



2017 Financial Statements



University of Kentucky
A Component Unit of the Commonwealth of Kentucky
Financial Statements
Years Ended June 30, 2017 and 2016

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MESSAGE FROM THE PRESIDENT

In varied and dynamic ways, the University of Kentucky showcases the extraordinary power of “we.” Over the last year, the UK family has tirelessly proven that we can accomplish a great deal in the pursuit of the lofty vision and bold mission of Kentucky’s indispensable institution. Together, we have confronted new challenges, risen to meet opportunities, and redefined what it means to be the University *for* Kentucky.

At the end of the first year of our 2015-2020 Strategic Plan, we acknowledged with pride all that we accomplished, while sharing a renewed commitment to the aspirational goals yet to be realized.

This year, we made progress on:

- Improving undergraduate student success and engagement;
- Strengthening our graduate programs;
- Enhancing the diversity and inclusivity of our campus;
- Expanding our research enterprise;
- And leveraging our expertise to advance the public good.

Bolstered by near record-setting applications, we have continued to enroll high-quality, diverse first-year classes that have moved our total enrollment beyond 30,760 students. With your help, these students are succeeding at higher levels. During the last academic year, UK conferred more than 6,900 degrees to students who leave here ready to lead lives of meaning and purpose.



At the same time, we have undertaken an intentional effort to maintain affordability and access, understanding that financial need is a major factor in whether students earn their degrees. Over the last several years, we have doubled the amount of institutional support for financial aid and scholarships, budgeting \$126 million in the upcoming academic year. As a result, the average out-of-pocket expense for tuition and mandatory fees paid by undergraduate resident students has increased by only \$392 in the last eight years.

To help advance our institution toward ambitious goals for first-to-second-year retention rates (90%) and six-year graduation rates (70%), we have started implementation of the UK LEADS (Leveraging Economic Affordability for Developing Success) program, which will

shift more of our institutional aid toward financial need. The effort is guided by our commitment to the four pillars of student success: academic success, financial stability, belonging and engagement, and wellness.

Faculty and staff researchers added to a growing portfolio of transformative research, discovery, and creative scholarship. In fiscal year 2016-17, UK received \$331.3 million in external research grants and contracts - signifying that we are a major player among research institutions in the country. The \$19.8 million Clinical and Translational Science Award (CTSA) from the National Institutes of Health - a renewal of UK's 2011 CTSA - is one of many competitive federal grants earned by UK researchers. The \$265 million multi-disciplinary research facility is taking shape alongside the newly named Lee T. Todd, Jr. Biopharmaceutical Building and the Biomedical/Biological Sciences Research Building. The new research facility will be a hub for efforts in discovery that addresses Kentucky questions, answers which often have global implications.

UK HealthCare continued to meet the needs of patients and families who require complex, outstanding health care through our network of providers and state-of-the-art academic medical center. Annual patient discharges have grown by more than 102% since 2003, surpassing 38,700 in the last fiscal year. UK HealthCare represents 43% of our \$3.7 billion academic and research enterprise, caring for patients throughout Kentucky and, increasingly, the region.

New partners joined in our progress as the University reached extraordinary

levels of success in private philanthropy. Last year, we experienced yet another outstanding year in philanthropy, raising \$175.6 million in private support and more than 98,000 gifts from 50,000 donors. These results are a forerunner to what is a highly anticipated, exciting, and impactful fundraising campaign.

These efforts are bolstered by the more than \$2.2 billion in capital investments to improve student success, instruction, research and discovery, quality of life, and health care initiated or approved over the last several years. More than 90% of that investment is the result of public-private partnerships, philanthropy, strategic use of our resources, or other collaborations such as unprecedented support from UK Athletics and private philanthropy for the Jacobs Science Building. In every case, the capital investments we made extend our ability to teach, discover, and heal those we serve.

The last year yielded positive returns for the University and, by extension, the Commonwealth of Kentucky. We have identified and are pursuing the right set of priorities for the right time, but disruptions - both current and future - to what we do and how we do it challenge us to continue thinking anew. Global disruptions, changes in the traditional student pipeline, flat or declining public support for our work, the need to address the complex questions of our day, and the pressure to improve efficiency and productivity demand a creative and sustainable response. The context of our time compels us to look ahead and adopt creative, ambitious, responsive, and lasting solutions that will enable us to achieve aspirational goals in teaching,

learning, research, care, and service. These disruptions are not unique to the University of Kentucky or our state; they will rock higher education for the foreseeable future. Our ability to adapt will be integral to our future success.

Our shared success and the collective power of “we” give me confidence that the University of Kentucky can, must, and will be creative leaders in academia. To thrive, it will take a shared effort from the entire UK family. This work, and our shared future, will be marked by challenge, but also by incredible opportunity.

I look forward to walking this path, together.

A handwritten signature in black ink that reads "Eli Capilouto". The signature is written in a cursive style with a large initial "E" and a long, sweeping underline.

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 financial statements of the business-type activities and the aggregate remaining fund information of the University of Kentucky (University), collectively a component unit of the Commonwealth of Kentucky, as of and for the years ended June 30, 2017 and 2016, 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 opinions 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 \$196,764 and \$196,673 as of June 30, 2017 and 2016, respectively, and total revenues of \$331,387 and \$318,003, 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 opinions, 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 as a blended component unit, 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 opinions.

Opinions

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 respective financial position of the business-type activities and the aggregate remaining fund information of the University as of June 30, 2017 and 2016, and the respective changes in financial position and, where applicable, cash flows thereof, for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Emphasis of Matter

As discussed in Note 1 of the financial statements, in 2017, the University adopted Governmental Accounting Standards Board No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. Our opinions are not modified with respect to this matter.

Required Supplementary Information

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

Other Information

Our audits were conducted for the purpose of forming opinions on the 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.

The governing board listing and the message from the president have 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 them.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 19, 2017, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.

BKD, LLP

Louisville, Kentucky
October 19, 2017

**UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED JUNE 30, 2017 AND 2016**

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, 2017 and 2016. 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 plays a critical leadership role for the Commonwealth of Kentucky (the Commonwealth) by contributing to the economic development and quality of life within Kentucky's borders and beyond. The University nurtures a diverse community characterized by fairness and equal opportunity.

Vision. As Kentucky's indispensable 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 renamed 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 the year 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 21st century economy; to conduct research that extends the boundaries of scientific discovery; to contribute to our economy, and addresses relevant questions; 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.

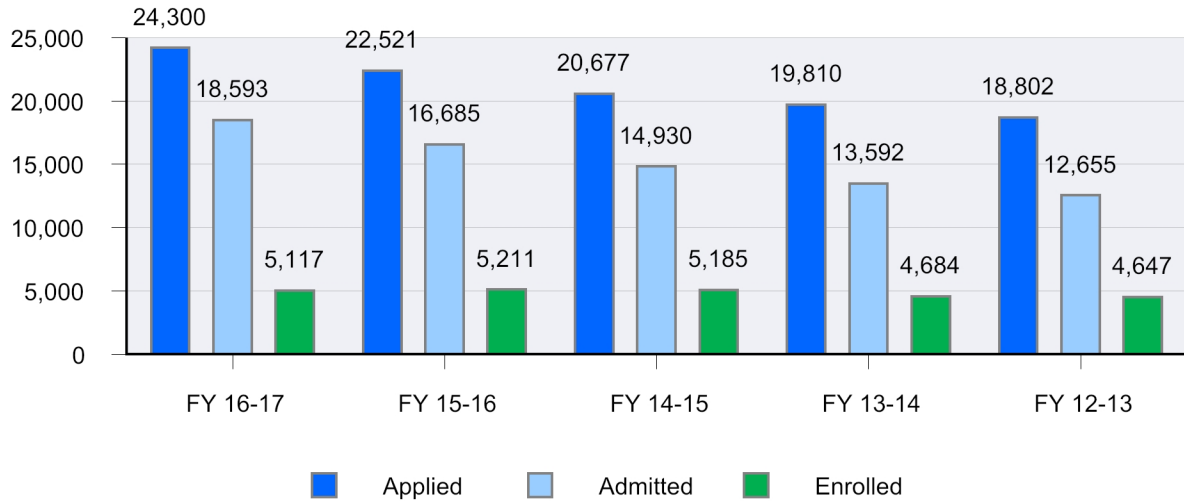
Under the leadership of Provost Timothy Tracy, progress on these objectives will be reported on an annual basis and presented to the UK Board of Trustees.

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 4,700 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 reaffirmed 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 2016, the University had 30,761 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 4,113 students (15.4%) since Fall 2007.

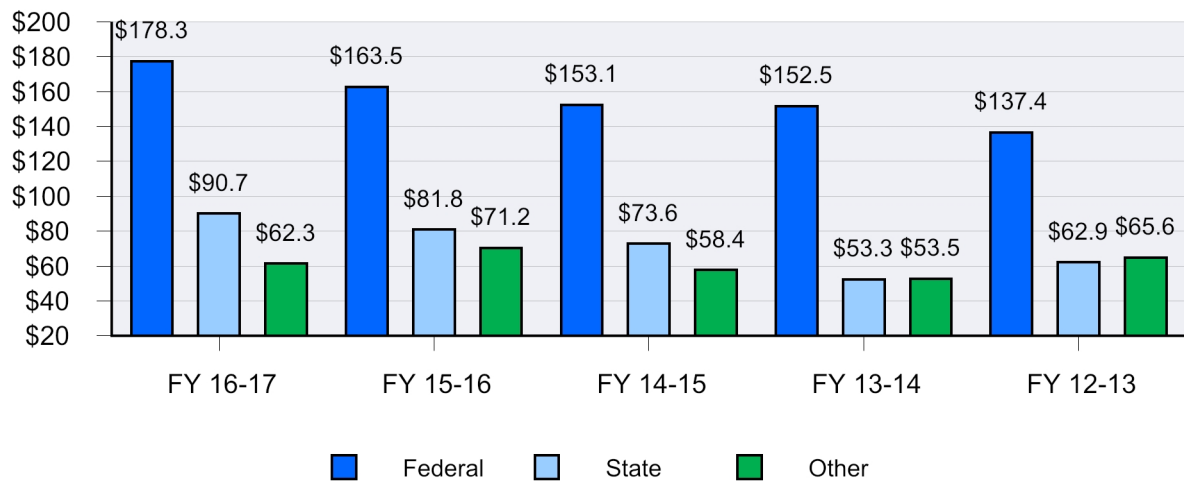
First Year Students Applied, Admitted and Enrolled (Fall Term)



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 \$349.7 million for fiscal year 2015-16, compared to \$331.7 million in fiscal year 2014-15. Research awards received during fiscal year 2016-17 total \$331.3 million, a five percent increase from the prior year amount of \$316.5 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, the University's advanced academic medical center and clinical care network, 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 2017, UK HealthCare was named number one in Kentucky in the latest U.S. News Best Hospitals ranking for the second consecutive year. 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 945 licensed beds with an average daily census of 722 patients. On a monthly basis, the System provides over 1,281 inpatient surgeries, 1,442 outpatient surgeries, 33,974 radiology procedures, 9,327 emergency department visits and 133,532 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. 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 \$6.19 billion, deferred outflows of resources of \$10.8 million, liabilities of \$1.80 billion and deferred inflows of resources of \$433.7 million as of June 30, 2017. 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 \$3.98 billion (64% of total assets).

