487
State and municipal fixed income securities	1,834	11,133	-	-	-	-	-	12,967
Total non-ended fixed income investments	223,320	102,772	15,842	18,578	8,458	780,630	-	1,149,600
<u>Endowed deposits and investments</u>								
Cash and cash equivalents	-	-	-	-	-	4,896	-	4,896
Corporate fixed income securities	523	338	3,435	3,281	294	201	-	8,072
Government agency fixed income securities	10	2,188	-	195	165	-	-	2,558
Pooled fixed income funds	-	1,175	-	-	-	89,976	-	91,151
U.S. Treasury fixed income securities	-	-	-	-	-	-	9,046	9,046
Total endowed fixed income investments	533	3,701	3,435	3,476	459	95,073	9,046	115,723
Total fixed income investments	\$ 223,853	\$ 106,473	\$ 19,277	\$ 22,054	\$ 8,917	\$ 875,703	\$ 9,046	\$ 1,265,323

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investment or collateral securities that are in possession of an outside party.

As a means of limiting its exposure to losses arising from custodial credit risk, the University's investment policies limit the exposure of its various investment types as follows:

- Overnight investments (deposits, money market funds and repurchase agreements) are not exposed to custodial credit risk other than repurchase agreements, during the fiscal year ended June 30, 2015, with the Commonwealth, which are held in the Commonwealth's name. Deposits and money market investments are held in the University's name by various financial institutions.
- Bond revenue fund investments held in the Commonwealth's investment pools are held in the Commonwealth's name by the Commonwealth's custodian.
- Short-term and intermediate-term investments held by the Commonwealth for the benefit of the University are invested in the Commonwealth's investment pools and are held in the name of the Commonwealth by the Commonwealth's custodian. Short-term and intermediate-term investments managed by the University are held in the University's name in a safekeeping account. The low duration strategy investments managed by an external manager are held in the University's name by the University's custodian.
- Investment securities held in bond debt service sinking funds are held by the respective bond trustee in a specific trust account for the benefit of the University and bondholders.
- Endowment investments are held in the University's name by the University's custodian.

The University's deposit and investment balances held in the name of the Commonwealth, included in the pooled fixed income funds above, were exposed to custodial credit risk of \$671.2 million as of June 30, 2016, all of which was held in bond revenue investment accounts. As of June 30, 2015, the amount exposed to custodial credit risk with the Commonwealth was \$729.0 million, with \$643.4 million being held in bond revenue investment accounts, \$60.0 million in short-term investments and \$25.6 million in overnight investments. For both 2016 and 2015, these balances were uninsured, not registered in the name of the University and held by the Commonwealth but not in the University's name.

Concentrations of Credit Risk. University investments can be exposed to a concentration of credit risk if significant amounts are invested in any one issuer.

As a means of limiting its exposure to concentrations of credit risk, the University's investment policies limit concentrations in various investment types as follows:

- Overnight investments (deposits, money market funds and repurchase agreements) are not limited to a maximum amount that may be invested in one issuer. However, all such deposits in excess of federal deposit insurance are required to be fully collateralized by U.S. Treasury and/or U.S. agency securities or other similar investments as provided by KRS 41.240.
- Bond revenue fund investments held in the Commonwealth's investment pools are limited as follows: U.S. dollar denominated corporate and Yankee securities issued by foreign and domestic issuers shall not exceed 35% of an individual pool and \$25.0 million per issuer, inclusive of commercial paper, bankers acceptances and certificates of deposit per individual pool; and U.S. dollar denominated sovereign debt shall not exceed five percent of any individual portfolio and \$25.0 million per issuer.
- Short-term and intermediate-term investments managed by the University and those held in the Commonwealth's investment pools are subject to the same credit concentration restrictions as denoted above for the bond revenue fund investments. Investments in the low duration strategy managed by an external manager are limited such that no single credit industry shall exceed 15% of the portfolio at purchase.
- There is no specific limit on the maximum amount of investment securities held in bond debt service sinking funds that may be invested in one issuer. However, such investments are limited to bonds or interest bearing notes of the U.S. government.
- Endowment fixed income managers are limited to a maximum investment in any one issuer of no more than five percent of total investments excluding sovereign debt of governments belonging in the Organization for Economic Co-operation and Development and U.S. agencies.

At June 30, 2016 and 2015, the University had no investments in any one issuer, other than U.S. Treasury and/or U.S. agency securities, that represented five percent or more of total investments.

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

As a means of limiting its exposure to fair value losses arising from increasing interest rates, the University's investment policies limit the maturity of its various investment types as follows:

- Overnight investments (deposits, money market funds and repurchase agreements) have limited exposure to interest rate risk due to the short-term nature of the investment. The University requires that all deposits and repurchase agreements be available for use on the next business day.
- Bond revenue fund investments and short-term investments held in the Commonwealth's short-term investment pool are limited to an average maturity that does not exceed 90 days. Such investments in the Commonwealth's intermediate-term investment pool must maintain an effective duration of less than three years.
- Short-term and intermediate-term investments managed by the University are generally limited to a maximum maturity of 24 months and those held in the Commonwealth's investment pools are subject to the same maturity and duration limits as denoted above for bond revenue fund investments. The portfolio duration of the low duration strategy investment managed by an external manager must be within a range of +/- 0.5 years of the Barclays Capital U.S. Government/Credit 1-5 Year Index.
- Investment securities held in bond debt service sinking funds are required to have a maturity no later than two years from the date of the investment.
- Endowment managers are permitted to use derivative instruments to limit interest rate risk. Additionally, endowment investments held by core-plus fixed income managers are limited to a duration that is within two years of the duration of the Barclays Capital U.S. Aggregate Bond Index and unconstrained fixed income strategies have been implemented to further protect against interest rate risk.

For June 30, 2016 and 2015, the maturity distribution of the University's fixed income investments is summarized below (in thousands):

Investment Type	2016					Total
	Maturities in Years					
	Less than 1	1-5	5-10	Greater than 10	Managed based on duration	
<u>Non-endowed deposits and investments</u>						
Cash and cash equivalents	\$ 217,555	\$ -	\$ -	\$ -	\$ 5,512	\$ 223,067
Certificates of deposit	30,394	-	-	-	-	30,394
Corporate fixed income securities	201	228	221	-	63,746	64,396
Government agency fixed income securities	-	119,316	225	-	8,624	128,165
Guaranteed investment contracts	8	-	34	4,680	-	4,722
Pooled fixed income funds	-	-	-	-	673,067	673,067
State and municipal fixed income securities	3,976	7,869	-	-	-	11,845
U.S. Treasury fixed income securities	-	-	-	-	32,878	32,878
Total non-endowed fixed income investments	<u>252,134</u>	<u>127,413</u>	<u>480</u>	<u>4,680</u>	<u>783,827</u>	<u>1,168,534</u>
<u>Endowed deposits and investments</u>						
Cash and cash equivalents	7,085	-	-	-	2,207	9,292
Corporate fixed income securities	1	-	-	21	5,651	5,673
Government agency fixed income securities	-	-	-	-	2,993	2,993
Other	-	-	-	-	28	28
Pooled fixed income funds	-	-	-	-	73,795	73,795
U.S. Treasury fixed income securities	30	74	-	-	11,082	11,186
Total endowed fixed income investments	<u>7,116</u>	<u>74</u>	<u>-</u>	<u>21</u>	<u>95,756</u>	<u>102,967</u>
Total fixed income investments	<u>\$ 259,250</u>	<u>\$ 127,487</u>	<u>\$ 480</u>	<u>\$ 4,701</u>	<u>\$ 879,583</u>	<u>\$ 1,271,501</u>

Investment Type	2015					Total
	Maturities in Years					
	Less than 1	1-5	5-10	Greater than 10	Managed based on duration	
<u>Non-endowed deposits and investments</u>						
Cash and cash equivalents	\$ 221,906	\$ -	\$ -	\$ -	\$ 814	\$ 222,720
Certificates of deposit	36,729	-	-	-	-	36,729
Corporate fixed income securities	323	452	224	-	51,746	52,745
Government agency fixed income securities	-	82,043	335	-	6,990	89,368
Guaranteed investment contracts	-	56	159	3,571	-	3,786
Pooled fixed income funds	-	-	-	-	730,798	730,798
Repurchase agreements	487	-	-	-	-	487
State and municipal fixed income securities	5,116	7,851	-	-	-	12,967
Total non-endowed fixed income investments	<u>264,561</u>	<u>90,402</u>	<u>718</u>	<u>3,571</u>	<u>790,348</u>	<u>1,149,600</u>
<u>Endowed deposits and investments</u>						
Cash and cash equivalents	2,718	-	-	-	2,178	4,896
Corporate fixed income securities	1	-	-	22	8,049	8,072
Government agency fixed income securities	-	-	-	-	2,558	2,558
Pooled fixed income funds	-	-	-	-	91,151	91,151
U.S. Treasury fixed income securities	-	101	-	-	8,945	9,046
Total endowed fixed income investments	<u>2,719</u>	<u>101</u>	<u>-</u>	<u>22</u>	<u>112,881</u>	<u>115,723</u>
Total fixed income investments	<u>\$ 267,280</u>	<u>\$ 90,503</u>	<u>\$ 718</u>	<u>\$ 3,593</u>	<u>\$ 903,229</u>	<u>\$ 1,265,323</u>

At June 30, 2016 and 2015, the University had the following investments managed based on duration (in thousands):

Investment Type	2016		2015	
	Fair Value	Modified Duration (Years)	Fair Value	Modified Duration (Years)
<u>Non-endowed deposits and investments</u>				
Cash and cash equivalents	\$ 5,512	2.4	\$ 814	2.3
Corporate fixed income securities	63,746	2.4	51,746	2.3
Government agency fixed income securities	8,624	2.4	6,990	2.3
U.S. Treasury fixed income securities	32,878	2.4	-	-
Pooled fixed income				
Commonwealth of Kentucky intermediate pool	287,927	1.1	60,000	1.1
Commonwealth of Kentucky limited pool	383,241	0.1	668,965	0.1
KTI	95	1.1	57	2.3
KMSF	1,804	3.8	1,776	2.9
Total non-endowment investment	<u>783,827</u>		<u>790,348</u>	
<u>Endowed deposits and investments</u>				
Cash and cash equivalents	2,207	4.4	2,178	4.5
Corporate fixed income	5,651	4.7	8,049	4.6
Government agency fixed income	2,993	4.7	2,558	4.6
Other	28	4.7	-	-
Pooled fixed income				
Pooled endowment fund	70,835	2.6	89,002	1.6
Other endowment investments	2,960	5.9	2,149	5.8
U.S. Treasury fixed income	11,082	4.7	8,945	3.2
Total endowment investment	<u>95,756</u>		<u>112,881</u>	
Total managed based on duration	<u>\$ 879,583</u>		<u>\$ 903,229</u>	

Foreign Currency Risk. Foreign currency risk is the risk that fluctuations in exchange rates will adversely affect the fair value of an investment or deposit.

The University's exposure to foreign currency risk derives from certain endowment investments. The University's endowment investment policy allows fixed income managers to invest a portion of their portfolios in non-U.S. securities. Additionally, the investment policy allows various pooled fund managers to invest in accordance with the guidelines established in each individual fund's prospectus, which allows for investment in non-U.S. securities. Endowment managers are permitted to use derivative instruments to limit foreign currency risk.

As of June 30, 2016 and 2015, the following endowment investments were subject to foreign currency risk (in thousands):

	Fair Value	
	2016	2015
Common stock	\$ 33,459	\$ 38,289
Pooled private equity funds	5,929	6,971
Pooled real estate funds	7,404	5,174
Cash equivalents	288	720
Total	<u>\$ 47,080</u>	<u>\$ 51,154</u>

### 3. NOTES, LOANS AND ACCOUNTS RECEIVABLE, NET

Notes, loans and accounts receivable as of June 30, 2016 and 2015 are as follows (in thousands):

	2016		
	Gross Receivable	Allowance	Net Receivable
Accrued interest receivable	\$ 1,554	\$ -	\$ 1,554
Dentistry patient accounts	3,085	(846)	2,239
Hospital patient accounts	199,788	(61,182)	138,606
KMSF patient accounts	42,014	(6,884)	35,130
Multimedia rights receivable	191,644	-	191,644
Pledges receivable (less discounts of \$8,303)	95,488	(29,930)	65,558
Reimbursement receivable - federal appropriations	2,153	-	2,153
Reimbursement receivable - grants and contracts	30,911	(325)	30,586
Service concession arrangements	90,646	-	90,646
Student loans	28,297	(3,261)	25,036
Student receivables	28,098	(16,233)	11,865
Other	29,969	-	29,969
<b>Total</b>	<b>\$ 743,647</b>	<b>\$ (118,661)</b>	<b>\$ 624,986</b>
Current portion			\$ 297,620
Noncurrent portion			327,366
<b>Total</b>			<b>\$ 624,986</b>

	2015		
	Gross Receivable	Allowance	Net Receivable
Accrued interest receivable	\$ 1,885	\$ -	\$ 1,885
Dentistry patient accounts	2,766	(696)	2,070
Hospital patient accounts	176,436	(40,923)	135,513
KMSF patient accounts	32,421	(4,003)	28,418
Multimedia rights receivable	210,000	-	210,000
Pledges receivable (less discounts of \$7,376)	78,537	(26,650)	51,887
Reimbursement receivable - federal appropriations	1,604	-	1,604
Reimbursement receivable - grants and contracts	32,793	(400)	32,393
Service concession arrangements	98,832	-	98,832
Student loans	29,747	(3,103)	26,644
Student receivables	28,189	(16,328)	11,861
Other	30,622	-	30,622
<b>Total</b>	<b>\$ 723,832</b>	<b>\$ (92,103)</b>	<b>\$ 631,729</b>
Current portion			\$ 292,776
Noncurrent portion			338,953
<b>Total</b>			<b>\$ 631,729</b>

In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, the University is required to record operating and capital pledges as revenue when all eligibility requirements have been met. Endowment pledges are not recognized as revenue until the gifts are actually received. For the years ended June 30, 2016 and 2015, the University recorded the discounted value of operating and capital pledges using a rate of two percent.

Deferred gifts through insurance, known bequests and irrevocable trusts in which the University has a remainder interest are estimated to be approximately \$144.1 million and \$115.7 million at June 30, 2016 and 2015, respectively. The University records these amounts as revenue when the cash is received.

#### 4. CAPITAL ASSETS, NET

Capital assets as of June 30, 2016 and capital asset activity for the year ended June 30, 2016 are summarized below (in thousands):

	June 30, 2015	Additions	Deletions	June 30, 2016
Land	\$ 73,347	\$ 1,298	\$ -	\$ 74,645
Land improvements - nonexhaustible	46,226	10,650	-	56,876
Land improvements - exhaustible	74,279	14,982	-	89,261
Buildings	2,431,549	432,802	17,612	2,846,739
Fixed equipment - communications	100,616	13,407	34	113,989
Infrastructure	99,956	7,833	-	107,789
Equipment	579,129	61,958	114,851	526,236
Vehicles	21,903	2,022	1,441	22,484
Library materials	145,933	1,819	529	147,223
Nondepreciable library materials	6,651	22	-	6,673
Capitalized software	155,915	12,645	-	168,560
Art	11,786	966	1	12,751
Certificate of need license	11,609	-	-	11,609
Construction in progress	266,891	198,946	206,811	259,026
	<u>4,025,790</u>	<u>759,350</u>	<u>341,279</u>	<u>4,443,861</u>
<u>Accumulated Depreciation</u>				
Land improvements - exhaustible	58,019	3,334	-	61,353
Buildings	865,995	71,540	13,144	924,391
Fixed equipment - communications	65,432	7,245	34	72,643
Infrastructure	36,615	3,900	-	40,515
Equipment	417,750	39,877	88,423	369,204
Vehicles	18,556	1,553	1,435	18,674
Library materials	137,183	2,307	-	139,490
Capitalized software	89,600	18,353	-	107,953
	<u>1,689,150</u>	<u>148,109</u>	<u>103,036</u>	<u>1,734,223</u>
Capital assets, net	<u>\$ 2,336,640</u>	<u>\$ 611,241</u>	<u>\$ 238,243</u>	<u>\$ 2,709,638</u>



Capital assets as of June 30, 2015 and capital asset activity for the year ended June 30, 2015 are summarized below (in thousands):

	June 30, 2014	Additions	Deletions	June 30, 2015
Land	\$ 72,394	\$ 953	\$ -	\$ 73,347
Land improvements - nonexhaustible	42,643	3,583	-	46,226
Land improvements - exhaustible	70,231	4,048	-	74,279
Buildings	2,209,332	247,090	24,873	2,431,549
Fixed equipment - communications	96,579	4,253	216	100,616
Infrastructure	95,385	4,619	48	99,956
Equipment	571,221	59,158	51,250	579,129
Vehicles	21,400	1,750	1,247	21,903
Library materials	144,330	2,565	962	145,933
Nondepreciable library materials	6,651	-	-	6,651
Capitalized software	142,580	13,486	151	155,915
Art	11,459	327	-	11,786
Certificate of need license	11,609	-	-	11,609
Construction in progress	91,637	213,434	38,180	266,891
	<u>3,587,451</u>	<u>555,266</u>	<u>116,927</u>	<u>4,025,790</u>
<u>Accumulated Depreciation</u>				
Land improvements - exhaustible	55,278	2,741	-	58,019
Buildings	822,366	59,489	15,860	865,995
Fixed equipment - communications	59,347	6,276	191	65,432
Infrastructure	33,001	3,631	17	36,615
Equipment	408,068	45,707	36,025	417,750
Vehicles	18,252	1,461	1,157	18,556
Library materials	134,477	2,706	-	137,183
Capitalized software	77,258	12,363	21	89,600
	<u>1,608,047</u>	<u>134,374</u>	<u>53,271</u>	<u>1,689,150</u>
Capital assets, net	<u>\$ 1,979,404</u>	<u>\$ 420,892</u>	<u>\$ 63,656</u>	<u>\$ 2,336,640</u>

At June 30, 2016, the University had construction projects in progress totaling approximately \$957.9 million in scope. The estimated cost to complete these projects was approximately \$699.5 million. Such construction was principally financed by cash reserves, gifts and grants, and proceeds from the University's general receipts bonds.

Interest costs incurred during construction, net of related investment income, are capitalized. Total interest capitalized was \$11.9 million for 2016 and \$8.0 million for 2015.

During fiscal years 2016 and 2015, the University utilized capital leases to acquire various items of equipment. As of June 30, 2016 and 2015, the net book value of land, buildings, equipment and software acquired through capital leases included in the above schedules totaled \$98.0 million and \$115.5 million, respectively.

During fiscal year 2016, 25 properties were demolished with an original cost of \$17.0 million and accumulated depreciation of \$13.1 million, for a total net book value written off of \$3.9 million. Most notably, the student center demolition was completed in 2016, which had an original cost of \$14.8 million and a net book value written off of \$2.9 million.

Non-cash capital asset and related financing activities as of June 30, 2016 and 2015 are summarized below (in thousands):

	<u>2016</u>	<u>2015</u>
Capital lease additions	\$ 6,888	\$ 26,063
Gifts of capital assets	\$ 1,932	\$ 2,750
Capital asset change in accounts payable	\$ (14,762)	\$ 39,976
Capital asset additions by service concession arrangements	\$ 146,910	\$ 150,107
Capitalized interest, net of investment income	\$ 11,886	\$ 8,037
Amortized bond discount and premium	\$ 6,528	\$ 7,719
Amortized difference between reacquisition price and net carrying amount of refunded debt	\$ 1,592	\$ 828
Capital asset trade in	\$ 734	\$ 1,594

## 5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2016 and 2015 are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Payable to vendors and contractors	\$ 193,926	\$ 183,829
Accrued expenses, including vacation and sick leave	94,258	78,311
Employee withholdings and deposits payable to third parties	38,633	49,168
Total	<u>\$ 326,817</u>	<u>\$ 311,308</u>

## 6. UNEARNED REVENUE

Unearned revenues as of June 30, 2016 are as follows (in thousands):

	<u>June 30, 2015</u>	<u>Additions</u>	<u>Reductions</u>	<u>June 30, 2016</u>	<u>Current Portion</u>	<u>Non-current Portion</u>
Unearned summer school revenue	\$ 9,102	\$ 10,217	\$ 10,037	\$ 9,282	\$ 9,282	\$ -
Unearned hospital revenue	10,622	80,586	84,178	7,030	7,030	-
Unearned grants and contracts revenue	25,967	71,619	67,035	30,551	30,551	-
Unearned multimedia rights revenue	207,084	544	14,044	193,584	14,037	179,547
Prepaid athletic ticket sales	13,531	12,464	15,279	10,716	10,716	-
Other	6,564	22,458	20,684	8,338	8,032	306
Total	<u>\$ 272,870</u>	<u>\$ 197,888</u>	<u>\$ 211,257</u>	<u>\$ 259,501</u>	<u>\$ 79,648</u>	<u>\$ 179,853</u>

Unearned revenues as of June 30, 2015 are as follows (in thousands):

	June 30, 2014	Additions	Reductions	June 30, 2015	Current Portion	Non-current Portion
Unearned summer school revenue	\$ 8,934	\$ 9,259	\$ 9,091	\$ 9,102	\$ 9,102	\$ -
Unearned hospital revenue	7,545	76,318	73,241	10,622	10,622	-
Unearned grants and contracts revenue	23,140	59,967	57,140	25,967	25,967	-
Unearned multimedia rights revenue	-	210,000	2,916	207,084	14,001	193,083
Prepaid athletic ticket sales	12,636	14,557	13,662	13,531	13,531	-
Other	7,762	10,151	11,349	6,564	6,553	11
Total	<u>\$ 60,017</u>	<u>\$ 380,252</u>	<u>\$ 167,399</u>	<u>\$ 272,870</u>	<u>\$ 79,776</u>	<u>\$ 193,094</u>

A multimedia rights partnership was formed in July 2014 between the University and JMI Sports providing athletics and campus multimedia marketing rights in a 15 year, \$210.0 million agreement. Under the contract, the University will receive a guaranteed rights fee in each of the 15 years of the partnership, starting at \$9.1 million in fiscal year 2015-16 and increasing to \$16.0 million in fiscal year 2029-30. The agreement also included a \$29.4 million signing bonus to be paid over the first two years of the contract. This agreement was modified in April 2016 to increase the signing bonus to \$29.9 million, which will now be paid over the first three years of the contract. This modification increased the total amount to be received to \$210.5 million.