- Total assets increased \$299.0 million (five percent), primarily due to increases in endowment investments and capital assets, net.

- Deferred outflows of resources decreased \$1.4 million (11%) due to the amortization of the difference between the reacquisition price and the net carrying amount of refunded debt.
- Total liabilities decreased \$19.6 million, primarily due to decreases in unearned revenue and bonds and capital lease obligations offset by increases in accounts payable and accrued liabilities.
- Deferred inflows of resources increased \$67.0 million (18%) primarily due to an increase in the service concession arrangement with Education Realty Trust (EdR).
- Total net position increased \$250.2 million (seven percent). Unrestricted net position increased \$48.8 million and net investment in capital assets increased \$136.2 million. Restricted net position increased \$65.2 million principally as a result of gain on endowment investments due to a positive return on the endowment pool.
- Operating revenues were \$2.73 billion and operating expenses were \$3.04 billion, resulting in a net loss from operations of \$308.8 million. Nonoperating and other revenues, net of nonoperating expenses, were \$559.0 million, including \$267.0 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
- Statement of Fiduciary Net Position
- Statement of Changes in Fiduciary Net Position
- 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 and its for-profit subsidiary, Kentucky Technology, Inc.
- 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.

The Fund for Advancement of Education and Research in the University of Kentucky Medical Center (The Fund) was dissolved on June 30, 2016. All assets held by The Fund were transferred to the University according to the Articles of Dissolution of The Fund on July 1, 2016.

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, 2017, with comparative information as of June 30, 2016. 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 (the difference between total assets and total liabilities and deferred inflows and outflows of resources) is 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 eroded 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, net, 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, 2017, 2016 and 2015 are as follows:

Condensed Statements of Net Position (in thousands)

| | 2017 | 2016 | 2015 |
|--|---------------------|---------------------|---------------------|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | | |
| Current assets | \$ 1,071,877 | \$ 1,058,800 | \$ 983,253 |
| Capital assets, net | 3,033,426 | 2,709,638 | 2,336,640 |
| Other noncurrent assets | 2,089,451 | 2,127,360 | 2,052,501 |
| Deferred outflows of resources | 10,808 | 12,164 | 13,755 |
| Total assets and deferred outflows of resources | <u>6,205,562</u> | <u>5,907,962</u> | <u>5,386,149</u> |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | |
| Current liabilities | 516,068 | 508,534 | 472,487 |
| Noncurrent liabilities | 1,279,070 | 1,306,155 | 1,215,280 |
| Deferred inflows of resources | 433,729 | 366,746 | 241,124 |
| Total liabilities and deferred inflows of resources | <u>2,228,867</u> | <u>2,181,435</u> | <u>1,928,891</u> |
| NET POSITION | | | |
| Net investment in capital assets | 1,663,197 | 1,527,034 | 1,422,560 |
| Restricted | | | |
| Nonexpendable | 613,522 | 601,703 | 585,074 |
| Expendable | 547,497 | 494,154 | 451,990 |
| Unrestricted | <u>1,152,479</u> | <u>1,103,636</u> | <u>997,634</u> |
| Total net position | <u>\$ 3,976,695</u> | <u>\$ 3,726,527</u> | <u>\$ 3,457,258</u> |

Assets. As of June 30, 2017, total assets amounted to \$6.19 billion. The largest asset class was capital assets, net, that totaled \$3.03 billion or 49% of total assets. Endowment investments were \$1.27 billion, or 20% of total assets and cash and cash equivalents totaled \$925.7 million, or 15% of total assets. During the year, total assets increased by a net \$299.0 million primarily due to increases in capital assets, net of \$323.8 million and endowment investments of \$166.6 million offset by decreases in cash and cash equivalents of \$166.4 million and other long-term investments of \$21.4 million.

Deferred Outflows of Resources. The University's deferred outflows of resources totaled \$10.8 million, a decrease of \$1.4 million, which represents the unamortized difference between the reacquisition price and the net carrying amount of refunded debt.

Liabilities. As of June 30, 2017, total liabilities amounted to \$1.80 billion. Bonds, notes and capital leases issued for educational buildings, housing, the UK HealthCare Hospital System facilities, Athletics' football stadium, student center and equipment totaled \$1.01 billion, or 56% of total liabilities. During the year, total liabilities decreased \$19.6 million primarily attributable to decreases in unearned revenue of \$1.5 million primarily due to the recognition of multimedia rights revenue as earned and long-term liabilities of \$26.9 million which was comprised of a \$30.9 million decrease in bonds, notes and capital leases and a \$4.0 million decrease in unamortized bond premium offset by an increase in other liabilities of \$8.1 million. Offsetting these decreases was an increase in accounts payable and accrued liabilities totaling \$8.8 million.

Deferred Inflows of Resources. The University's deferred inflows of resources totaled \$433.7 million that represents service concession arrangements with EdR of \$299.0 million, Aramark of \$131.5 million and Barnes and Noble of \$3.2 million. During the year, deferred inflows of resources increased \$67.0 million primarily due to an increase in EdR of \$76.7 million due to the completion of two new residence halls offset by a decrease in Aramark of \$8.8 million due to the amortization of revenue as earned for the service concession arrangement.

Net Position. The University's net position of \$3.98 billion as of June 30, 2017 is reported on the Statement of Net Position in three net position categories: net investment in capital assets, \$1.66 billion (42%); restricted nonexpendable, \$613.5 million (15%) and restricted expendable, \$547.5 million (14%); and unrestricted, \$1.15 billion (29%).

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 \$250.2 million during the year ended June 30, 2017. Net investment in capital assets increased \$136.2 million due to excess of additions of capital assets and principal payments of capital debt offset by depreciation expense. Restricted net position increased \$65.2 million as a result of gain on endowment investments due to a positive return on the endowment pool. Unrestricted net position increased \$48.8 million, primarily in UK HealthCare Hospital System due to the net increase in revenues in excess of expenses and positive return on the quasi endowment investments.

2016 Versus 2015. During the year ended June 30, 2016:

- Total assets increased by a net \$523.4 million primarily due to an increase in capital assets, net of \$373.0 million, cash and cash equivalents of \$155.6 million and other long-term investments of \$24.4 million offset by a decrease in endowment investments of \$21.0 million and notes, loans and accounts receivable, net of \$6.7 million.
- Deferred outflows of resources decreased \$1.6 million due to the unamortized difference between the reacquisition price and the net carrying amount of refunded debt.
- Total liabilities increased \$126.9 million primarily in the issuance of new debt of \$163.0 million offset by principal payments of \$49.8 million as well as an increase in other long-term liabilities of \$11.6 million and an increase in accounts payable and accrued liabilities of \$15.5 million offset by a decrease in unearned revenue of \$13.4 million.
- Deferred inflows of resources increased \$125.6 million due to the service concession arrangements with EdR and Aramark.
- Total net position increased \$269.3 million. 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.

Statement of Revenues, Expenses and Changes in Net Position

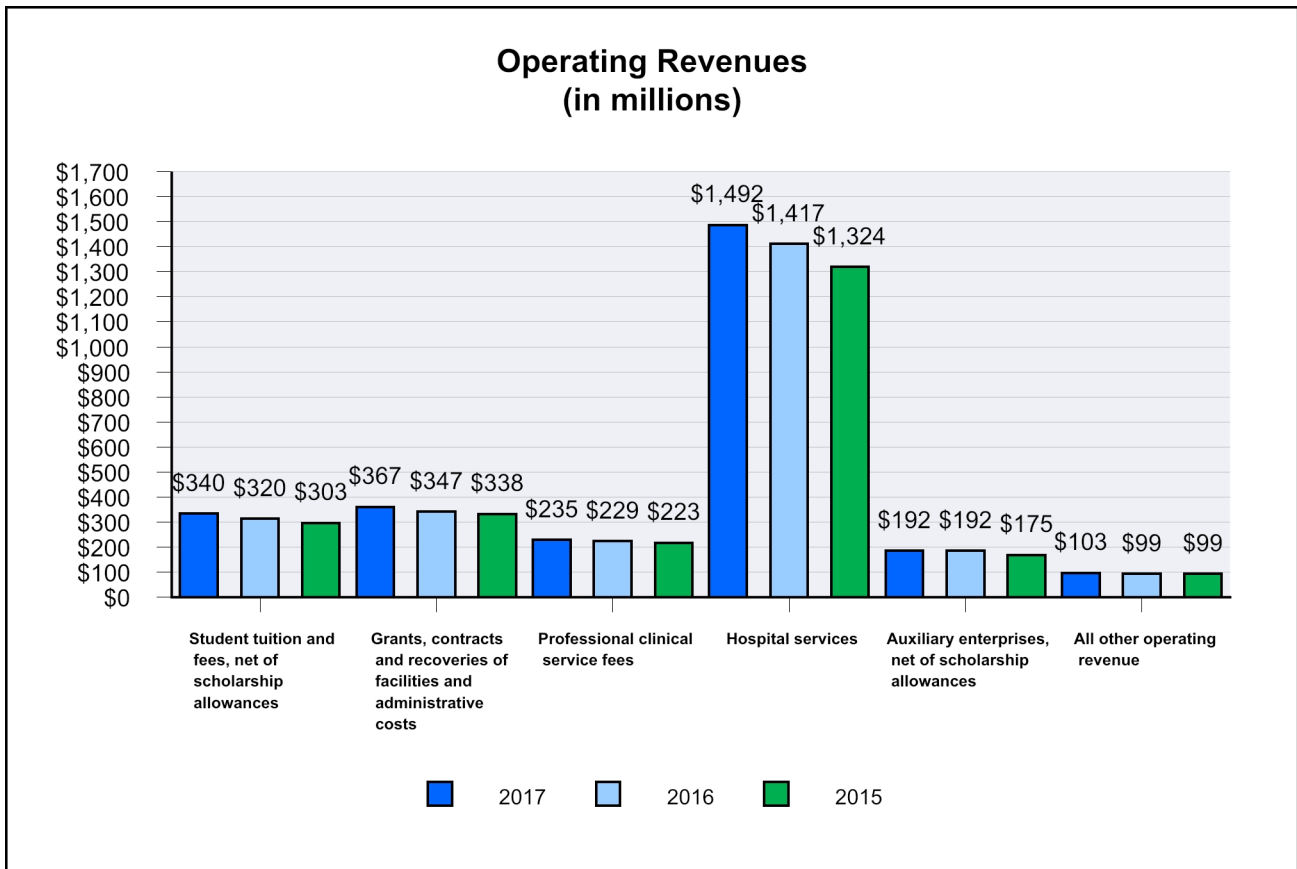
The Statement of Revenues, Expenses and Changes in Net Position is the University's income statement. It details how net position has changed during the year ended June 30, 2017, with comparative information for the year ended June 30, 2016. This statement is prepared on the accrual basis of accounting 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 loss from operations prior to the addition of nonoperating revenues (expenses). 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, 2017, 2016 and 2015 are as follows:

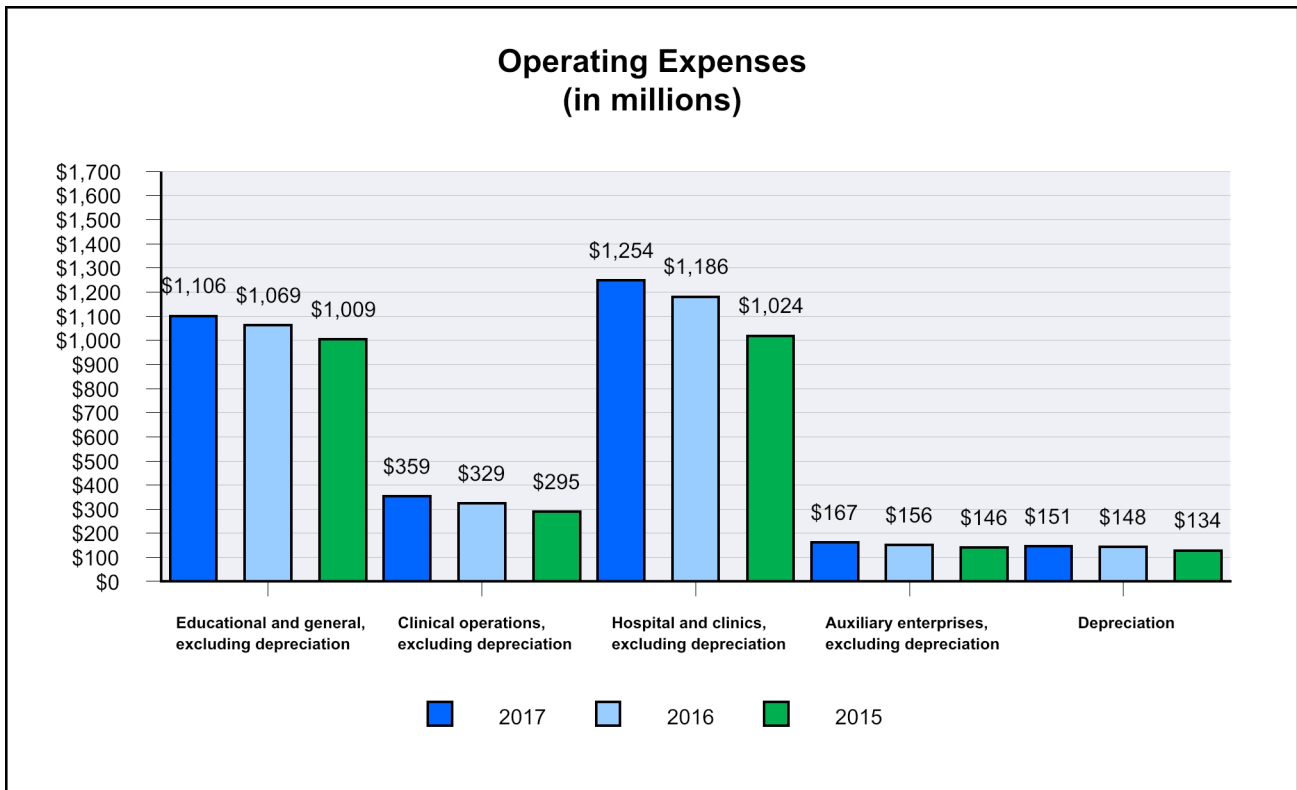
Condensed Statements of Revenues, Expenses and Changes in Net Position (in thousands)

| | <u>2017</u> | <u>2016</u> | <u>2015</u> |
|---|---------------------|---------------------|---------------------|
| OPERATING REVENUES | | | |
| Student tuition and fees, net of scholarship allowances | \$ 339,665 | \$ 319,627 | \$ 302,936 |
| Grants and contracts | 312,451 | 295,486 | 290,199 |
| Recoveries of facilities and administrative costs | 54,507 | 51,088 | 48,154 |
| Sales and services | 50,696 | 49,399 | 54,375 |
| Federal and county appropriations | 41,238 | 42,983 | 39,510 |
| Professional clinical service fees | 235,261 | 229,075 | 223,291 |
| Hospital services | 1,492,388 | 1,417,243 | 1,323,652 |
| Auxiliary enterprises, net of scholarship allowances | 192,197 | 191,532 | 175,232 |
| Other operating revenues | 10,668 | 7,931 | 5,059 |
| Total operating revenues | <u>2,729,071</u> | <u>2,604,364</u> | <u>2,462,408</u> |
| OPERATING EXPENSES | | | |
| Educational and general, excluding depreciation | 1,105,693 | 1,069,059 | 1,009,398 |
| Clinical operations, excluding depreciation | 359,002 | 328,705 | 294,430 |
| Hospital and clinics, excluding depreciation | 1,253,804 | 1,185,515 | 1,023,959 |
| Auxiliary enterprises, excluding depreciation | 167,358 | 156,081 | 146,452 |
| Depreciation | 151,445 | 148,109 | 134,374 |
| Other operating expenses | 594 | 570 | 640 |
| Total operating expenses | <u>3,037,896</u> | <u>2,888,039</u> | <u>2,609,253</u> |
| NET LOSS FROM OPERATIONS | <u>(308,825)</u> | <u>(283,675)</u> | <u>(146,845)</u> |
| NONOPERATING REVENUES (EXPENSES) | | | |
| State appropriations | 267,029 | 279,611 | 279,611 |
| Gift and non-exchange grants | 112,918 | 127,796 | 105,506 |
| Investment income (loss) | 114,018 | (3,241) | 44,925 |
| Interest on capital asset-related debt | (35,086) | (28,444) | (27,691) |
| Capital grants and gifts | 69,398 | 165,896 | 45,341 |
| Additions to permanent endowments | 9,760 | 13,052 | 7,758 |
| Other, net | 20,956 | (1,726) | 4,801 |
| Total nonoperating revenues (expenses) | <u>558,993</u> | <u>552,944</u> | <u>460,251</u> |
| INCREASE IN NET POSITION | 250,168 | 269,269 | 313,406 |
| NET POSITION, beginning of year | <u>3,726,527</u> | <u>3,457,258</u> | <u>3,143,852</u> |
| NET POSITION, end of year | <u>\$ 3,976,695</u> | <u>\$ 3,726,527</u> | <u>\$ 3,457,258</u> |



Total operating revenues were \$2.73 billion for the year ended June 30, 2017, an increase of \$124.7 million (five percent). The primary components of operating revenues were student tuition and fees, net of scholarship allowances, of \$339.7 million; grants and contracts and recoveries of facilities and administrative costs of \$367.0 million; professional clinical service fees of \$235.3 million; and hospital services of \$1.49 billion.

The major increase was in hospital services revenue of \$75.1 million attributable to an increase in rates, partially driven by patient acuity, and improved payer mix. Other significant increases in operating revenues related to net student tuition and fees of \$20.0 million due to tuition and fee rate increases as well as increased enrollment; grants and contracts and recoveries of facilities and administrative costs of \$20.4 million due to increases in federal and state grants and contracts; and professional clinical service fees of \$6.2 million.



Operating expenses totaled \$3.04 billion, an increase of \$149.9 million (five percent). Of this amount, \$1.11 billion, excluding depreciation, was expended for educational and general programs, including instruction, research and public service. Clinical operations expenses, excluding depreciation, were \$359.0 million; hospital and clinics expenses, excluding depreciation, amounted to \$1.25 billion; and auxiliary enterprises expenses, excluding depreciation, were \$167.4 million. Depreciation expense for the year amounted to \$151.4 million.

Educational and general expenses, excluding depreciation, increased \$36.6 million due primarily to increases in instruction of \$11.5 million, research of \$14.9 million, public service of \$2.0 million, academic support of \$6.0 million, institutional support of \$4.1 million and student financial aid of \$2.6 million offset by decreases in student services of \$2.1 million and operations and maintenance of plant of \$2.8 million. Clinical operations expenses, excluding depreciation, increased \$30.3 million primarily due to increased staffing and market adjustments for clinical faculty and staff. Hospital and clinics expenses, excluding depreciation, increased \$68.3 million primarily due to additional staffing and supplies required for increased patient volume and market adjustments for clinical staff. Auxiliary enterprises expenses, excluding depreciation, increased \$11.3 million primarily attributable to increases in Athletics of \$6.6 million due to contractual increases in coaches' salaries and minor renovation and maintenance costs at Kroger Field (formerly Commonwealth Stadium) and in other auxiliary of \$6.2 million principally due to expanded services in parking and transportation as well as an increase in student health services expenses. Depreciation expense increased \$3.3 million primarily due to new buildings and renovations.

The net loss from operations for the year was \$308.8 million. Nonoperating and other revenues, net of expenses, totaled \$559.0 million and included state appropriations of \$267.0 million. Investment income totaled \$114.0 million, an increase of \$117.3 million; gifts and non-exchange grants totaled \$112.9 million, a decrease of \$14.9 million; capital grants and gifts totaled \$69.4 million, a decrease of \$96.5 million and additions to permanent endowments totaled \$9.8 million, a decrease of \$3.3 million.

2016 Versus 2015. Total operating revenues were \$2.60 billion for the year ended June 30, 2016, including: student tuition and fees, net of scholarship allowances, of \$319.6 million (12%); grants and contracts and recoveries of facilities and administrative costs of \$346.6 million (13%); professional clinical service fees of

\$229.1 million (nine percent); and hospital services of \$1.42 billion (54%). Operating revenues for fiscal year 2016 increased \$142.0 million (six percent) over fiscal year 2015, primarily due to increases in hospital services 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; net student tuition and fees of \$16.7 million due to tuition and fees rate increases as well as increased enrollment; grants and 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 in fiscal year 2016. Of this amount, \$1.07 billion (37%), excluding depreciation, was expended for educational and general programs, including instruction, research and public service. Hospital and clinics expenses, excluding depreciation, totaled \$1.19 billion (41%) of the total operating expenses, and clinical operations expenses, excluding depreciation, were \$328.7 million (11%). Depreciation expense amounted to \$148.1 million (five percent). Operating expenses for fiscal year 2016 increased \$278.8 million (11%) compared to fiscal year 2015 primarily due to an increase in hospital and clinics expenses, excluding depreciation, of \$161.6 million (16%); educational and general expenses, excluding depreciation, of \$59.7 million (six percent); clinical operations expenses, excluding depreciation, of \$34.3 million (12%) and depreciation expense of \$13.7 million (10%). Auxiliary enterprises expenses, excluding depreciation, also increased \$9.6 million (seven percent).

The net loss from operations for the 2016 fiscal year totaled \$283.7 million. Nonoperating and other revenues, net of expenses, totaled \$553.0 million, resulting in an increase in net position of \$269.3 million for the year. Nonoperating revenues (expenses) included state appropriations of \$279.6 million for the years ended June 30, 2016 and 2015, respectively.

Statement of Cash Flows

The Statement of Cash Flows details how cash has increased or decreased during the fiscal year ended June 30, 2017, with comparative financial information for the fiscal year ended June 30, 2016. 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 capital debt, and capital debt repayments. Purchases of investments and proceeds from sales and maturities 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, 2017, 2016 and 2015 are as follows:

Condensed Statements of Cash Flows (in thousands)

| | 2017 | 2016 | 2015 |
|---|--------------|--------------|-------------|
| CASH PROVIDED (USED) BY: | | | |
| Operating activities | \$ (159,465) | \$ (89,874) | \$ 12,002 |
| Noncapital financing activities | 395,283 | 422,807 | 405,234 |
| Capital and related financing activities | (381,081) | (176,131) | (178,778) |
| Investing activities | (21,170) | (1,202) | 17,315 |
| Net increase (decrease) in cash and cash equivalents | (166,433) | 155,600 | 255,773 |
| CASH AND CASH EQUIVALENTS, beginning of year | 1,092,107 | 936,507 | 680,734 |
| CASH AND CASH EQUIVALENTS, end of year | \$ 925,674 | \$ 1,092,107 | \$ 936,507 |

The University's cash and cash equivalents decreased \$166.4 million in fiscal year 2017. Total cash provided by noncapital financing activities was \$395.3 million, a decrease of \$27.5 million compared to fiscal year 2016. Total cash used by operating activities was \$159.5 million, an increase of \$69.6 million; cash used by capital and related financing activities was \$381.1 million, an increase of \$205.0 million: reflecting both capital funding sources (debt proceeds) and uses (purchases of capital assets and debt service). Total cash used by investing activities was \$21.2 million, an increase of \$20.0 million.

Major sources of cash provided by operating activities were hospital services of \$1.49 billion; grants and contracts and recoveries of facilities and administrative costs of \$369.8 million; student tuition and fees of \$338.6 million; and professional clinical service fees of \$235.0 million. Major uses of cash for operating activities were payments to employees for salaries, wages and benefits of \$1.85 billion and to vendors and contractors of \$994.2 million.

Noncapital financing activities include state appropriations from the Commonwealth of \$272.6 million, gifts and grants for other than noncapital purposes of \$106.3 million and other receipts of \$17.4 million.

Capital and related financing activities include proceeds of capital debt of \$59.5 million and capital grants and gifts of \$82.0 million. Cash of \$370.9 million was expended for construction and purchases of capital assets and \$95.5 million was expended for principal and interest payments on capital debt and leases.

Investing activities include proceeds from sales and maturities of investments of \$830.4 million and interest and dividends on investments of \$25.6 million. Cash of \$877.1 million was used for purchase of investments.

2016 Versus 2015. Cash balances were higher when comparing fiscal year 2016 to fiscal year 2015. The \$155.6 million net increase in cash and cash equivalents was created from more cash provided by noncapital financing activities and less cash used by capital and related financing activities offset by more cash used for operating activities and investing activities.

Capital Assets and Debt Administration

Capital Assets.

Capital assets, net of accumulated depreciation, totaled \$3.03 billion at June 30, 2017, an increase of \$323.8 million. Capital assets as of June 30, 2017, 2016 and 2015, and significant changes in capital assets during the years ended June 30, 2016 and 2017 are as follows (in millions):

| | Balance June, 30 2015 | Net Additions (Deletions) FY 2015-16 | Balance June, 30 2016 | Net Additions (Deletions) FY 2016-17 | Balance June, 30 2017 |
|--|--------------------------|---|--------------------------|---|--------------------------|
| Land and land improvements | \$ 194 | \$ 27 | \$ 221 | \$ 32 | \$ 253 |
| Buildings, fixed equipment and infrastructure | 2,632 | 436 | 3,068 | 325 | 3,393 |
| Equipment, vehicles and capitalized software | 757 | (40) | 717 | 61 | 778 |
| Library materials and art | 164 | 3 | 167 | 1 | 168 |
| Certificate of need | 12 | — | 12 | — | 12 |
| Construction in progress | 267 | (8) | 259 | 37 | 296 |
| Accumulated depreciation | (1,689) | (45) | (1,734) | (133) | (1,867) |
| Total | <u>\$ 2,337</u> | <u>\$ 373</u> | <u>\$ 2,710</u> | <u>\$ 323</u> | <u>\$ 3,033</u> |

At June 30, 2017, the University had commitments in construction in progress for capital projects totaling approximately \$986.9 million in scope. Major projects include the construction of the new research building, student center, baseball stadium and health care facilities. The estimated cost to complete the projects in progress was approximately \$686.2 million.

Net additions also include EdR Phase II construction totaling \$78.5 million and Aramark capital construction and renovation projects of \$2.1 million.

Debt.

At June 30, 2017, capital debt amounting to \$1.01 billion, summarized by trust indenture and type, is as follows (in millions):

| | 2017 | 2016 | 2015 |
|----------------------------------|-----------------|-----------------|---------------|
| General Receipts bonds and notes | \$ 910 | \$ 946 | \$ 821 |
| Capital lease obligations | 83 | 79 | 90 |
| Notes payable | 20 | 19 | 19 |
| Total | <u>\$ 1,013</u> | <u>\$ 1,044</u> | <u>\$ 930</u> |

Debt decreased \$30.9 million during the year primarily due to principal payments of the University's debt obligations of \$49.7 million, partially offset by the issuance of General Receipts Bonds 2017 Series A and B for \$36.8 million, which refunded \$39.0 million of General Receipts Bonds 2010 Series A and Notes 2006 Series A. Partially offsetting the decrease are additions to capital leases and other long-term obligations of \$20.2 million. Also KMSF issued notes through Clark County and Scott County in the amount of \$19.8 million, which refunded \$19.0 million of the Central Bank note.

Economic and Other Factors That Will Affect the Future

Senior leadership continues to believe that the University is well-positioned to maintain its fiscally sound 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:

- According to a recent study by the Center on Budget and Policy Priorities (<http://www.cbpp.org/research/funding-down-tuition-up>), Kentucky ranks 7th-worst among all states in the percentage change in state spending per student, inflation adjusted, from 2008 to 2016. The study further highlights that recently most states increased funding per student for their postsecondary education systems. Thirty-eight states invested more per student in fiscal year 2015-16 than in fiscal year 2014-15. However, Kentucky continues to disinvest. This is even more evident in a review of the change in the distribution of Kentucky General Funds. From the 2004-06 biennium to 2016-18, Kentucky General Fund appropriations increased by \$6.50 billion, or 41 percent, from \$15.90 billion to \$22.40 billion. Over the same period, Kentucky General Fund appropriations to postsecondary education have decreased approximately \$100.0 million.
- According to the 2017 Kentucky Annual Economic Report by the University of Kentucky Gatton College of Business and Economics Center for Business and Economic Research (CBER), Kentucky's public pension programs are in dire financial condition, evidenced by a \$32.60 billion unfunded liability. By multiple measures, Kentucky's public pension system ranks as one of the most financially troubled among the 50 states. Governor Matt Bevin is expected to call a special session of the Kentucky General Assembly in the fall 2017 to address the funding problems with the public pension programs. While the University does not participate in the state's pension programs, the amount of available state funds for public postsecondary education will continue to be negatively impacted by the programs' financial condition.
- With regard to state support for postsecondary education, the enacted 2016-18 state budget included a 4.5% reduction in state appropriations for fiscal year 2016-17 and reallocated 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. The Kentucky Council on Postsecondary Education recently announced the results of the performance funding model for fiscal year 2017-18. Based on the model's 11 metrics, the University of Kentucky will receive \$60,400 more than its original allocation of \$13.4 million to the performance funding pool.
- Preliminary numbers for Fall 2017 indicate total enrollment will exceed 30,000 for the fourth consecutive year and student demand is expected to remain strong in the future. Over the next several years, under the UK Leveraging Economic Affordability for Developing Success (LEADS) program, the University will begin to award more of its institutional aid based on financial need. The LEADS initiative aligns with the UK Strategic Plan, which contemplates moving graduation rates to 70% and retention rates to 90% by 2020.
- UK HealthCare's vision is to create a system that rationalizes care, not rations care; providing a seamless continuum of care using a network committed to value - the best outcomes delivered most efficiently. Annual discharges from UK's hospitals have increased by more than 42% over the last 10 years, with annual discharges expected to exceed 40,000 by fiscal year 2017-18. The number of outpatient visits to UK's clinics has increased by more than 100% in the last 10 years to 1.6 million visits in fiscal year 2016-17. As a result of the Affordable Care Act (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 27% compared to Kentucky's 100%, (source: UK CBER 2017 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.
- UK is one of 22 universities in the country with the trifecta of top federal grants: an NCI-designated cancer center, the Clinical and Translational Science Award, and an Alzheimer's Disease Center. UK faculty and staff researchers were awarded \$331.3 million in external grants and contracts, in fiscal year 2016-17. As of June 30, 2017, grants and contracts of approximately \$226.5 million, an increase of approximately \$25.1 million from the previous year, have been awarded to the University but not expended.

- The University is completing a momentous physical transformation including academic, research, health care and athletic projects. From July 2011 to June 2016, over 116 projects totaling \$2.10 billion have been initiated. A major component of the University's physical transformation involved revitalization of on-campus housing and dining using comprehensive public/private partnerships (P3). The multiphase housing P3 was 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 2017, 14 new residence halls have opened with 6,850 total beds. Other transformation projects recently completed or currently underway include:
 - A \$406.6 million multiphase renovation and upgrade of UK HealthCare facilities, including the Kentucky's Children Hospital, which 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 March 2021.
 - 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 \$201.3 million renovation and expansion of the student center financed by the University that is expected to open in January 2018.
 - A \$126.5 million renovation and expansion of Kroger Field and a \$45.0 million football training facility and practice field, which opened in August 2015 and 2016, respectively, both completely financed by Athletics.
 - 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 \$65.0 million renovation and expansion of the Gatton College of Business and Economics, financed by the University, which opened in August 2016.
 - A \$56.0 million renovation and expansion of the College of Law building financed by \$35.0 million of state bonds and up to \$21.0 million by the University. The renovated and expanded facility is expected to be completed in June 2019.
 - A new \$49.0 million baseball stadium construction project, financed completely by Athletics which is expected to be completed in July 2018.
- The University will continue its long-term endowment investment strategy to maximize total returns, at an appropriate level of risk, while utilizing a spending rate policy to insulate programs funded by the endowment from temporary market volatility.