## 7. LONG-TERM LIABILITIES

Long-term liabilities as of June 30, 2016 and long-term liability activity for the year ended June 30, 2016 are summarized below (in thousands):

	June 30, 2015	Additions	Reductions	June 30, 2016	Current Portion	Non-current Portion
<u>Bonds, notes and capital leases</u>						
General receipts notes	\$ 69,195	\$ -	\$ 16,440	\$ 52,755	\$ 11,330	\$ 41,425
General receipts bonds	751,735	155,780	14,845	892,670	21,425	871,245
Capital leases and other						
long-term obligations	89,984	7,233	17,916	79,301	16,185	63,116
Notes payable	19,529	-	600	18,929	18,929	-
Total bonds, notes and capital leases	<u>930,443</u>	<u>163,013</u>	<u>49,801</u>	<u>1,043,655</u>	<u>67,869</u>	<u>975,786</u>
<u>Other liabilities</u>						
Annuities payable	3,802	461	624	3,639	549	3,090
Automobile and property self insurance	462	275	259	478	478	-
Compensated absences	7,300	-	100	7,200	781	6,419
Federal loan programs	20,377	452	369	20,460	-	20,460
Health insurance	8,580	46,375	44,936	10,019	10,019	-
Insurance executory costs	6,075	5,385	155	11,305	155	11,150
Long-term disability	2	-	2	-	-	-
Medical malpractice	30,597	15,112	12,416	33,293	6,652	26,641
Retiree health benefits trust	108,815	13,036	1,839	120,012	-	120,012
Unamortized bond premium	60,629	5,147	6,529	59,247	6,504	52,743
Unemployment compensation	575	716	728	563	563	-
Workers compensation	25,080	4,184	6,660	22,604	5,933	16,671
Other	9,667	14,961	8,720	15,908	2,566	13,342
Total other liabilities	<u>281,961</u>	<u>106,104</u>	<u>83,337</u>	<u>304,728</u>	<u>34,200</u>	<u>270,528</u>
Total	<u>\$ 1,212,404</u>	<u>\$ 269,117</u>	<u>\$ 133,138</u>	<u>\$ 1,348,383</u>	<u>\$ 102,069</u>	<u>\$ 1,246,314</u>

Long-term liabilities as of June 30, 2015 and long-term liability activity for the year ended June 30, 2015 are summarized below (in thousands):

	June 30, 2014	Additions	Reductions	June 30, 2015	Current Portion	Non-current Portion
<u>Bonds, notes and capital leases</u>						
General receipts notes	\$ 265,180	\$ -	\$ 195,985	\$ 69,195	\$ 16,440	\$ 52,755
General receipts bonds	432,500	347,185	27,950	751,735	14,845	736,890
Educational buildings bonds	33,350	-	33,350	-	-	-
Capital leases and other long-term obligations	86,485	26,693	23,194	89,984	17,298	72,686
Notes payable	20,664	-	1,135	19,529	600	18,929
<b>Total bonds, notes and capital leases</b>	<b>838,179</b>	<b>373,878</b>	<b>281,614</b>	<b>930,443</b>	<b>49,183</b>	<b>881,260</b>
<u>Other liabilities</u>						
Annuities payable	5,701	653	2,552	3,802	565	3,237
Arbitrage rebate	27	-	27	-	-	-
Automobile and property self insurance	440	1,491	1,469	462	462	-
Compensated absences	7,634	-	334	7,300	721	6,579
Federal loan programs	20,533	375	531	20,377	-	20,377
Health insurance	7,189	40,620	39,229	8,580	8,580	-
Insurance executory costs	-	6,157	82	6,075	82	5,993
Long-term disability	-	2	-	2	2	-
Medical malpractice	29,297	8,959	7,659	30,597	6,006	24,591
Retiree health benefits trust	97,317	11,498	-	108,815	-	108,815
Unamortized bond premium	22,160	46,250	7,781	60,629	6,437	54,192
Unemployment compensation	622	705	752	575	575	-
Workers compensation	21,773	9,967	6,660	25,080	7,167	17,913
Other	8,402	7,812	6,547	9,667	1,623	8,044
<b>Total other liabilities</b>	<b>221,095</b>	<b>134,489</b>	<b>73,623</b>	<b>281,961</b>	<b>32,220</b>	<b>249,741</b>
<b>Total</b>	<b>\$ 1,059,274</b>	<b>\$ 508,367</b>	<b>\$ 355,237</b>	<b>\$ 1,212,404</b>	<b>\$ 81,403</b>	<b>\$ 1,131,001</b>

Annuities payable consists of the present value of future payments due under charitable remainder annuity trusts, charitable remainder unitrusts, lead trusts, irrevocable trusts and charitable gift annuities, discounted at 3.6% to 10.8%.

Bond discounts and premiums are amortized over the life of the bond using the effective interest method.

Bonds payable consist of general receipts bonds and general receipts notes in the original amount of \$1.29 billion dated October 6, 2006 through February 10, 2016, which bear interest at 1.0% to 4.7%. The bonds are payable in annual installments through April 1, 2046. The University is required to make semi-annual deposits of varying amounts to the debt service funds held by the trustees. The bonds are secured by the net revenues of the University and the assets restricted under the bond indenture agreements. Capital leases are due in periodic installments through November 20, 2028 and bear interest at 1.4% to 4.5%. All bonds, except for the General Receipts 2012 Bonds Series A and General Receipts 2014 Bonds Series C, totaling \$919.6 million, are callable between October 2016 and April 2025.

The indenture agreements require that certain funds be established with the trustee and with the Commonwealth.

On February 10, 2016, approximately \$155.8 million of University of Kentucky General Receipts 2016 Bonds Series A and B at a true interest cost of 3.6% and 2.8%, respectively, were issued for the purpose of funding the construction of the new student center.

In prior fiscal years, certain general receipts bonds series were issued as Build America Bonds (BAB) as authorized under the American Recovery and Reinvestment Act of 2009 and as Qualified Energy Conservation Bonds (QECCB) as authorized under the Recovery Act and the Hiring Incentive to Restore Employment Act of 2010. The University will receive an annual cash subsidy from the U.S. Treasury equal to 35% (BAB) and 80% (QECCB) of the interest payable on the bonds. The subsidy, which was approximately \$2.3 million during fiscal years 2016 and 2015, was included in gifts and non-exchange grants in the Statements of Revenues, Expenses and Changes in Net Position. The subsidy payment is contingent on federal regulations and may be subject to change. On March 1, 2013, the President signed an executive order reducing the budgetary authority in accounts subject to sequestration. As a result, the BAB subsidy was reduced to approximately 33% and 32% in 2016 and 2015, respectively. The QECCB subsidy was reduced to approximately 74% in 2016 and 2015.

Principal maturities and interest on bonds, notes and capital leases for the next five fiscal years and in subsequent five-year fiscal periods as of June 30, 2016, are as follows (in thousands):

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2017	\$ 67,869	\$ 43,493	\$ 111,362
2018	52,147	40,409	92,556
2019	48,238	38,590	86,828
2020	49,551	36,826	86,377
2021	48,658	34,701	83,359
2022-2026	252,867	146,592	399,459
2027-2031	157,245	93,237	250,482
2032-2036	130,740	65,286	196,026
2037-2041	133,910	36,789	170,699
2042-2046	102,430	10,688	113,118
Total	<u>\$ 1,043,655</u>	<u>\$ 546,611</u>	<u>\$ 1,590,266</u>

At June 30, 2016, assets with a fair market value of approximately \$129.9 million have been placed on deposit with trustees to totally defease bonds with a par amount of approximately \$122.6 million. The liability for these fully defeased bonds is not included in the financial statements.

## 8. DEFERRED INFLOWS OF RESOURCES

As of June 30, 2016 and 2015, deferred inflows of resources are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Aramark service concession arrangement	\$ 140,306	\$ 105,900
Barnes and Noble service concession arrangement	4,084	4,924
EdR service concession arrangement	222,356	130,300
Total	<u>\$ 366,746</u>	<u>\$ 241,124</u>

The University has entered into a multi-phase housing project with a third party developer, Education Realty Trust (EdR), to complete a long-term housing plan. Phase I, signed in April 2012, was for two four-story buildings (601 beds), and opened in August 2013. The project, with a cost of \$25.2 million, is on land owned by the University and leased to EdR for a 50 year term with options for additional 10 year and 15 year terms thereafter. At the conclusion of the initial 50 year term or the first renewal option, the University will be required to purchase the buildings from EdR for an appraised value, unless the ground lease is renewed for the first or second optional extension. At the conclusion of the second optional extension, the University is required to purchase the buildings for the greater of current net book value or \$10. Ground lease is a percentage of gross revenues. The University accounts for the ground lease as an operating lease. These facilities are subject to ad valorem tax.

Phase II-A and Phase II-B, which opened in August 2014 and August 2015 respectively, included the development of eight residence halls at a cost of \$238.4 million. The residence halls are reported as a capital asset with a carrying value of \$233.4 million at June 30, 2016 and deferred inflows of resources in the amount

of \$222.3 million pursuant to the service concession arrangement. The 75 year term lease with EdR includes maintenance standards for the facilities and parameters for the room rental rates for the contract duration. The University will receive a percentage of the total revenues and a share of the net income, after EdR achieves a minimum internal rate of return. Phase II-A and subsequent phases are exempt from ad valorem tax.

Future plans include Phase II-C for the construction of two residence halls at an approximate cost of \$83.9 million opening in August 2016; Phase III-A, expected to open in August 2017, will be a \$74.0 million, 771 bed facility which will provide apartment style units for upper class, graduate and professional students; Phase III-B, expected to also open in August 2017, will be a \$37.1 million, 346 bed facility to house undergraduate students and will include space dedicated to the future Lewis Honors College.

In July 2014, the University entered into an approximately \$250.0 million contract with Aramark Enterprise Services, LLC (Aramark), forming a 15 year public/private partnership. This partnership is transforming dining services offered to students, faculty, staff, and the community served. Under the partnership, several new food brands are located on campus. Aramark provides meals covered under the University's student boarding plans and declining balance dollars. The contract allows for dining commissions to be paid to the University with guaranteed minimum amounts for each contract year. Aramark is providing \$70.0 million in facilities investments, including \$40.0 million in new facilities, subject to board approval, to be completed by fiscal year 2017-18. As part of these facilities investments, Aramark constructed a new K Lair Grill at Haggin Hall, made substantial upgrades to the student center food court and constructed "The 90" dining facility for the Fall 2015 semester. The completed projects are reported as a capital asset with a carrying value of \$56.0 million at June 30, 2016 and deferred inflows of resources in the amount of \$52.0 million pursuant to the service concession arrangement. The present value of the guaranteed minimum payments over the remaining 13 years of the contract is reported as a receivable of \$86.7 million and deferred inflows of resources in the amount of \$88.3 million pursuant to the service concession arrangement.

In June 2015, the University entered into a contract with Barnes and Noble College Booksellers (Barnes and Noble) to operate and provide services for the bookstore for ten years with an additional five year renewal option period. Barnes and Noble constructed a temporary bookstore for use until the new student center opens in January 2018. The present value of the guaranteed minimum payments over the remaining 14 years of the contract period is reported as a receivable of \$4.0 million and deferred inflows of resources in the amount of \$4.1 million pursuant to the service concession arrangement.

## 9. COMPONENTS OF RESTRICTED EXPENDABLE NET POSITION

Restricted expendable net position are subject to externally imposed stipulations or conditions that must be followed and cannot be used for support of general operations of the University. As of June 30, 2016 and 2015, restricted expendable net position is composed of the following (in thousands):

	2016	2015
Appreciation on permanent endowments	\$ 123,005	\$ 158,121
Term endowments	7,432	9,123
Quasi-endowments initially funded with restricted assets	50,090	50,775
Funds restricted for capital projects and debt service	186,185	129,458
Funds restricted for noncapital purposes	115,987	93,605
Loan funds (primarily University funds required for federal match)	11,455	10,908
Total	\$ 494,154	\$ 451,990

## 10. DESIGNATIONS OF UNRESTRICTED NET POSITION

Unrestricted net position is designated for specific purposes by action of the Board or management or may otherwise be limited by contractual agreements. Commitments for the use of unrestricted net position as of June 30, 2016 and 2015 are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Working capital requirements	\$ 92,944	\$ 109,072
Budget appropriations for future year fiscal operations	209,665	180,535
Designated for capital projects	43,930	36,831
Designated for renewal and replacement of capital assets	52,368	31,021
UK HealthCare Hospital System	647,928	585,764
Affiliated corporations and component units	56,801	54,411
Total	<u>\$ 1,103,636</u>	<u>\$ 997,634</u>

## 11. PLEDGED REVENUES

Pledged revenues for 2016 and 2015 as defined by the General Receipts Trust Indenture, are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Student tuition and fees	\$ 319,627	\$ 302,936
Nongovernmental grants and contracts	1,145	849
Recoveries of facilities and administrative costs	51,088	48,154
Sales and services	48,710	40,004
Hospital services	1,417,243	1,323,652
Auxiliary enterprises - housing and dining	39,103	39,265
Auxiliary enterprises - athletics	102,995	88,928
Auxiliary enterprises - other	49,434	47,039
Other operating revenue	838	852
State appropriations	279,611	279,611
Gifts and grants	4,583	4,955
Investment income	10,761	21,774
Total	<u>\$ 2,325,138</u>	<u>\$ 2,198,019</u>

The University has substantially pledged all of the unrestricted operating and nonoperating revenues to repay the general receipts bonds and notes issued during 2005 to 2016. Proceeds from the bonds and notes provided funding for new construction, major renovations, and for the refunding of bonds and notes issued over the years. The bonds are payable from unrestricted revenues, operating and nonoperating, and are payable through 2046. Annual principal and interest payments on bonds are expected to require approximately three percent of pledged revenue. The total principal and interest remaining to be paid on the bonds is approximately \$1.47 billion and \$1.28 billion in 2016 and 2015, respectively. Principal and interest paid for 2016 and 2015 was \$64.6 million and \$53.2 million, respectively.

## 12. INVESTMENT INCOME

Components of investment income (loss) for the years ended June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Interest and dividends earned on endowment investments	\$ 15,073	\$ 12,154
Realized and unrealized gains (losses) on endowment investments	(26,808)	9,877
Interest and dividends on cash and non-endowment investments	7,463	3,242
Realized and unrealized gains (losses) on non-endowment investments	(49)	18,293
Investment income from external trusts	1,656	1,622
Total	<u>\$ (2,665)</u>	<u>\$ 45,188</u>

## 13. FUNDS HELD IN TRUST BY OTHERS

The University is the income beneficiary of various trusts that are held and controlled by external trustees. For the years ended June 30, 2016 and 2015, the University received income from these trusts of approximately \$1.7 million and \$1.6 million, respectively. The market value of the external trust assets as of June 30, 2016 and 2015 was approximately \$37.4 million and \$41.5 million, respectively. As the University does not have ownership of the trust assets held by external trustees, the trusts are recorded at a nominal value of \$1 each.

Effective January 1, 2016, the University became the administrator of five trusts that were previously held and controlled by external trustees. The University received income from these self-administered trusts of approximately \$42,000. The market value of the self-administered trusts as of June 30, 2016 was approximately \$1.8 million and included in endowment investments.

## 14. GRANTS AND CONTRACTS AWARDED

At June 30, 2016 and 2015, grants and contracts of approximately \$201.4 million and \$189.2 million, respectively, have been awarded to the University and the University of Kentucky Research Foundation, but not expended. These amounts will be recognized in future periods.

## 15. RETIREMENT PLANS

Regular full-time employees, including faculty, are participants in the University of Kentucky Retirement Plan, a defined contribution plan. The University of Kentucky Retirement Plan consists of five groups as follows:

Group I	Established July 1, 1964, for faculty and certain administrative officials.
Group II	Established July 1, 1971, for staff members in the clerical, technical and service categories.
Group III	Established July 1, 1972, for staff members in the managerial, professional and scientific categories.
Group IV	Established January 1, 1973, for staff members having U.S. Civil Service retirement entitlement.
Group V	Established July 1, 1987, for staff members covered under the Federal Employees Retirement System that replaced Civil Service (those whose employment began during the period from January 1, 1984 to March 31, 1987). Staff members whose employment began after March 31, 1987 are under one of the above University of Kentucky Retirement Plans.



Participation in the University of Kentucky Retirement Plan is mandatory for all regular full-time employees in groups I, II and III who are age 30 or older. Participation is voluntary for regular full-time employees under the age of 30 and for those employees in groups IV and V. Participants in groups I, II, III and IV contribute five percent and the University contributes 10% of the participant's eligible compensation to the retirement plan. Participants in group V contribute one percent and the University contributes two percent of the participant's eligible compensation to the retirement plan.

The University has authorized two retirement plan carriers, as follows:

- Teachers Insurance and Annuity Association (TIAA)
- Fidelity Investments Institutional Services Company

Under the fully funded University of Kentucky Retirement Plan, the University and plan participants make contributions to provide retirement benefits to employees in individually owned contracts. All payments are vested immediately for employees hired prior to January 1, 2010. For employees hired after January 1, 2010, employer contributions are vested after three years. The University's contributions and costs for 2016 and 2015 were approximately \$107.1 million and \$97.7 million, respectively. Employees contributed approximately \$53.3 million in 2016 and \$48.6 million in 2015. The University's total payroll costs were approximately \$1.37 billion and \$1.26 billion for the years ended June 30, 2016 and 2015, respectively. The payroll for employees covered by the retirement plan was approximately \$1.07 billion and \$975.0 million for the years ended 2016 and 2015, respectively.

Regular full-time KMSF employees become eligible to participate in a defined contribution plan on the first of the month following the employee's regular full time hire date and attainment of age 21. KMSF contributes 10% of the employee's earnings and employees do not contribute to this plan. KMSF contributions for 2016 and 2015 were approximately \$863,000 and \$695,000, respectively. The total payroll costs for employees covered by the defined contribution plan were approximately \$8.7 million and \$7.1 million for the years ended June 30, 2016 and 2015, respectively. Participants become vested in the plan according to years of service, with 100% vesting at three years or more.

In addition to retirement benefits provided from the group retirement plan, the University provides supplemental retirement income benefits to certain eligible employees in each of the retirement groups (see note 16).

## **16. MINIMUM ANNUAL RETIREMENT BENEFITS AND SUPPLEMENTAL RETIREMENT INCOME**

Employees in retirement groups I, II and III (see note 15) who were age 40 or older prior to the date of establishment of each group plan, and who were employed by the University prior to that date, qualify for the minimum annual retirement benefit provisions of the retirement plan. Benefits for these eligible employees are based upon a percentage, determined through years of service, of the participant's annual salary in the last year of employment prior to retirement. Retirement benefits as determined are funded by each individual retiree's accumulation in the group retirement plan, with the balance, if necessary, provided by the University as supplemental retirement income. No active employees were eligible for this benefit for the years ended June 30, 2016 and 2015.

The Legislature of the Commonwealth appropriates funds to the University which the University has used for payment of supplemental retirement income benefits since adoption of the group retirement plans, and is expected to continue this practice. However, the Constitution of the Commonwealth prohibits the commitment of future revenues beyond the end of the current biennium. The University does not recognize the liability for supplemental retirement income benefits during the service life of covered employees, but recognizes its costs when funds are appropriated by the Legislature and payments are made. The University intends to continue paying supplemental retirement income benefits. Supplemental retirement benefit payments were approximately \$1.3 million and \$1.4 million for the years ended June 30, 2016 and 2015, respectively.

The latest actuarial valuation was prepared as of July 1, 2015 by TIAA. The actuarial present value of accumulated supplemental retirement income benefits as determined by this valuation, utilizing an assumed rate of return of 3.2%, was approximately \$6.4 million.

## 17. HEALTH INSURANCE BENEFITS FOR RETIREES

The University administers a single-employer defined benefit healthcare plan including medical and prescription drug benefits. The plan provides lifetime healthcare insurance benefits for eligible retirees and their surviving spouses. Employees are eligible for the University retiree health benefits upon retirement after (a) completing 15 years of continuous service and (b) age plus years of service equal at least 75 years (“rule of 75”). Employees hired on or after January 1, 2006 are eligible to participate in the retiree healthcare plan on an “access only” basis upon retirement, but they must pay 100% of the cost of the selected plan. Employees hired prior to January 1, 2006 are eligible for the University subsidy based on their hire date and surviving spouses receive one-half of the health credit their spouse was entitled to if they were covered by the health plan at the time of the retiree’s death. No health credit is provided to a spouse of a living retiree. Human Resources policies and procedures define retiree health benefits and can be amended by the President of the University as delegated by the Board. Employees who were hired before August 1, 1965 are also eligible for \$5,000 of life insurance coverage upon retirement.

The retiree health plan does not issue a publicly available financial report, but it is included in this report of the University using the economic resources measurement focus and the accrual basis of accounting under which expenses, including benefits and refunds, are recorded when the liability is incurred. Employer contributions are recorded in the accounting period in which they are earned and become measureable. Investments are reported at fair market value and based on published prices and quotations from major investment brokers at current exchange rates, as available.

The contribution requirements of plan members and the University are established and may be amended by the President of the University. For employees hired before January 1, 2006, the University provides a pre-65 credit of up to 90% of the “true retiree” cost of the least expensive pre-65 medical plan. For post-65 benefits, the University provides a credit equal to 90% of the “true retiree” cost of the post-65 medical plan. For fiscal year 2016, the University contributed \$24.8 million to the plan. Plan members receiving benefits contributed 31.5% of the premium costs, an average for combined single and family coverage. In fiscal year 2016, total member contributions were approximately \$5.2 million.

The University has established a trust fund to segregate plan assets, and currently plans to contribute amounts to the trust fund sufficient to fully fund the annual required contribution (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The University plans to continue to finance retiree benefits by pre-funding benefits and contributing the ARC into a segregated, protected trust fund and will amortize the initial unfunded actuarial accrued liability (UAAL) over a 30 year closed period. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The current ARC of \$23.7 million is 4.8% of annual covered payroll. There are no long-term contracts for contributions to the plan.