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 increasing its reputation as 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, 2017 AND 2016

| | <u>2017</u> | <u>2016</u> |
|--|----------------------------|----------------------------|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | |
| Current Assets | | |
| Cash and cash equivalents | \$ 684,693 | \$ 693,743 |
| Notes, loans and accounts receivable, net | 327,611 | 297,620 |
| Investments | 6,794 | 16,977 |
| Inventories and other assets | <u>52,779</u> | <u>50,460</u> |
| Total current assets | <u>1,071,877</u> | <u>1,058,800</u> |
| Noncurrent Assets | | |
| Restricted cash and cash equivalents | 240,981 | 398,364 |
| Endowment investments | 1,268,396 | 1,101,772 |
| Other long-term investments | 277,980 | 299,417 |
| Notes, loans and accounts receivable, net | 301,683 | 327,366 |
| Other noncurrent assets | 411 | 441 |
| Capital assets, net | <u>3,033,426</u> | <u>2,709,638</u> |
| Total noncurrent assets | <u>5,122,877</u> | <u>4,836,998</u> |
| Total assets | 6,194,754 | 5,895,798 |
| Deferred Outflows of Resources | | |
| | <u>10,808</u> | <u>12,164</u> |
| Total assets and deferred outflows of resources | <u>6,205,562</u> | <u>5,907,962</u> |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | |
| Current Liabilities | | |
| Accounts payable and accrued liabilities | 335,643 | 326,817 |
| Unearned revenue | 91,380 | 79,648 |
| Long-term liabilities - current portion | <u>89,045</u> | <u>102,069</u> |
| Total current liabilities | <u>516,068</u> | <u>508,534</u> |
| Noncurrent Liabilities | | |
| Unearned revenue | 166,599 | 179,853 |
| Long-term liabilities | <u>1,112,471</u> | <u>1,126,302</u> |
| Total noncurrent liabilities | <u>1,279,070</u> | <u>1,306,155</u> |
| Total liabilities | 1,795,138 | 1,814,689 |
| Deferred Inflows of Resources | | |
| | <u>433,729</u> | <u>366,746</u> |
| Total liabilities and deferred inflows of resources | <u>2,228,867</u> | <u>2,181,435</u> |
| NET POSITION | | |
| Net investment in capital assets | <u>1,663,197</u> | <u>1,527,034</u> |
| Restricted | | |
| Nonexpendable | | |
| Scholarships and fellowships | 158,249 | 150,458 |
| Research | 274,907 | 273,161 |
| Instruction | 83,822 | 82,455 |
| Academic support | 85,446 | 85,183 |
| Other | <u>11,098</u> | <u>10,446</u> |
| Total restricted nonexpendable | <u>613,522</u> | <u>601,703</u> |
| Expendable | | |
| Scholarships and fellowships | 80,375 | 65,097 |
| Research | 98,228 | 77,082 |
| Instruction | 52,227 | 49,620 |
| Academic support | 73,798 | 59,790 |
| Loans | 12,111 | 11,455 |
| Capital projects | 166,659 | 186,168 |
| Debt service | 3,774 | 17 |
| Auxiliary | 28,594 | 14,631 |
| Other | <u>31,731</u> | <u>30,294</u> |
| Total restricted expendable | <u>547,497</u> | <u>494,154</u> |
| Total restricted | <u>1,161,019</u> | <u>1,095,857</u> |
| Unrestricted | <u>1,152,479</u> | <u>1,103,636</u> |
| Total net position | <u>\$ 3,976,695</u> | <u>\$ 3,726,527</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, 2017 AND 2016

| | <u>2017</u> | <u>2016</u> |
|--|----------------------------|----------------------------|
| OPERATING REVENUES | | |
| Student tuition and fees | \$ 490,596 | \$ 457,893 |
| Less: Scholarship allowances | <u>(150,931)</u> | <u>(138,266)</u> |
| Net student tuition and fees | 339,665 | 319,627 |
| Federal grants and contracts | 181,888 | 169,291 |
| State and local grants and contracts | 97,268 | 91,216 |
| Nongovernmental grants and contracts | 33,295 | 34,979 |
| Recoveries of facilities and administrative costs | 54,507 | 51,088 |
| Sales and services | 50,696 | 49,399 |
| Federal appropriations | 16,332 | 19,266 |
| County appropriations | 24,906 | 23,717 |
| Professional clinical service fees | 235,261 | 229,075 |
| Hospital services | 1,492,388 | 1,417,243 |
| Auxiliary enterprises: | | |
| Housing and dining | 38,772 | 41,041 |
| Less: Scholarship allowances | <u>(1,194)</u> | <u>(1,938)</u> |
| Net housing and dining | 37,578 | 39,103 |
| Athletics | 102,341 | 102,995 |
| Other auxiliaries | 52,278 | 49,434 |
| Other operating revenues | <u>10,668</u> | <u>7,931</u> |
| Total operating revenues | <u>2,729,071</u> | <u>2,604,364</u> |
| OPERATING EXPENSES | | |
| Educational and general: | | |
| Instruction | 314,506 | 303,013 |
| Research | 276,088 | 261,171 |
| Public service | 186,579 | 184,582 |
| Libraries | 22,637 | 22,273 |
| Academic support | 83,117 | 77,079 |
| Student services | 39,951 | 42,083 |
| Institutional support | 62,730 | 58,643 |
| Operations and maintenance of plant | 80,661 | 83,420 |
| Student financial aid | 39,424 | 36,795 |
| Depreciation | <u>65,220</u> | <u>65,188</u> |
| Total educational and general | 1,170,913 | 1,134,247 |
| Clinical operations (including depreciation of \$3,721 in 2017 and \$8,390 in 2016) | 362,723 | 337,095 |
| Hospital and clinics (including depreciation of \$56,682 in 2017 and \$53,603 in 2016) | 1,310,486 | 1,239,118 |
| Auxiliary enterprises: | | |
| Housing and dining (including depreciation of \$9,756 in 2017 and \$6,259 in 2016) | 29,228 | 27,227 |
| Athletics (including depreciation of \$15,377 in 2017 and \$13,071 in 2016) | 130,773 | 121,859 |
| Other auxiliaries (including depreciation of \$689 in 2017 and \$1,598 in 2016) | 33,179 | 27,923 |
| Other operating expenses | <u>594</u> | <u>570</u> |
| Total operating expenses | <u>3,037,896</u> | <u>2,888,039</u> |
| Net loss from operations | <u>(308,825)</u> | <u>(283,675)</u> |
| NONOPERATING REVENUES (EXPENSES) | | |
| State appropriations | 267,029 | 279,611 |
| Gifts and non-exchange grants | 112,918 | 127,796 |
| Investment income (loss) | 114,018 | (3,241) |
| Interest on capital asset-related debt | (35,086) | (28,444) |
| Other nonoperating revenues and expenses, net | 16,650 | 16,653 |
| Net nonoperating revenues (expenses) | <u>475,529</u> | <u>392,375</u> |
| Net income (loss) before other revenues, expenses, gains or losses | <u>166,704</u> | <u>108,700</u> |
| Capital grants and gifts | 69,398 | 165,896 |
| Additions to permanent endowments | 9,760 | 13,052 |
| Other, net | <u>4,306</u> | <u>(18,379)</u> |
| Total other revenues (expenses) | <u>83,464</u> | <u>160,569</u> |
| INCREASE IN NET POSITION | <u>250,168</u> | <u>269,269</u> |
| NET POSITION, beginning of year | <u>3,726,527</u> | <u>3,457,258</u> |
| NET POSITION, end of year | <u>\$ 3,976,695</u> | <u>\$ 3,726,527</u> |

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, 2017 AND 2016

| | <u>2017</u> | <u>2016</u> |
|--|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Student tuition and fees | \$ 338,574 | \$ 320,092 |
| Grants and contracts | 315,181 | 299,217 |
| Recoveries of facilities and administrative costs | 54,587 | 52,313 |
| Sales and services | 49,167 | 51,744 |
| Federal appropriations | 15,896 | 18,630 |
| County appropriations | 25,558 | 22,869 |
| Payments to vendors and contractors | (994,156) | (923,966) |
| Student financial aid | (39,478) | (36,794) |
| Salaries, wages and benefits | (1,852,245) | (1,755,876) |
| Professional clinical service fees | 235,027 | 223,744 |
| Hospital services | 1,485,060 | 1,417,430 |
| Auxiliary enterprises receipts | 194,848 | 208,425 |
| Loans issued to students | (5,880) | (5,915) |
| Collection of loans to students | 4,315 | 7,529 |
| Self insurance receipts | 69,094 | 67,275 |
| Self insurance payments | (65,580) | (64,860) |
| Other receipts (payments) | 10,567 | 8,269 |
| Net cash provided (used) by operating activities | <u>(159,465)</u> | <u>(89,874)</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | |
| State appropriations | 272,621 | 274,019 |
| Gifts and grants received for other than capital purposes: | | |
| Gifts received for endowment purposes | 9,760 | 13,052 |
| Gifts received for other purposes | 96,500 | 113,956 |
| Agency and loan program receipts | 237,142 | 232,673 |
| Agency and loan program payments | (238,110) | (229,244) |
| Other financing receipts (payments) | 17,370 | 18,351 |
| Net cash provided (used) by noncapital financing activities | <u>395,283</u> | <u>422,807</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | |
| Capital grants and gifts | 81,999 | 164,154 |
| Purchases of capital assets | (370,883) | (416,832) |
| Proceeds from capital debt | 59,544 | 159,541 |
| Payments to refunding bond agents | (58,593) | — |
| Proceeds from sales of capital assets | 252 | — |
| Principal paid on capital debt and leases | (49,673) | (49,753) |
| Interest paid on capital debt and leases | (45,803) | (38,782) |
| Other financing receipts (payments) | 2,076 | 5,541 |
| Net cash provided (used) by capital and related financing activities | <u>(381,081)</u> | <u>(176,131)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Proceeds from sales and maturities of investments | 830,375 | 627,549 |
| Interest and dividends on investments | 25,568 | 24,745 |
| Purchases of investments | (877,113) | (653,496) |
| Net cash provided (used) by investing activities | <u>(21,170)</u> | <u>(1,202)</u> |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | <u>(166,433)</u> | <u>155,600</u> |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>1,092,107</u> | <u>936,507</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 925,674</u> | <u>\$ 1,092,107</u> |
| Reconciliation of net loss from operations to net cash provided (used) by operating activities: | | |
| Net loss from operations | \$ (308,825) | \$ (283,675) |
| Adjustments to reconcile net loss from operations to net cash provided (used) by operating activities: | | |
| Depreciation expense | 151,445 | 148,109 |
| Change in assets and liabilities: | | |
| Notes, loans and accounts receivable, net | (8,538) | 16,775 |
| Inventories and other assets | (3,464) | (3,229) |
| Accounts payable and accrued liabilities | 11,922 | 36,070 |
| Unearned revenue | (1,520) | (13,337) |
| Long-term liabilities | 7,056 | 8,018 |
| Deferred inflows of resources | (7,541) | 1,395 |
| Net cash provided (used) by operating activities | <u>\$ (159,465)</u> | <u>\$ (89,874)</u> |

See notes to financial statements

UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
STATEMENTS OF FIDUCIARY NET POSITION (in thousands)
JUNE 30, 2017 AND 2016

| | <u>2017</u> | <u>2016</u> |
|---|-------------------|-------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 2,278 | \$ 697 |
| Accrued interest receivable | 5 | 3 |
| Investments | 160,445 | 135,944 |
| Total assets | <u>162,728</u> | <u>136,644</u> |
| LIABILITIES | | |
| Accounts payable and accrued liabilities | <u>—</u> | <u>—</u> |
| Total liabilities | <u>—</u> | <u>—</u> |
| NET POSITION | | |
| Net position restricted for postemployment benefits other than pensions | <u>\$ 162,728</u> | <u>\$ 136,644</u> |

UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION (in thousands)
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016

| | <u>2017</u> | <u>2016</u> |
|---|-------------------|-------------------|
| Additions | | |
| Investment income: | | |
| Interest and dividend income | \$ 2,332 | \$ 2,002 |
| Net appreciation (depreciation) in fair value of investments | 12,132 | (3,250) |
| Less investment expense | — | — |
| Net investment income (loss) | <u>14,464</u> | <u>(1,248)</u> |
| Contributions: | | |
| University of Kentucky | 26,007 | 26,337 |
| Beneficiaries | 5,500 | 5,183 |
| Total contributions | <u>31,507</u> | <u>31,520</u> |
| Total additions | <u>45,971</u> | <u>30,272</u> |
| Deductions | | |
| Administrative expenses | 735 | 654 |
| Payments to retirees and beneficiaries | 19,152 | 18,369 |
| Total deductions | <u>19,887</u> | <u>19,023</u> |
| INCREASE (DECREASE) IN NET POSITION | <u>26,084</u> | <u>11,249</u> |
| NET POSITION restricted for postemployment benefits other than pensions, beginning of year | <u>136,644</u> | <u>125,395</u> |
| NET POSITION restricted for postemployment benefits other than pensions, end of year | <u>\$ 162,728</u> | <u>\$ 136,644</u> |

UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017 and 2016

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 (UKRF) and its for-profit subsidiary, Kentucky Technology, Inc. (KTI); 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 the following 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/ufs/financial-statements-and-investor-information.