The following table presents the other postemployment benefits (OPEB) cost for the year, the amount contributed and changes in the OPEB Plan for fiscal year 2016 (in thousands):

Annual required contribution	\$ 23,741
Contributions made	(24,373)
Change in net OPEB obligation/(asset)	(632)
Net OPEB obligation/(asset) - beginning of year	(387)
Net OPEB obligation/(asset) - end of year	<u>\$ (1,019)</u>

The University's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for fiscal year 2016, 2015 and 2014, are as follows (in thousands):

Fiscal Year Ended	Annual OPEB cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation/(Asset)
6/30/2014	\$19,801	100.0%	(\$239)
6/30/2015	\$20,395	100.7%	(\$387)
6/30/2016	\$23,741	102.7%	(\$1,019)

As of July 1, 2016, the actuarial accrued liability (AAL) for benefits was \$349.5 million, with an actuarial value of assets of \$120.0 million, resulting in an UAAL of \$229.5 million. The covered payroll (annual payroll of active employees covered by the plan) was \$489.9 million and the ratio of the UAAL to the covered payroll was 46.8% at June 30, 2016. The University implemented the University of Kentucky OPEB Trust in July 2007, after the July 1, 2007 actuarial valuation date. As of June 30, 2016, net trust fund assets totaled \$120.0 million.

Actuarial valuation of an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of events far into the future. Examples include assumptions about future employment, mortality and the healthcare cost trend. Actuarially determined amounts are subject to continual revisions as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, is designed to present multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

The projection of benefits for financial reporting purposes is based on the substantive plan (the plan as understood by the employer and the plan members) and includes the type of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects for legal or contractual funding limitations on the pattern of cost sharing between the employer and plan member in the future. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the July 1, 2015 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 7.5% discount rate based on the University's ARC funding policy based on the expected long-term return on the separate trust assets that will be used to finance the payment of plan benefits. The projected annual healthcare trend rate is initially 7.1% for the pre-65 members, five percent for post-65 medical benefits and 10.0% for post-65 prescription benefits, reduced in decrements to an ultimate rate of 2.2% for pre-65 members after nine years, five percent for post-65 medical benefits immediately and five percent for post-65 prescription benefits after 13 years. The post-65 medical benefits annual healthcare trend is reduced to -2.1% in 2047 as the University will adjust their benefits each year to remain below the excise tax limit. The expected long-term payroll growth rate was assumed to be three percent per year. The initial UAAL is being amortized as a level percent of pay amount on a closed basis. The remaining amortization period at July 1, 2015 was 22 years.

## 18. LONG-TERM DISABILITY BENEFIT PLAN

The University is self-funded for a long-term disability income program and has established a trust for the purpose of paying claims and establishing necessary reserves. Regular employees with a full-time equivalent of 0.75 or greater who have completed 12 months of service are automatically enrolled in the plan. To be covered, an employee must be actively at work on the first day of the month after the employee completes one full year of service. An employee approved for long-term disability receives benefits based on the employee's basic regular monthly salary at the time of the onset of the disabling condition. Primary income benefits provide payment of 60% of the basic regular monthly salary less any disability received from government programs and/or another employer for the same condition. Basic salary for medical faculty is defined as the tenure base salary. Other sources of income used in the benefit formula include Social Security, worker's

compensation or other similar government programs, veterans' or other governmental disability payments, or other employer-sponsored disability benefits.

Employees approved for long-term disability receive 100% of their basic salary for the first six months and 60% thereafter. Benefits end when plan members recover, die, terminate employment or retire. In most cases, claimants retire at age 65. The plan also includes provisions for health insurance that allow participants who were enrolled in a health plan at the time their disability benefit began to continue health coverage (University subsidy limited to 29 months for claimants approved on or after October 1, 2006), life insurance benefit (\$10,000 before July 1, 2007 or one times salary on or after July 1, 2007) and retirement contributions equal to 10% of pre-disability salary per year for applications filed on or after October 1, 2006 and 15% of pre-disability salary per year for applications filed before October 1, 2006.

The long-term disability plan does not issue a publicly available financial report, but is included in this report of the University using the economic resources measurement focus and the accrual basis of accounting under which expenses, including benefits and refunds, are recorded when the liability is incurred. Employer contributions are recorded in the accounting period in which they are earned and become measurable. Investments are reported at fair market value and based on published prices and quotations from major investment brokers at current exchange rates, as available. The coverage of the long-term disability benefits is established and may be amended by the President of the University.

The University currently plans to contribute amounts to the trust fund sufficient to fully fund the ARC, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The University plans to continue to finance long-term disabilities by pre-funding benefits and contributing to the ARC into a segregated, protected trust fund and will amortize the initial UAAL over a 30 year closed period. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The current ARC of \$1.9 million is 0.2% of annual covered payroll. There are no long-term contracts for contributions to the plan.

The following table presents the OPEB cost for the year, the amount contributed and changes in the OPEB plan for fiscal year 2016 (in thousands):

Annual required contribution	\$ 1,926
Contributions made	(1,929)
Change in net OPEB obligation/(asset)	(3)
Net OPEB obligation/(asset) - beginning of year	2
Net OPEB obligation/(asset) - end of year	<u>\$ (1)</u>

The University's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for fiscal year 2016, 2015 and 2014 are as follows (in thousands):

Fiscal Year Ended	Annual OPEB cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation/(Asset)
6/30/2014	\$2,139	100.5%	(\$4)
6/30/2015	\$2,203	99.7%	\$2
6/30/2016	\$1,926	100.2%	(\$1)

As of July 1, 2016, the AAL for benefits was \$23.5 million and the actuarial value of assets was \$16.6 million, resulting in an UAAL of \$6.9 million. The covered payroll (annual payroll of active employees covered by the plan) was \$883.7 million and the ratio of the UAAL to the covered payroll was 0.8% at June 30, 2016.

Actuarial valuation of an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of events far into the future. Major factors affecting all long-term disability benefits are the rate at which people become disabled and how quickly they are expected to recover from disability. These rates will improve or deteriorate over time, for example with the state of the economy, with technological

development and health related events. Other factors that could also impact the liability include salary inflation, changes in utilization patterns, changes to government programs and technological advances, such as new drugs or equipment. Actuarially determined amounts are subject to continual revisions as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, is designed to present multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

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

In the July 1, 2015 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 7.5% discount rate based on the University's funding policy (ARC funding) based on the expected long-term return on the separate trust assets that will be used to finance the payment of plan benefits. The projected elimination period is six months; termination (mortality and recovery from disability) and gender and age-related disability incidence rates are based on the 2012 SOA Group Long-Term Disability Table. Benefits end when members recover, die, terminate employment or retire. For long-term disabilities arising at age 64 or later, the duration of the long-term disability payments is limited to 12 months. Payments are assumed to be made until the later of (a) age 65 or (b) five years after date of disability. An employee approved for long-term disability benefits receives primary and supplemental payment benefits based on the employee's basic regular monthly salary at the time of onset of the disabling condition. Primary income benefits provide payment of 60% of the basic regular monthly salary less any disability received from government programs and/or other employers for the same condition. Basic salary for medical faculty is defined as the tenure base salary. Other sources of income used in the benefit formula include Social Security, workers' compensation or other similar government programs, veterans' or other governmental disability payments, or other employer-sponsored disability benefits.

Claimants that file applications and who are approved for benefits on October 1, 2006 or after will have benefits based on the following schedule:

Months	Percentage of Salary
1-6	100%
7-End of Benefit	60%

The projected long-term income benefit is based on actual net benefit currently being paid with social security offset. For people who have been disabled for less than 24 months and are currently not entitled to a social security offset, it was assumed that the offset will eventually be approved according to the following table:

Months Since Disability	Proportion
<12	5%
12-17	40%
18-23	40%
24+	80%

The future salary increase for active members was assumed to be three percent per year. The initial UAAL is being amortized as a level percent of pay amount on a closed basis. The remaining amortization period at July 1, 2015 was 22 years.

## **19. RISK MANAGEMENT**

The University is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by (1) the State Fire and Tornado Insurance Fund (the insurance fund), (2) Sovereign Immunity and the State Board of Claims, or (3) in the case of risks not covered by the insurance fund and Sovereign Immunity, commercial insurance, participation in insurance risk retention groups or self-insurance.

The insurance fund covers losses to property from fire, wind, earthquake, flood and most other causes of loss between \$1,000 and \$1.0 million per occurrence. Losses in excess of \$1.0 million are insured by commercial carriers up to \$1.25 billion per occurrence with buildings and contents insured at replacement cost. As a state agency, the University is vested with Sovereign Immunity and is subject to the provisions of the Board of Claims Act, under which the University's liability for certain negligence claims is limited to \$200,000 for any one person or \$350,000 for all persons damaged by a single act of negligence. Claims against educators' errors and omissions and wrongful acts are insured through a reciprocal risk retention group. There have been no significant reductions in insurance coverage from 2015 to 2016. Settlements have not exceeded insurance coverage during the past three years.

The University and its agents are insured against medical malpractice by a combination of Sovereign Immunity, self-insurance, commercial liability insurance and an excess coverage fund established by the Commonwealth. An actuarial valuation is performed to determine the self-insurance funding requirements and the fund liability, which has been discounted using an interest rate of 3.5%. The malpractice liability as of June 30, 2016 is based on the requirements of GASB Statement No. 10, which requires that a liability for claims be recorded if it is probable that a loss has occurred and the amount of loss can be reasonably estimated. The liability includes an estimate for claims that have been incurred but not reported as of June 30, 2016.

The University also self-insures certain employee benefits, including health insurance, worker's compensation and unemployment claims to the extent not covered by insurance. The University has recorded an estimate for asserted claims at June 30, 2016.

## **20. CONTINGENCIES**

The University is a defendant in various lawsuits. The nature of the educational and health care industries is such that, from time to time, claims will be presented on account of alleged negligence, acts of discrimination, medical malpractice, breach of contract or disagreements arising from the interpretation of laws or regulations. While some of these claims may be for substantial amounts, they are not unusual in the ordinary course of providing educational and health care services at a large institution. However, University officials are of the opinion, based on advice of in-house legal counsel, that the effect of the ultimate outcome of all litigation will not be material to the future operations or financial position of the University.

## **21. RESEARCH CHALLENGE TRUST FUND**

The Research Challenge Trust Fund (RCTF) was created by the Kentucky General Assembly with the passage of the Postsecondary Education Improvement Act of 1997 (House Bill 1). The objectives of the RCTF, as stated in House Bill 1, include support of efforts by the University to attain status as a top-20 public research university. The RCTF Endowment Match Program provides state funds on a dollar-for-dollar match basis. This program, also known as "Bucks for Brains," supports endowed chairs, professorships and graduate fellowships, and the research and graduate mission of the University.

With the passage of the 2008-10 budget of the Commonwealth, the 2008 General Assembly authorized \$50.0 million in General Fund supported bonds in 2008-09 for the RCTF to support the Endowment Match Program and a newly created Research Capital Match Program. In accordance with KRS 164.7917, these funds were allocated two-thirds to the University of Kentucky (\$33.3 million) and one-third to the University of Louisville (\$16.7 million). At its June 9, 2009 board meeting, the Board approved the allocation of the University's RCTF appropriation as follows: \$21.9 million to the Research Capital Match Program and \$11.4 million to the Endowment Match Program.

The status of the RCTF endowed funds as of June 30, 2016, is summarized below (in thousands):

	Kentucky General Assembly Funding	University of Kentucky Share of Funding	State Funds Received to Date
1998 Biennium	\$ 100,000	\$ 66,667	\$ 66,667
2000 Biennium	100,000	68,857	68,857
2002 Biennium	100,000	66,667	66,667
2008 Biennium: Capital Projects	21,927	21,927	21,927
2008 Biennium: RCTF	28,073	11,406	11,406
Total	<u>\$ 350,000</u>	<u>\$ 235,524</u>	<u>\$ 235,524</u>

Interest income of approximately \$2.2 million was earned on the state matching funds and included in the University's share of the 2000 biennium funding. As of June 30, 2016, all private gifts and pledges matched by the RCTF program have been received.

## 22. CANCER RESEARCH MATCHING FUND

The Kentucky General Assembly created the Cancer Research Institutions Matching Fund, which is funded by a one-cent surtax levied on every 20 cigarettes sold in Kentucky. Tax revenues are made available equally to the University of Kentucky and the University of Louisville when matched dollar-for-dollar by private sources.

A summary of the receipts and expenses related to the fund as of June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Funds from private sources approved for match	\$ 7,761	\$ 7,749
Cigarette excise tax funds distributed	1,925	1,953
Total cancer research matching fund revenues	<u>\$ 9,686</u>	<u>\$ 9,702</u>
Cancer research matching fund expenses	<u>\$ 7,524</u>	<u>\$ 7,763</u>

## 23. NATURAL CLASSIFICATION

The University's operating expenses by natural classification for the years ended June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Salaries and wages	\$ 1,382,346	\$ 1,265,729
Employee benefits	365,932	343,916
Supplies and services	740,199	621,350
Depreciation	148,109	134,374
Student scholarships and financial aid	60,477	54,676
Purchased utilities	49,421	50,970
Other, various	141,555	138,238
Total	<u>\$ 2,888,039</u>	<u>\$ 2,609,253</u>

## 24. COMBINED CONDENSED STATEMENTS

The University of Kentucky and its blended component units' condensed statements for the years ended June 30, 2016 and 2015 were summarized as follows (in thousands):

UNIVERSITY OF KENTUCKY  
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COMBINED CONDENSED STATEMENT OF NET POSITION AS OF JUNE 30, 2016  
(in thousands)

	UK	Research Foundation		The Fund	Gluck Equine Research Foundation		Humanities Foundation	Mining Engineering Foundation	Center on Aging	Central Kentucky Management Services	Kentucky Medical Services Foundation	Eliminations	Total
		\$			\$								
<b>ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>													
<b>Current Assets</b>													
Cash and cash equivalents	\$ 627,555	\$ 54,566	\$ 9,260	\$ 338	\$ 86	\$ 26	\$ 167	\$ 1,493	\$ 252	\$ -	\$ 693,743		
Notes, loans and accounts receivable, net	265,830	30,796	3,580	-	-	-	-	428	48,177	(51,191)	297,620		
Investments	-	-	-	-	-	-	-	-	16,977	-	16,977		
Inventories and other assets	46,267	3,889	90	-	-	-	-	18	370	(174)	50,460		
Total current assets	939,652	89,251	12,930	338	86	26	167	1,939	65,776	(51,365)	1,058,800		
<b>Noncurrent Assets</b>													
Restricted cash and cash equivalents	398,569	-	-	-	-	-	-	-	-	-	398,569		
Endowment investments	1,197,209	12,817	153	8,286	1,282	1,832	-	-	-	-	1,221,579		
Other long-term investments	250,753	886	-	-	-	-	-	-	48,029	(251)	299,417		
Notes, loans and accounts receivable, net	326,518	35	-	-	-	-	-	-	813	-	327,366		
Other noncurrent assets	441	-	451	-	-	-	-	-	-	(451)	441		
Capital assets, net	2,618,461	9,035	-	-	-	-	-	87	82,055	-	2,709,638		
Total noncurrent assets	4,791,951	22,773	604	8,286	1,282	1,832	-	87	130,897	(702)	4,957,010		
Total assets	5,731,603	112,024	13,534	8,624	1,368	1,858	167	2,026	196,673	(52,067)	6,015,810		
Total assets and deferred outflows of resources	5,743,767	112,024	13,534	8,624	1,368	1,858	167	2,026	196,673	(52,067)	6,027,974		
<b>LIABILITIES AND DEFERRED INFLOWS OF RESOURCES</b>													
<b>Current Liabilities</b>													
Accounts payable and accrued liabilities	313,361	10,436	1,879	-	-	8	-	1,939	111,763	(112,569)	326,817		
Unearned revenue	44,531	32,784	111	-	-	-	-	-	2,847	(625)	79,648		
Long-term liabilities - current portion	80,147	-	-	-	-	-	-	-	21,922	-	102,069		
Total current liabilities	438,039	43,220	1,990	-	-	8	-	1,939	136,532	(113,194)	508,534		
<b>Noncurrent Liabilities</b>													
Unearned revenue	179,853	-	-	-	-	-	-	-	-	-	179,853		
Long-term liabilities	1,221,865	404	-	-	-	-	-	-	24,045	-	1,246,314		
Total noncurrent liabilities	1,401,718	404	-	-	-	-	-	-	24,045	-	1,426,167		
Total liabilities	1,839,757	43,624	1,990	-	-	8	-	1,939	160,577	(113,194)	1,934,701		
Total liabilities and deferred inflows of resources	2,206,503	43,624	1,990	-	-	8	-	1,939	160,577	(113,194)	2,301,447		
<b>NET POSITION</b>													
<b>Net investment in capital assets</b>	1,481,816	9,035	-	-	-	-	-	87	36,096	-	1,527,034		
<b>Restricted</b>													
Nonexpendable	594,954	832	31	4,607	618	661	-	-	-	-	601,703		
Expendable	483,596	3,983	452	4,017	750	1,189	167	-	-	-	484,154		
Total restricted	1,078,550	4,815	483	8,624	1,368	1,850	167	-	-	-	1,085,857		
<b>Unrestricted</b>	976,898	54,550	11,061	-	-	-	-	-	-	61,127	1,103,636		
Total net position	3,537,264	68,400	11,544	8,624	1,368	1,850	167	87	36,096	61,127	3,726,527		



UNIVERSITY OF KENTUCKY  
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COMBINED CONDENSED STATEMENT OF NET POSITION AS OF JUNE 30, 2015  
(in thousands)

	UK	Research Foundation	The Fund	Gluck Equine Research Foundation	Humanities Foundation	Mining Engineering Foundation	Center on Aging	Central Kentucky Management Services	Kentucky Medical Services Foundation	Eliminations	Total
<b>ASSETS AND DEFERRED OUTFLOWS OF RESOURCES</b>											
<b>Current Assets</b>											
Cash and cash equivalents	\$ 560,450	\$ 49,592	\$ 10,308	\$ 247	\$ 63	\$ 21	\$ 170	\$ 549	\$ 561	\$ -	\$ 621,961
Notes, loans and accounts receivable, net	265,519	32,559	2,597	-	-	-	-	1,035	41,333	(50,267)	292,776
Investments	-	-	-	-	-	-	-	-	21,702	-	21,702
Inventories and other assets	44,609	2,129	1	-	-	-	-	18	57	-	46,814
Total current assets	870,578	84,280	12,906	247	63	21	170	1,602	63,653	(50,267)	983,253
<b>Noncurrent Assets</b>											
Restricted cash and cash equivalents	315,522	-	-	-	-	-	-	-	-	-	315,522
Endowment investments	1,214,848	4,296	165	8,941	1,383	1,924	-	-	-	-	1,231,557
Other long-term investments	219,257	1,080	-	-	-	-	-	-	54,927	(263)	275,001
Notes, loans and accounts receivable, net	338,149	2	-	-	-	-	-	-	802	-	338,953
Other noncurrent assets	283	-	-	-	-	-	-	-	-	-	283
Capital assets, net	2,251,254	9,504	-	-	-	-	-	137	75,745	-	2,336,640
Total noncurrent assets	4,339,313	14,882	165	8,941	1,383	1,924	-	137	131,474	(263)	4,497,956
Total assets	5,209,891	99,162	13,071	9,188	1,446	1,945	170	1,739	195,127	(50,530)	5,481,209
Deferred Outflows of Resources	13,755	-	-	-	-	-	-	-	-	-	13,755
Total assets and deferred outflows of resources	5,223,646	99,162	13,071	9,188	1,446	1,945	170	1,739	195,127	(50,530)	5,494,964
<b>LIABILITIES AND DEFERRED INFLOWS OF RESOURCES</b>											
<b>Current Liabilities</b>											
Accounts payable and accrued liabilities	299,974	10,489	661	1	-	11	5	1,602	119,325	(120,760)	311,308
Unearned revenue	49,905	29,783	88	-	-	-	-	-	-	-	79,776
Long-term liabilities - current portion	78,337	-	-	-	-	-	-	-	3,066	-	81,403
Total current liabilities	428,216	40,272	749	1	-	11	5	1,602	122,391	(120,760)	472,487
<b>Noncurrent Liabilities</b>											
Unearned revenue	193,094	-	-	-	-	-	-	-	-	-	193,094
Long-term liabilities	1,091,295	480	-	-	-	-	-	-	39,226	-	1,131,001
Total noncurrent liabilities	1,284,389	480	-	-	-	-	-	-	39,226	-	1,324,095
Total liabilities	1,712,605	40,752	749	1	-	11	5	1,602	161,617	(120,760)	1,796,582
Deferred Inflows of Resources	241,124	-	-	-	-	-	-	-	-	-	241,124
Total liabilities and deferred inflows of resources	1,953,729	40,752	749	1	-	11	5	1,602	161,617	(120,760)	2,037,706
<b>INTERFUND BALANCES</b>											
	(934)	-	934	-	-	-	-	-	-	-	-
<b>NET POSITION</b>											
<b>Net investment in capital assets</b>	1,379,409	9,504	-	-	-	-	-	137	33,510	-	1,422,560
<b>Restricted</b>											
Nonexpendable	578,336	823	31	4,607	618	659	-	-	-	-	585,074
Expendable	440,113	4,395	634	4,580	828	1,275	165	-	-	-	451,990
Total restricted	1,018,449	5,218	665	9,187	1,446	1,934	165	-	-	-	1,037,064
<b>Unrestricted</b>											
	872,993	43,688	10,723	-	-	-	-	-	-	70,230	997,634
Total net position	\$ 3,270,851	\$ 58,410	\$ 11,388	\$ 9,187	\$ 1,446	\$ 1,934	\$ 165	\$ 137	\$ 33,510	\$ 70,230	\$ 3,457,258

UNIVERSITY OF KENTUCKY  
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY  
COMBINED CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION FOR THE YEAR ENDED JUNE 30, 2016  
(in thousands)