The Fund for Advancement of Education and Research in the University of Kentucky Medical Center (The Fund) was dissolved on June 30, 2016. All assets held by The Fund were transferred to the University according to the Articles of Dissolution of The Fund on July 1, 2016.

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. The fiduciary funds financial statement presentation is intended to report the assets held in trust for the beneficiaries of the other postemployment benefit plans and focuses on the net position and the changes in net position.

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 note 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 (loss) 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 is recorded net of estimated uncollectible amounts based upon a review of outstanding receivables, historical collection information, and existing economic conditions.

Inventories. Inventories are stated 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 2,200 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, 2017 and 2016, the University’s annual endowment management fee was 0.50%.

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, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|---|------------------|------------------|
| Gross spending policy distribution | \$ 43,982 | \$ 40,791 |
| Reinvested spending policy distribution | (21,125) | (18,661) |
| Net spending policy distribution | <u>\$ 22,857</u> | <u>\$ 22,130</u> |
| Management fee | <u>\$ 5,758</u> | <u>\$ 5,375</u> |

Capital Assets. Capital assets are stated at cost at the date of acquisition or, in the case of gifts, at fair market value at the 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, 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 \$10.8 million and \$12.2 million as of June 30, 2017 and 2016, 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, 2017 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 or third parties on behalf of the students. 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 25% and 31%, respectively, of the System's net patient services revenues before the provision for doubtful accounts for the year ended June 30, 2017 and approximately 24% and 31%, respectively for the year ended June 30, 2016. 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. With expanded Medicaid, more Kentuckians are becoming insured, resulting in a decrease in the System's self-pay population. This has led to the System's inability to qualify for Disproportionate Share Hospital payments from Medicaid. The monies received from Medicaid which will be recouped are represented as third-party payer

settlements and included in accrued liabilities on the Statement of Net position totaled \$59.4 million and \$41.1 million for the years ended June 30, 2017 and 2016, respectively.

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. The amount of charges forgone for the services and supplies furnished under the System's charity care policy aggregated to approximately \$49.3 million and \$33.0 million for the years ended June 30, 2017 and 2016, respectively.

Management Contract Revenue. The System entered into a contract with the Kentucky Cabinet for Health and Family Services (CHFS) to manage Eastern State Hospital (ESH) and Central Kentucky Recovery Center (CKRC). Under the contract the System is reimbursed 100% of the related operating expenses up to a limit of \$37.2 million, and \$1.9 million, for ESH and CKRC, respectively. The System also receives an eight percent management fee. The initial contract term was August 13, 2013 to June 30, 2014 with the option to renew the contract for two additional one-year terms. Subsequent to year end, the contract was renewed for the period of July 1, 2017 to June 30, 2018 with substantially the same terms.

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 24. During fiscal years 2017 and 2016, departmental research in nonsponsored accounts of approximately \$75.2 million and \$67.9 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 make 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.

Adoption of GASB Statement No. 74. In June 2015, GASB issued GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which intends to improve financial reporting for

state and local governmental postemployment benefit plans other than pension plans. Also, in June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which intends to improve financial reporting by requiring recognition of the entire Other Postemployment Benefits (OPEB) liability and a more comprehensive measure of OPEB expense. GASB Statement No. 74 was adopted during fiscal year 2017 resulting in presentation of fiduciary fund financial statements, additional note disclosures and required supplementary information regarding net postemployment benefits liability. Certain fiscal year 2016 information was not presented because the actuarial valuation for prior periods was not available for implementation of GASB Statement No. 74. The adoption of GASB Statement No. 75 will require the University to record a net postemployment benefits liability on its Statements of Net Position. The University has determined adoption will have a significant impact on its financial statements and will reduce unrestricted net position when implemented during the year ending June 30, 2018.

Recent Accounting Pronouncements. As of June 30, 2017, the GASB has issued the following applicable statements to the University but are not yet implemented.

- 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 addresses employers whose employees are provided defined contribution other post-employment benefits (OPEB) and establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expenses. The University continues to work with an actuary to determine the impact of the pronouncement and estimates the OPEB liability of approximately \$267.3 million for the unfunded portion to be recorded on the University's financial statements. See notes 16 and 17 for information on the OPEB plans and funds held in trust.
- 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 recognize 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. See note 13 for information on funds held in trust by others.
- GASB Statement No. 84, *Fiduciary Activities*, issued January 2017. The provisions of this Statement are effective for fiscal years beginning after December 15, 2018 (fiscal year 2020). This Statement provides guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes and will require the University to include fiduciary fund financial statements for material fiduciary activities before the notes to the financial statements. The University has determined Statement No. 84 will have no material impact on its financial statements.
- GASB Statement No. 87, *Leases*, issued June 2017. The provisions of the Statement are effective for fiscal years beginning after December 15, 2019 (fiscal year 2021). This Statement requires certain lease assets and liabilities for leases that previously were classified as operating leases to be recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. The Statement establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The University has yet to determine the impact Statement No. 87 will have on its financial statements.

Reclassifications. Certain reclassifications have been made to the fiscal year 2016 financial statements to conform to the fiscal year 2017 financial statement presentation. These reclassifications had no effect on the 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 money market funds and deposits with local banks and the Commonwealth.
- Bond revenue fund and bond project fund investments held by the Treasurer of the Commonwealth as required by the University's bond trust indentures and invested in high quality global 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 and
 - managed by an external manager in a low duration strategy.
- Debt service reserve 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 and to maintain sound financial management practices.

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, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|---|--------------|--------------|
| <u>Statement of Net Position classification</u> | | |
| Current cash and cash equivalents | \$ 684,693 | \$ 693,743 |
| Restricted cash and cash equivalents | 240,981 | 398,364 |
| Total cash and cash equivalents | 925,674 | 1,092,107 |
| Current investments | 6,794 | 16,977 |
| Endowment investments | 1,268,396 | 1,101,772 |
| Other long-term investments | 277,980 | 299,417 |
| Total deposits and investments | \$ 2,478,844 | \$ 2,510,273 |

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 following table to permit reconciliation of the fair value hierarchy to the amounts presented in the Statements of Net Position.

The University has the following valuation measurements, by type, at June 30, 2017 (in thousands):

| | Fair Value Measurement Using | | | | | | Amortized or historical cost |
|--|------------------------------|--|---|---|------------------------------|-----------------------|------------------------------|
| | Total value | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total measured at fair value | Net asset value (NAV) | |
| <u>Non-endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | \$ 197,048 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 197,048 |
| Cash surrender value of life insurance policies | 3,829 | — | — | — | — | — | 3,829 |
| Certificates of deposit | 24,048 | — | 24,048 | — | 24,048 | — | — |
| Deposits with the Commonwealth of Kentucky ¹ | 146,346 | — | — | — | — | — | 146,346 |
| Global equity - international | 4,101 | 4,101 | — | — | 4,101 | — | — |
| Global equity - private ² | 676 | 56 | — | — | 56 | — | 620 |
| Global equity - U.S. | 10,116 | 10,116 | — | — | 10,116 | — | — |
| Global fixed income - high quality/rate sensitive ³ | 812,287 | 25 | 461,902 | — | 461,927 | — | 350,360 |
| Global fixed income - public credit | 4,583 | 3,787 | 796 | — | 4,583 | — | — |
| Guaranteed investment contracts | 5,896 | — | — | — | — | — | 5,896 |
| Other | 3 | — | — | — | — | — | 3 |
| Real assets - public | 1,515 | 1,515 | — | — | 1,515 | — | — |
| Total non-endowed deposits and investments | 1,210,448 | 19,600 | 486,746 | — | 506,346 | — | 704,102 |
| <u>Endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | 4,890 | — | — | — | — | — | 4,890 |
| Diversifying strategies ⁴ | 238,830 | — | — | — | — | 238,830 | — |
| Global equity - hedged funds | 105,684 | — | — | — | — | 105,684 | — |
| Global equity - international | 175,481 | 33,825 | 974 | 13 | 34,812 | 140,669 | — |
| Global equity - private ⁵ | 180,121 | — | — | 691 | 691 | 179,430 | — |
| Global equity - U.S. | 120,392 | 6,513 | 1,371 | — | 7,884 | 112,508 | — |
| Global fixed income - high quality/rate sensitive | 104,082 | 37,615 | 49,510 | — | 87,125 | 16,957 | — |
| Global fixed income - private credit ⁵ | 38,519 | — | — | — | — | 38,519 | — |
| Global fixed income - public credit | 61,472 | 30 | 2,205 | — | 2,235 | 59,237 | — |
| Real assets - private ⁵ | 121,645 | — | — | — | — | 121,645 | — |
| Real assets - public | 117,280 | 37,993 | — | — | 37,993 | 79,287 | — |
| Total endowed deposits and investments | 1,268,396 | 115,976 | 54,060 | 704 | 170,740 | 1,092,766 | 4,890 |
| Total deposits and investments | \$ 2,478,844 | \$ 135,576 | \$ 540,806 | \$ 704 | \$ 677,086 | \$ 1,092,766 | \$ 708,992 |

- 1) Non-endowed deposits with the Commonwealth include deposits held by the state for capital construction, tobacco research and state appropriations. The University does not earn investment income on these funds; all investment income accrues to the Commonwealth.
- 2) Non-endowed global equity - private includes a limited partnership whose fair market value is measured using its cost basis of \$172,000 as of December 31, 2016.
- 3) Non-endowed global fixed income - high quality/rate sensitive includes deposits and investments in the Commonwealth's limited pool and intermediate pool funds. As of June 30, 2017, \$350.4 million was held in the Commonwealth's limited-term investment pool and \$239.1 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.
- 4) Endowed diversifying strategies include investments in various diversified, unconstrained strategies including hedge funds and global tactical asset allocation strategies.
- 5) Endowed global equity - private, global fixed income - private credit and real assets - private include alternative investments whose fair market value is measured using its net asset value as of March 31, 2017 of \$179.4 million, \$820,587, and \$55.1 million, respectively.