	UK	Research Foundation	The Fund	Gluck Equine Research Foundation	Humanities Foundation	Mining Engineering Foundation	Center on Aging	Central Kentucky Management Services	Kentucky Medical Services Foundation	Eliminations	Total
<b>OPERATING REVENUES</b>	\$ 319,627	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 319,627
Student tuition and fees, net	1,459	167,832	-	-	-	-	-	-	-	-	169,291
Federal grants and contracts	72,868	16,459	1,889	-	-	-	-	-	-	-	91,216
State and local grants and contracts	236,266	33,803	10,603	-	-	-	-	-	(245,693)	-	34,979
Nongovernmental grants and contracts	200	50,888	-	-	-	-	-	-	-	-	51,088
Recoveries of facilities and administrative costs	30,374	3,160	16,092	-	-	-	31	31,404	-	(32,238)	48,823
Sales and services	19,266	-	-	-	-	-	-	-	-	-	19,266
Federal appropriations	23,717	-	-	-	-	-	-	233,590	-	(4,515)	229,075
County appropriations	-	-	-	-	-	-	-	-	-	(6,049)	23,717
Professional clinical service fees	1,423,292	-	-	-	-	-	-	-	-	(300)	1,417,243
Hospital services	39,403	-	-	-	-	-	-	-	-	-	39,403
Auxiliary enterprises:	102,995	-	-	-	-	-	-	-	-	-	102,995
Housing and dining, net	49,434	-	-	-	-	-	-	-	-	-	49,434
Athletics	838	-	-	-	-	-	-	-	-	(77,157)	7,931
Other auxiliaries	-	-	-	-	-	-	-	-	-	(365,952)	2,603,788
Other operating revenues	2,319,739	272,142	28,584	-	-	-	31	31,404	317,840	-	2,603,788
Total operating revenues	2,908,900	9,482	1,161	38	5	53	-	-	-	(128)	3,014,663
<b>OPERATING EXPENSES</b>	90,376	166,756	1,415	-	-	-	-	-	-	(2,564)	256,021
Educational and general:	167,137	72,314	14,729	-	-	-	-	-	-	(69,966)	184,214
Instruction	21,807	-	393	-	-	-	-	-	-	(2)	22,198
Research	66,571	1,803	6,229	-	-	-	-	-	-	(3)	74,600
Public service	43,463	5	1,168	-	3	-	-	-	-	(69)	44,570
Libraries	57,704	857	144	-	-	-	134	31,399	-	(31,595)	58,643
Academic support	90,730	11	438	-	-	-	-	-	-	(7,759)	83,420
Student services	34,055	1,494	1,201	-	47	-	-	-	-	(2)	36,795
Institutional support	64,675	486	-	-	-	-	-	27	-	-	65,188
Operations and maintenance of plant	927,408	253,208	26,878	38	55	53	134	31,426	-	(112,088)	1,127,112
Student financial aid	209,028	-	-	-	-	-	-	-	314,412	(240,066)	283,374
Depreciation	1,303,623	-	60	-	-	-	-	-	-	(3,086)	1,300,597
Total educational and general	2,216,952	253,208	26,938	38	55	53	134	31,426	-	(355,177)	2,888,039
Net income (loss) from operations	(297,213)	18,934	1,646	(38)	(55)	(53)	(103)	(22)	3,428	(10,775)	(284,251)
Nonoperating revenues (expenses)	279,611	-	-	-	-	-	-	-	-	-	279,611
State appropriations	128,401	245	207	12	2	-	125	-	-	(1,196)	127,796
Gifts and non-exchange grants	(2,228)	135	23	(119)	(18)	(25)	1	-	162	(596)	(2,665)
Investment income (loss)	(27,442)	-	-	-	-	-	-	-	(1,002)	-	(28,444)
Interest on capital asset-related debt	14,330	(13,245)	(651)	(418)	(7)	(9)	-	-	-	-	-
Grant to/(from) the University for non-capital purposes	4,185	8,366	-	-	-	-	-	-	-	-	12,551
Other nonoperating revenues and expenses, net	396,957	(4,499)	(421)	(525)	(23)	(34)	126	-	(840)	4,102	16,653
Net nonoperating revenues (expenses)	99,644	14,435	1,225	(563)	(78)	(87)	23	(22)	2,588	(8,465)	108,700
Net income (loss) before other revenues, expenses, gains, or losses	161,859	4,675	-	-	-	-	-	-	-	(638)	165,896
Capital grants and gifts	13,041	8	-	-	-	3	-	-	-	-	13,052
Additions to permanent endowments	10,197	(9,107)	(1,069)	-	-	-	(21)	-	-	-	-
Grant to/(from) the University for capital purposes	(18,328)	(21)	(1,069)	-	-	3	(21)	(28)	(2)	(638)	(18,379)
Other, net	166,769	(4,445)	156	(563)	(78)	(84)	2	(50)	2,586	(9,103)	269,269
Total other revenues (expenses)	3,270,851	58,410	11,388	9,187	1,446	1,934	165	137	33,510	70,230	3,457,258
<b>INCREASE (DECREASE) IN NET POSITION</b>	\$ 3,537,264	\$ 68,400	\$ 11,544	\$ 8,624	\$ 1,368	\$ 1,850	\$ 167	\$ 87	\$ 36,096	\$ 61,127	\$ 3,726,527
<b>NET POSITION, beginning of year</b>											
<b>NET POSITION, end of year</b>											

**UNIVERSITY OF KENTUCKY  
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY  
COMBINED CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION FOR THE YEAR ENDED JUNE 30, 2015**  
(in thousands)

	UK	Research Foundation	The Fund	Gluck Equine Research Foundation	Humanities Foundation	Mining Engineering Foundation	Center on Aging Services	Central Kentucky Management Services	Kentucky Medical Services Foundation	Eliminations	Total
<b>OPERATING REVENUES</b>											
Student tuition and fees, net	\$ 302,936	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 302,936
Federal grants and contracts	1,552	166,573	-	-	-	-	-	-	-	-	168,125
State and local grants and contracts	73,425	16,890	1,954	-	-	-	-	-	-	-	92,269
Nongovernmental grants and contracts	201,138	28,851	6,311	-	-	-	-	-	-	(206,495)	29,805
Recoveries of facilities and administrative costs	271	47,883	-	-	-	-	-	-	-	-	48,154
Sales and services	25,479	15,273	14,210	1	-	-	29	26,708	-	(27,588)	54,112
Federal appropriations	17,535	-	-	-	-	-	-	-	-	-	17,535
County appropriations	21,975	-	-	-	-	-	-	-	-	(3,906)	21,975
Professional clinical service fees	-	-	-	-	-	-	-	-	227,197	(4,978)	223,291
Hospital services	-	-	-	-	-	-	-	-	-	-	-
Auxiliary enterprises:	1,328,630	-	-	-	-	-	-	-	-	-	1,323,652
Housing and dining, net	39,921	-	-	-	-	-	-	-	-	(656)	39,265
Athletics	88,928	-	-	-	-	-	-	-	-	-	88,928
Other auxiliaries	47,040	-	-	-	-	-	-	-	-	(1)	47,039
Other operating revenues	853	-	-	-	-	-	-	-	79,185	(74,979)	5,059
Total operating revenues	2,149,683	275,470	22,475	1	-	-	29	26,708	306,382	(318,603)	2,462,145
<b>OPERATING EXPENSES</b>											
Educational and general:											
Instruction	274,970	10,555	1,028	-	1	59	-	-	-	(236)	286,377
Research	84,883	160,755	180	42	-	-	-	-	-	(2,349)	243,511
Public service	174,908	75,675	3,550	-	-	-	-	-	-	(72,596)	181,537
Libraries	21,085	-	-	-	-	-	-	-	-	(1)	21,084
Academic support	67,472	1,825	3,812	-	-	-	-	-	-	(31)	73,078
Student services	37,748	-	1,038	-	1	-	-	-	-	(139)	38,648
Institutional support	55,013	569	125	6	-	-	102	26,695	-	(26,887)	55,623
Operations and maintenance of plant	70,904	1	391	-	-	-	-	-	-	(192)	71,104
Student financial aid	30,261	1,328	1,266	-	40	-	-	-	-	(1)	32,894
Depreciation	64,125	1,380	-	-	-	-	-	43	-	-	65,548
Total educational and general	881,369	252,088	11,390	48	42	59	102	26,738	-	(102,432)	1,069,404
Clinical operations (including depreciation of \$2,743)	179,675	-	-	-	-	-	-	-	289,627	(222,871)	246,431
Hospital and clinics (including depreciation of \$53,167)	1,141,835	-	60	-	-	-	-	-	-	(7,772)	1,134,123
Auxiliary enterprises:											
Housing and dining (including depreciation of \$5,279)	30,970	-	-	-	-	-	-	-	-	(9)	30,961
Athletics (including depreciation of \$6,031)	102,156	-	-	-	-	-	-	-	-	(460)	101,696
Other auxiliaries (including depreciation of \$1,606)	26,500	-	-	-	-	-	-	-	-	(502)	25,998
Other operating expenses	640	-	-	-	-	-	-	-	-	-	640
Total operating expenses	2,363,145	252,088	11,450	48	42	59	102	26,738	289,627	(334,046)	2,609,253
Net income (loss) from operations	(213,462)	23,382	11,025	(47)	(42)	(59)	(73)	(30)	16,755	15,443	(147,108)
<b>NONOPERATING REVENUES (EXPENSES)</b>											
State appropriations	279,611	-	-	-	-	-	-	-	-	-	279,611
Gifts and non-exchange grants	105,557	461	190	118	1	-	129	-	-	(950)	105,506
Investment income (loss)	27,338	18,047	9	175	27	39	-	1	102	(550)	45,188
Interest on capital asset-related debt	(26,710)	(49)	-	-	-	-	-	-	(932)	-	(27,691)
Grant to/(from) the University for non-capital purposes	36,167	(26,431)	(9,433)	(295)	(3)	(5)	-	-	-	-	-
Other nonoperating revenues and expenses, net	7,145	1,843	-	-	-	-	-	-	-	-	-
Net nonoperating revenues (expenses)	429,108	(6,129)	(9,234)	(2)	25	34	129	1	(830)	(1,500)	8,988
Net income (loss) before other revenues, expenses, gains, or losses	215,646	17,253	1,791	(49)	(17)	(25)	56	(29)	15,925	13,943	264,494
Capital grants and gifts	38,999	6,424	-	-	-	-	-	-	-	(82)	45,341
Additions to permanent endowments	7,752	1	-	-	-	5	-	-	-	-	7,758
Grant to/(from) the University for capital purposes	11,088	(11,176)	88	-	-	-	-	-	-	-	-
Other, net	(2,516)	(1,524)	-	-	-	-	-	(36)	(111)	-	(4,187)
Total other revenues (expenses)	55,323	(6,275)	88	-	-	5	-	(36)	(111)	(82)	48,912
INCREASE (DECREASE) IN NET POSITION	270,969	10,978	1,879	(49)	(17)	(20)	56	(65)	15,814	13,861	313,406
NET POSITION, beginning of year	2,999,882	47,432	9,509	9,236	1,463	1,954	109	202	17,696	56,369	3,143,852
NET POSITION, end of year	\$ 3,270,851	\$ 58,410	\$ 11,388	\$ 9,187	\$ 1,446	\$ 1,934	\$ 165	\$ 137	\$ 33,510	\$ 70,230	\$ 3,457,258

**UNIVERSITY OF KENTUCKY  
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY  
COMBINED CONDENSED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2016  
(in thousands)**

	UK	Research Foundation	The Fund	Gluck Equine Research Foundation	Humanities Foundation	Mining Engineering Foundation	Center on Aging	Central Kentucky Management Services	Kentucky Medical Services Foundation	Eliminations	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>											
Student tuition and fees	\$ 320,092	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 320,092
Grants and contracts	311,689	221,584	11,637	-	-	-	-	-	-	(245,693)	299,217
Recoveries of facilities and administrative costs	215	52,098	-	-	-	-	-	-	-	-	52,313
Sales and services	29,613	3,185	16,964	-	-	-	31	31,391	2,847	(32,863)	51,168
Federal appropriations	18,630	-	-	-	-	-	-	-	-	-	18,630
County appropriations	-	-	-	-	-	-	-	-	-	-	22,869
Payments to vendors and contractors	(879,967)	(91,828)	(12,746)	(10)	(55)	(17)	(138)	(1,482)	(301,716)	363,993	(923,966)
Student financial aid	(35,593)	-	(1,201)	-	-	-	-	-	-	-	(36,794)
Salaries, wages and benefits	(1,540,753)	(161,136)	(13,290)	(30)	-	(39)	-	(28,959)	(11,667)	-	(1,755,876)
Professional clinic service fees	-	-	-	-	-	-	-	-	-	(2,990)	223,744
Hospital services	1,424,078	-	-	-	-	-	-	-	226,734	(6,648)	1,417,430
Auxiliary enterprise receipts	208,725	-	-	-	-	-	-	-	-	(300)	208,425
Loans issued to students	(5,915)	-	-	-	-	-	-	-	-	-	(5,915)
Collection of loans to students	7,529	-	-	-	-	-	-	-	-	-	7,529
Self insurance receipts	67,791	-	-	-	-	-	-	-	(516)	-	67,275
Self insurance payments	(64,860)	-	-	-	-	-	-	-	-	-	(64,860)
Other operating receipts (payments), net	1,225	-	-	-	-	-	-	-	84,203	(77,159)	8,269
Net cash provided (used) by operating activities	(114,632)	23,901	1,364	(40)	(55)	(66)	(107)	950	(115)	(1,660)	(90,450)
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>											
State appropriations	274,019	-	-	-	-	-	-	-	-	-	274,019
Gifts and grants received for other than capital purposes:											
Gifts received for endowment purposes	13,041	8	-	-	-	3	-	-	-	-	13,052
Agency and loan program receipts	114,542	263	207	13	2	-	125	-	-	(1,196)	113,956
Agency and loan program payments	(229,244)	-	-	-	-	-	-	-	-	-	(229,244)
Grants (to) from the University for non-capital purposes	18,622	(13,245)	(1,585)	(418)	(6)	(9)	-	-	-	-	-
Other noncapital financing receipts (payments), net	438,916	(6,150)	(1,378)	(405)	(4)	(6)	125	-	-	4,102	29,548
Net cash provided (used) by noncapital financing activities	160,117	4,675	-	-	-	-	-	-	-	2,906	434,004
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>											
Capital grants and gifts	(408,788)	(81)	-	-	-	-	-	(6)	(7,957)	(638)	164,154
Purchases of capital assets	159,541	-	-	-	-	-	-	-	-	-	(416,832)
Proceeds from capital debt	(46,732)	-	-	-	-	-	-	-	(3,021)	-	159,541
Principal paid on capital debt and leases	(37,780)	-	-	-	-	-	-	-	(1,002)	-	(49,753)
Interest paid on capital debt and leases	10,197	(9,107)	(1,069)	-	-	-	(21)	-	-	-	(38,782)
Grants (to) from the University for capital purposes	5,562	(21)	-	-	-	-	-	-	-	-	-
Other capital and related financing receipts (payments), net	(157,883)	(4,534)	(1,069)	-	-	-	(21)	(6)	(11,980)	(638)	5,541
Net cash provided (used) by capital and related financing activities	627,051	4,311	53	2,847	440	578	(21)	(6)	14,448	(638)	(176,131)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>											
Proceeds from sales and maturities of investments	24,873	58	27	99	15	22	-	-	1,531	(608)	649,728
Interest and dividends on investments	(668,173)	(12,612)	(45)	(2,410)	(373)	(533)	-	-	(4,193)	-	26,017
Purchase of investments	(16,249)	(8,243)	35	536	82	67	-	-	11,786	(608)	(688,339)
Net cash provided (used) by investing activities	150,152	4,974	(1,048)	91	23	5	(3)	944	(309)	-	(12,594)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>											
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	875,972	49,592	10,308	247	63	21	170	549	561	-	937,483
<b>CASH AND CASH EQUIVALENTS, end of year</b>	\$ 1,026,124	\$ 54,566	\$ 9,260	\$ 338	\$ 86	\$ 26	\$ 167	\$ 1,493	\$ 252	\$ -	\$ 1,092,312

**UNIVERSITY OF KENTUCKY  
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COMBINED CONDENSED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2015  
(in thousands)**

	UK	Research Foundation	The Fund	Gluck Equine Research Foundation	Humanities Foundation	Mining Engineering Foundation	Center on Aging	Central Kentucky Management Services	Kentucky Medical Services Foundation	Eliminations	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>											
Student tuition and fees	\$ 301,454	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 301,454
Grants and contracts	267,304	213,631	10,224	-	-	-	-	-	-	(206,495)	284,664
Recoveries of facilities and administrative costs	275	48,182	-	-	-	-	-	-	-	-	48,457
Sales and services	28,933	16,166	14,061	1	-	-	29	24,771	-	(30,496)	53,465
Federal appropriations	18,749	-	-	-	-	-	-	-	-	-	18,749
County appropriations	22,640	-	-	-	-	-	-	-	-	-	22,640
Payments to vendors and contractors	(31,630)	(86,551)	(7,730)	(18)	(42)	(22)	(95)	(1,347)	(254,657)	306,897	(827,529)
Student financial aid	(1,401,783)	(182,243)	(2,248)	(29)	-	(24)	(2)	(23,449)	(8,501)	11,131	(1,598,279)
Salaries, wages and benefits	1,342,864	-	-	-	-	-	-	-	210,597	(4,205)	1,338,659
Professional clinic service fees	172,042	-	-	-	-	-	-	-	-	(657)	171,385
Hospital services	(18,231)	-	-	-	-	-	-	-	-	-	(18,231)
Auxiliary enterprise receipts	18,425	-	-	-	-	-	-	-	470	-	18,425
Loans issued to students	60,882	-	-	-	-	-	-	-	-	-	60,882
Collection of loans to students	(56,750)	-	-	-	-	-	-	-	-	-	(56,750)
Self insurance receipts	375	-	-	-	-	-	-	-	-	-	375
Self insurance payments	(58,415)	29,185	13,041	(46)	(42)	(46)	(68)	(25)	78,648	(74,578)	4,445
Other operating receipts (payments), net									26,557	1,597	11,738
Net cash provided (used) by operating activities	279,611	-	-	-	-	-	-	-	-	-	279,611
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>											
State appropriations	7,776	1	-	-	-	5	-	-	-	-	7,782
Gifts and grants received for other than capital purposes:											
Gifts received for endowment purposes	113,296	442	190	118	-	-	129	-	-	(950)	113,225
Gifts received for other purposes	227,347	-	-	-	-	-	-	-	-	-	227,347
Agency and loan program receipts	(229,398)	-	-	-	-	-	-	-	-	-	(229,398)
Agency and loan program payments	37,602	(27,994)	(9,305)	(295)	(3)	(5)	-	-	-	-	-
Grants (to) from the University for non-capital purposes	14,438	3,727	-	-	-	-	-	-	-	-	18,165
Other noncapital financing receipts (payments), net	450,672	(23,824)	(9,115)	(177)	(3)	-	129	-	-	(950)	416,732
Net cash provided (used) by noncapital financing activities	24,632	6,424	-	-	-	-	-	(14)	(17,056)	(82)	30,974
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>											
Capital grants and gifts	(266,098)	(863)	-	-	-	-	-	-	-	-	(284,031)
Purchases of capital assets	392,077	-	-	-	-	-	-	-	-	-	392,077
Proceeds from capital debt	(248,642)	-	-	-	-	-	-	-	-	-	(248,642)
Payments to refunding bond agents	10,180	-	-	-	-	-	-	-	-	-	10,180
Proceeds from sales of capital assets	(47,024)	(194)	-	-	-	-	-	-	(2,654)	-	(49,872)
Principal paid on capital debt and leases	(33,868)	(49)	-	-	-	-	-	-	(932)	-	(34,849)
Interest paid on capital debt and leases	11,088	(11,176)	88	-	-	-	-	-	-	-	-
Grants (to) from the University for capital purposes	5,386	(1)	-	-	-	-	-	-	-	-	5,385
Other capital and related financing receipts (payments), net	(152,269)	(5,859)	88	-	-	-	-	(14)	(20,642)	(82)	(178,778)
Net cash provided (used) by capital and related financing activities	313,635	(2,946)	4	1,589	246	385	-	-	45	-	312,958
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>											
Proceeds from sales and maturities of investments, net	97	20,211	8	93	14	20	-	1	(29)	(565)	19,850
Interest and dividends on investments	(333,901)	(779)	(31)	(1,589)	(246)	(342)	-	-	(5,623)	-	(342,511)
Purchase of investments	-	23,219	-	-	-	-	-	-	-	(3,342)	19,877
Net proceeds from sale of CLI stock, net of cash acquired	(55)	12,975	(19)	93	14	63	-	1	(5,607)	(565)	6,900
Repayment of debt and other related to sale of CLI stock	239,933	12,477	3,995	(130)	(31)	17	61	(38)	308	-	256,592
Net cash provided (used) by investing activities	636,039	37,115	6,313	377	94	4	109	587	253	-	680,891
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	\$ 875,972	\$ 49,592	\$ 10,308	\$ 247	\$ 63	\$ 21	\$ 170	\$ 549	\$ 561	\$ -	\$ 937,483
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>											
<b>CASH AND CASH EQUIVALENTS, end of year</b>											

**UNIVERSITY OF KENTUCKY**  
**A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY**  
**REQUIRED SUPPLEMENTARY INFORMATION**

**1. HEALTH INSURANCE BENEFITS FOR RETIREES**

The University of Kentucky's (the University) Other Postemployment Benefit (OPEB) plan is administered through the University's OPEB trust fund as an irrevocable trust. Assets of the trust fund are dedicated to providing post-retirement health insurance coverage to current and eligible future university retirees. Only employees hired prior to January 1, 2006 are eligible to receive post-retirement health insurance benefits.

The following schedules present the University's actuarially determined funding progress and required contributions for the University's OPEB trust using the projected unit credit actuarial cost method:

Schedule of Funding Progress by Valuation Date  
(in thousands)

Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as a Percentage of Covered Payroll
July 1, 2014	\$97,317	\$268,335	\$171,018	36.3%	\$513,748	33.3%
July 1, 2015	\$108,815	\$337,665	\$228,850	32.2%	\$509,627	44.9%
July 1, 2016	\$120,012	\$349,503	\$229,491	34.3%	\$489,855	46.8%

Schedule of Employer Contributions  
(in thousands)

Year Ended	Annual Required Contributions	Percentage Contributed
June 30, 2014	\$19,801	100.0%
June 30, 2015	\$20,395	100.7%
June 30, 2016	\$23,741	102.7%

**2. LONG-TERM DISABILITY BENEFIT PLAN**

The University is self-funded for a long-term disability income program and has established a trust for the purpose of paying claims and establishing necessary reserves. Regular employees with a full-time equivalent of .75 or greater who have completed 12 months of service are automatically enrolled in the plan.

The following schedules present the University's actuarially determined funding progress and required contributions for the University's long-term disability benefit trust fund using the projected unit credit actuarial cost method:

Schedule of Funding Progress by Valuation Date  
(in thousands)

Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as a Percentage of Covered Payroll
July 1, 2014	\$15,977	\$23,650	\$7,673	67.6%	\$768,214	1.0%
July 1, 2015	\$16,576	\$22,730	\$6,154	72.9%	\$813,205	0.8%
July 1, 2016	\$16,629	\$23,457	\$6,828	70.9%	\$883,682	0.8%

Schedule of Employer Contributions  
(in thousands)

<u>Year Ended</u>	<u>Annual Required Contributions</u>	<u>Percentage Contributed</u>
June 30, 2014	\$2,139	100.5%
June 30, 2015	\$2,203	99.7%
June 30, 2016	\$1,926	100.2%

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