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

| | Fair Value Measurement Using | | | | | | |
|--|------------------------------|--|---|---|------------------------------|-----------------------|------------------------------|
| | Total Value | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total measured at fair value | Net asset value (NAV) | Amortized or historical cost |
| <u>Non-endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | \$ 208,152 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 208,152 |
| Cash surrender value of life insurance policies | 3,383 | — | — | — | — | — | 3,383 |
| Certificates of deposit | 30,394 | — | 30,394 | — | 30,394 | — | — |
| Deposits with the Commonwealth of Kentucky ¹ | 234,343 | — | — | — | — | — | 234,343 |
| Global equity - international | 2,398 | 2,398 | — | — | 2,398 | — | — |
| Global equity - private ² | 309 | 87 | — | — | 87 | — | 222 |
| Global equity - U.S. | 7,839 | 7,392 | — | — | 7,392 | — | 447 |
| Global fixed income - high quality/rate sensitive ³ | 914,059 | 95 | 525,211 | — | 525,306 | — | 388,753 |
| Global fixed income - public credit | 1,804 | 1,804 | — | — | 1,804 | — | — |
| Guaranteed investment contracts | 4,722 | — | — | — | — | — | 4,722 |
| Other | 4 | — | — | — | — | — | 4 |
| Real assets - public | 1,094 | 1,094 | — | — | 1,094 | — | — |
| Total non-endowed deposits and investments | 1,408,501 | 12,870 | 555,605 | — | 568,475 | — | 840,026 |
| <u>Endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | 8,032 | — | — | — | — | — | 8,032 |
| Diversifying strategies ⁴ | 178,755 | — | — | — | — | 178,755 | — |
| Global equity - hedged funds | 148,846 | — | — | — | — | 148,846 | — |
| Global equity - international | 153,083 | 31,126 | 639 | 13 | 31,778 | 121,305 | — |
| Global equity - private ⁵ | 156,538 | — | — | 735 | 735 | 155,803 | — |
| Global equity - U.S. | 149,525 | 5,785 | 1,270 | — | 7,055 | 142,470 | — |
| Global fixed income - high quality/rate sensitive | 41,221 | — | 21,551 | — | 21,551 | 19,670 | — |
| Global fixed income - private credit ⁵ | 22,160 | — | — | — | — | 22,160 | — |
| Global fixed income - public credit | 45,245 | — | 2,669 | — | 2,669 | 42,576 | — |
| Real assets - private ⁵ | 118,964 | — | — | — | — | 118,964 | — |
| Real assets - public | 79,403 | 35,292 | — | — | 35,292 | 44,111 | — |
| Total endowed deposits and investments | 1,101,772 | 72,203 | 26,129 | 748 | 99,080 | 994,660 | 8,032 |
| Total deposits and investments | \$ 2,510,273 | \$ 85,073 | \$ 581,734 | \$ 748 | \$ 667,555 | \$ 994,660 | \$ 848,058 |

- 1) Non-endowed deposits with the Commonwealth include deposits held by the state for capital construction, tobacco research and state appropriations. The University does not earn investment income on these funds; all investment income accrues to the Commonwealth.
- 2) Non-endowed global equity - private includes a limited partnership whose fair market value is measured using its cost basis of \$222,000 as of December 31, 2015.
- 3) Non-endowed global fixed income - high quality/rate sensitive includes 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.
- 4) Endowed diversifying strategies include investments in various diversified, unconstrained strategies including hedge funds and global tactical asset allocation strategies. The fair market value includes an alternative investment measured using its net asset value as of March 31, 2016 of \$527,854.
- 5) Endowed global equity - private, global fixed income - private credit and real assets - private include alternative investments whose fair market value is measured using its net asset value as of March 31, 2016 of \$155.8 million, \$1.1 million, and \$116.2 million, respectively.

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.

Level 3 valuation for global equity investments are valued using either discounted cash flow or market comparable companies technique.

Investments valued using the net asset value (NAV) per share (or its equivalent) as of June 30, 2017 and 2016 are as follows (in thousands):

| | | 2017 | | | | | | |
|---|-----------------------|------------------------------------|-------------------------------------|-------------------------|------------------------------|-------------------------|----------------------------|----------------------|
| | | Redemption Frequency/Notice Period | | | | | | |
| | Net asset value (NAV) | Daily, weekly/ 1 - 7 days | Semi-monthly, monthly/ 15 - 75 days | Quarterly/ 60 - 90 days | Semi-annually/ 60 - 180 days | Annually/ 90 - 180 days | End of term/ 5 to 10 years | Unfunded commitments |
| Diversifying strategies | \$ 238,830 | \$ 61,041 | \$ 72,581 | \$ 69,494 | \$ — | \$ 26,924 | \$ 8,790 | \$ — |
| Global equity - hedged funds | 105,684 | — | 53,612 | 13,485 | 11,549 | 27,038 | — | — |
| Global equity - international | 140,669 | 45,394 | 95,275 | — | — | — | — | — |
| Global equity - private | 179,430 | — | — | — | — | — | 179,430 | 85,180 |
| Global equity - U.S. | 112,508 | 96,931 | 15,577 | — | — | — | — | — |
| Global fixed income - high quality/rate sensitive | 16,957 | 16,957 | — | — | — | — | — | — |
| Global fixed income - private credit | 38,519 | — | — | — | — | — | 38,519 | 12,956 |
| Global fixed income - public credit | 59,237 | 21,885 | — | — | 23,301 | 14,051 | — | — |
| Real assets - private | 121,645 | — | — | 48,966 | — | — | 72,679 | 57,908 |
| Real assets - public | 79,287 | 36,230 | 43,057 | — | — | — | — | — |
| Total measured at net asset value | \$ 1,092,766 | \$ 278,438 | \$ 280,102 | \$ 131,945 | \$ 34,850 | \$ 68,013 | \$ 299,418 | \$ 156,044 |

| | | 2016 | | | | | | |
|---|-----------------------|------------------------------------|-------------------------------------|-------------------------|------------------------------|-------------------------|----------------------------|----------------------|
| | | Redemption Frequency/Notice Period | | | | | | |
| | Net asset value (NAV) | Daily, weekly/ 1 - 7 days | Semi-monthly, monthly/ 15 - 75 days | Quarterly/ 60 - 90 days | Semi-annually/ 60 - 180 days | Annually/ 90 - 180 days | End of term/ 5 to 10 years | Unfunded commitments |
| Diversifying strategies | \$ 178,755 | \$ 74,547 | \$ — | \$ 104,208 | \$ — | \$ — | \$ — | \$ — |
| Global equity - hedged funds | 148,846 | — | 110,890 | 37,956 | — | — | — | — |
| Global equity - international | 121,305 | 20,613 | 100,692 | — | — | — | — | — |
| Global equity - private | 155,803 | — | — | — | — | — | 155,803 | 106,635 |
| Global equity - U.S. | 142,470 | — | 142,470 | — | — | — | — | — |
| Global fixed income - high quality/rate sensitive | 19,670 | 19,670 | — | — | — | — | — | — |
| Global fixed income - private credit | 22,160 | — | — | — | — | — | 22,160 | — |
| Global fixed income - public credit | 42,576 | 42,576 | — | — | — | — | — | 4,640 |
| Real assets - private | 118,964 | 2,743 | — | 48,853 | — | — | 67,368 | — |
| Real assets - public | 44,111 | 44,111 | — | — | — | — | — | 68,622 |
| Total measured at net asset value | \$ 994,660 | \$ 204,260 | \$ 354,052 | \$ 191,017 | \$ — | \$ — | \$ 245,331 | \$ 179,897 |

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 reasonably possible that changes in the values of investment securities will occur in the near term and that such changes 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 investments (deposits and money market funds) 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 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. Money market fund portfolios consist of securities eligible for short-term investments.
- Bond revenue fund and bond project 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 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, 2017 and 2016, respectively, the credit quality of the University's fixed income investments is summarized below (in thousands):

| | 2017 | | | | | | | 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 | \$ 197,048 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 197,048 |
| Certificates of deposit | — | — | — | — | — | 24,048 | — | 24,048 |
| Global fixed income - high quality/rate sensitive | 8,909 | 9,744 | 41,410 | 29,697 | 3,063 | 589,521 | 129,943 | 812,287 |
| Global fixed income - public credit | — | 180 | 428 | 188 | — | 3,787 | — | 4,583 |
| Guaranteed investment contracts | — | 69 | — | — | — | 5,827 | — | 5,896 |
| Total non-ended fixed income investments | <u>205,957</u> | <u>9,993</u> | <u>41,838</u> | <u>29,885</u> | <u>3,063</u> | <u>623,183</u> | <u>129,943</u> | <u>1,043,862</u> |
| <u>Endowed deposits and investments</u> | | | | | | | | |
| Cash and cash equivalents | — | — | — | — | — | 4,890 | — | 4,890 |
| Global fixed income - high quality/rate sensitive | 956 | 1,117 | 4,981 | 2,659 | 68 | 2,519 | 91,782 | 104,082 |
| Global fixed income - private credit | — | — | — | — | — | 38,519 | — | 38,519 |
| Global fixed income - public credit | 261 | 52 | 123 | 287 | 810 | 38,053 | 21,886 | 61,472 |
| Total endowed fixed income investments | <u>1,217</u> | <u>1,169</u> | <u>5,104</u> | <u>2,946</u> | <u>878</u> | <u>83,981</u> | <u>113,668</u> | <u>208,963</u> |
| Total fixed income investments | <u>\$ 207,174</u> | <u>\$ 11,162</u> | <u>\$ 46,942</u> | <u>\$ 32,831</u> | <u>\$ 3,941</u> | <u>\$ 707,164</u> | <u>\$ 243,611</u> | <u>\$ 1,252,825</u> |
| | | | | | | | | |
| 2016 | | | | | | | | |
| S&P/Moody's Credit Ratings | | | | | | | | |
| | AAA/Aaa | AA/Aa | A | BBB/Baa | Below BBB/Baa | Not rated | Rating not applicable | Total |
| <u>Non-ended deposits and investments</u> | | | | | | | | |
| Cash and cash equivalents | \$ 195,853 | \$ — | \$ — | \$ — | \$ — | \$ 12,299 | \$ — | \$ 208,152 |
| Certificates of deposit | — | — | — | — | — | 30,394 | — | 30,394 |
| Global fixed income - high quality/rate sensitive | 11,333 | 13,411 | 20,922 | 24,994 | 13,697 | 677,063 | 152,639 | 914,059 |
| Global fixed income - public credit | — | — | — | — | — | 1,804 | — | 1,804 |
| Guaranteed investment contracts | — | 34 | — | — | — | 4,688 | — | 4,722 |
| Total non-ended fixed income investments | <u>207,186</u> | <u>13,445</u> | <u>20,922</u> | <u>24,994</u> | <u>13,697</u> | <u>726,248</u> | <u>152,639</u> | <u>1,159,131</u> |
| <u>Endowed deposits and investments</u> | | | | | | | | |
| Cash and cash equivalents | — | — | — | — | — | 8,032 | — | 8,032 |
| Global fixed income - high quality/rate sensitive | 845 | 139 | 1,621 | 1,809 | 683 | 23,335 | 12,789 | 41,221 |
| Global fixed income - private credit | — | — | — | — | — | 22,160 | — | 22,160 |
| Global fixed income - public credit | 386 | 62 | 183 | 381 | 746 | 43,487 | — | 45,245 |
| Total endowed fixed income investments | <u>1,231</u> | <u>201</u> | <u>1,804</u> | <u>2,190</u> | <u>1,429</u> | <u>97,014</u> | <u>12,789</u> | <u>116,658</u> |
| Total fixed income investments | <u>\$ 208,417</u> | <u>\$ 13,646</u> | <u>\$ 22,726</u> | <u>\$ 27,184</u> | <u>\$ 15,126</u> | <u>\$ 823,262</u> | <u>\$ 165,428</u> | <u>\$ 1,275,789</u> |

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 and money market funds) are not exposed to custodial credit risk. Deposits and money market funds are held in the University's name by various financial institutions.
- Bond revenue fund and bond project 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 debt service reserve funds are held by the respective bond trustee in a specific trust account for the benefit of the University and its bondholders.
- Endowment investments are held in the University's name by the University's custodian.

Non-endowed global fixed income - high quality/rate sensitive investments whose fair market value was \$589.5 million and \$671.2 million, as of June 30, 2017 and 2016, respectively, were exposed to custodial credit risk. These bond revenue fund investments were held by the Commonwealth, uninsured and not registered in the name of the University.

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 and money market funds) are not limited to a maximum amount that may be invested in one issuer. However, 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 and bond project 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 debt service reserve 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, 2017 and 2016, 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 and money market funds) have limited exposure to interest rate risk due to the short-term nature of the investment. The University requires that all deposits and money market funds be available for use on the next business day.
- Bond revenue fund and bond project fund 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 36 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 Bond Index.
- Investment securities held in debt service reserve 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 manager 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 mitigate interest rate risk.

For June 30, 2017 and 2016, the maturity distribution of the University's fixed income investments is summarized below (in thousands):

| | 2017 | | | | | | Total |
|---|---------------------|------------|----------|-----------------|---------------------------|----------------------|--------------|
| | Maturities in Years | | | | | | |
| | Less than 1 | 1-5 | 5-10 | Greater than 10 | Managed based on duration | Alternative strategy | |
| <u>Non-endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | \$ 197,048 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 197,048 |
| Certificates of deposit | 22,824 | 1,224 | — | — | — | — | 24,048 |
| Global fixed income - high quality/rate sensitive | 935 | 128,268 | 550 | 210 | 682,324 | — | 812,287 |
| Global fixed income - public credit | 40 | 285 | 522 | — | 3,736 | — | 4,583 |
| Guaranteed investment contracts | 69 | — | 5,827 | — | — | — | 5,896 |
| Total non-endowed fixed income investments | 220,916 | 129,777 | 6,899 | 210 | 686,060 | — | 1,043,862 |
| <u>Endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | 4,890 | — | — | — | — | — | 4,890 |
| Global fixed income - high quality/rate sensitive | 22 | 44 | — | — | 104,016 | — | 104,082 |
| Global fixed income - private credit ¹ | — | — | — | — | — | 38,519 | 38,519 |
| Global fixed income - public credit | — | — | — | — | 24,121 | 37,351 | 61,472 |
| Total endowed fixed income investments | 4,912 | 44 | — | — | 128,137 | 75,870 | 208,963 |
| Total fixed income investments | \$ 225,828 | \$ 129,821 | \$ 6,899 | \$ 210 | \$ 814,197 | \$ 75,870 | \$ 1,252,825 |
| | | | | | | | |
| 2016 | | | | | | | |
| <u>Maturities in Years</u> | | | | | | | |
| | Less than 1 | 1-5 | 5-10 | Greater than 10 | Managed based on duration | Alternative strategy | Total |
| <u>Non-endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | \$ 208,152 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 208,152 |
| Certificates of deposit | 30,394 | — | — | — | — | — | 30,394 |
| Global fixed income - high quality/rate sensitive | 4,176 | 127,414 | 446 | — | 782,023 | — | 914,059 |
| Global fixed income - public credit | — | — | — | — | 1,804 | — | 1,804 |
| Guaranteed investment contracts | 8 | — | 34 | 4,680 | — | — | 4,722 |
| Total non-endowed fixed income investments | 242,730 | 127,414 | 480 | 4,680 | 783,827 | — | 1,159,131 |
| <u>Endowed deposits and investments</u> | | | | | | | |
| Cash and cash equivalents | 8,032 | — | — | — | — | — | 8,032 |
| Global fixed income - high quality/rate sensitive | 27 | 67 | — | — | 41,127 | — | 41,221 |
| Global fixed income - private credit ¹ | — | — | — | — | — | 22,160 | 22,160 |
| Global fixed income - public credit | — | — | — | — | 45,245 | — | 45,245 |
| Total endowed fixed income investments | 8,059 | 67 | — | — | 86,372 | 22,160 | 116,658 |
| Total fixed income investments | \$ 250,789 | \$ 127,481 | \$ 480 | \$ 4,680 | \$ 870,199 | \$ 22,160 | \$ 1,275,789 |

1) Endowment global fixed income - private and public credit includes alternative investments that are not managed within traditional maturity or duration constraints.

At June 30, 2017 and 2016, the University had the following investments managed based on duration (in thousands):

| | 2017 | | 2016 | |
|---|-------------------|---------------------------|-------------------|---------------------------|
| | Fair Value | Modified Duration (Years) | Fair Value | Modified Duration (Years) |
| <u>Non-endowed deposits and investments</u> | | | | |
| Global fixed income - high quality/rate sensitive | | | | |
| Commonwealth of Kentucky intermediate pool | \$ 239,135 | 1.1 | \$ 287,927 | 1.1 |
| Commonwealth of Kentucky limited pool | 350,360 | 0.1 | 383,241 | 0.1 |
| Externally managed low duration strategy fund | 92,804 | 2.6 | 110,760 | 2.4 |
| Kentucky Technology, Inc. | 25 | 3.0 | 95 | 1.1 |
| Global fixed income - public credit | 3,736 | 4.9 | 1,804 | 3.8 |
| Total non-endowment investment | <u>686,060</u> | | <u>783,827</u> | |
| <u>Endowed deposits and investments</u> | | | | |
| Global fixed income - high quality/rate sensitive | 104,016 | 5.3 | 41,127 | 5.2 |
| Global fixed income - public credit | 24,121 | 2.6 | 45,245 | 1.4 |
| Total endowment investment | <u>128,137</u> | | <u>86,372</u> | |
| Total managed based on duration | <u>\$ 814,197</u> | | <u>\$ 870,199</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, 2017 and 2016, the following endowment investments were subject to foreign currency risk (in thousands):

| | Fair Value | |
|-------------------------------|------------------|------------------|
| | 2017 | 2016 |
| Global equity - international | \$ 37,719 | \$ 30,500 |
| Global equity - private | 4,738 | 5,347 |
| Real assets - private | 6,208 | 6,678 |
| Total | <u>\$ 48,665</u> | <u>\$ 42,525</u> |

3. NOTES, LOANS AND ACCOUNTS RECEIVABLE, NET

Notes, loans and accounts receivable as of June 30, 2017 and 2016 are as follows (in thousands):

| | 2017 | | |
|---|---------------------|---------------------|-------------------|
| | Gross Receivable | Allowance | Net Receivable |
| Accrued interest receivable | \$ 1,488 | \$ — | \$ 1,488 |
| Dentistry patient accounts | 2,429 | (532) | 1,897 |
| Hospital patient accounts (net of contractual allowances) | 235,689 | (73,136) | 162,553 |
| KMSF patient accounts (net of contractual allowances) | 41,813 | (6,921) | 34,892 |
| Multimedia rights receivable | 172,414 | — | 172,414 |
| Pledges receivables (less discounts of \$8,997) | 97,089 | (31,287) | 65,802 |
| Reimbursement receivable - federal appropriations | 2,712 | — | 2,712 |
| Reimbursement receivable - grants and contracts | 32,503 | (325) | 32,178 |
| Service concession arrangements | 87,116 | — | 87,116 |
| Student loans | 29,771 | (3,188) | 26,583 |
| Student accounts | 28,301 | (14,107) | 14,194 |
| Other | 27,465 | — | 27,465 |
| Total | <u>\$ 758,790</u> | <u>\$ (129,496)</u> | <u>\$ 629,294</u> |
| Current portion | | | \$ 327,611 |
| Noncurrent portion | | | 301,683 |
| Total | | | <u>\$ 629,294</u> |
| | 2016 | | |
| | Gross Receivable | Allowance | Net Receivable |
| Accrued interest receivable | \$ 1,554 | \$ — | \$ 1,554 |
| Dentistry patient accounts | 3,085 | (846) | 2,239 |
| Hospital patient accounts (net of contractual allowances) | 199,788 | (61,182) | 138,606 |
| KMSF patient accounts (net of contractual allowances) | 42,014 | (6,884) | 35,130 |
| Multimedia rights receivable | 191,644 | — | 191,644 |
| Pledges receivables (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 accounts | 28,098 | (16,233) | 11,865 |
| Other | 29,969 | — | 29,969 |
| Total | <u>\$ 743,647</u> | <u>\$ (118,661)</u> | <u>\$ 624,986</u> |
| Current portion | | | \$ 297,620 |
| Noncurrent portion | | | 327,366 |
| Total | | | <u>\$ 624,986</u> |

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, 2017 and 2016, 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 \$171.7 million and \$144.1 million at June 30, 2017 and 2016, respectively. The University records these amounts as revenue when the cash is received.

4. CAPITAL ASSETS, NET

Capital assets as of June 30, 2017 and capital asset activity for the year ended June 30, 2017 are summarized below (in thousands):

| | June 30, 2016 | Additions | Deletions | June 30, 2017 |
|------------------------------------|---------------------|-------------------|-------------------|---------------------|
| Land | \$ 74,645 | \$ 8,393 | \$ 7 | \$ 83,031 |
| Land improvements - nonexhaustible | 56,876 | 9,137 | — | 66,013 |
| Land improvements - exhaustible | 89,261 | 14,799 | — | 104,060 |
| Buildings | 2,846,739 | 305,033 | 2,889 | 3,148,883 |
| Fixed equipment - communications | 113,989 | 14,941 | — | 128,930 |
| Infrastructure | 107,789 | 7,457 | — | 115,246 |
| Equipment | 526,236 | 68,960 | 25,081 | 570,115 |
| Vehicles | 22,484 | 1,881 | 1,420 | 22,945 |
| Library materials | 147,223 | 1,743 | 845 | 148,121 |
| Nondepreciable library materials | 6,673 | — | — | 6,673 |
| Capitalized software | 168,560 | 16,960 | — | 185,520 |
| Art | 12,751 | 226 | — | 12,977 |
| Certificate of need | 11,609 | — | — | 11,609 |
| Construction in progress | 259,026 | 223,696 | 186,867 | 295,855 |
| | <u>4,443,861</u> | <u>673,226</u> | <u>217,109</u> | <u>4,899,978</u> |
| <u>Accumulated Depreciation</u> | | | | |
| Land improvements - exhaustible | 61,353 | 4,995 | — | 66,348 |
| Buildings | 924,391 | 79,945 | 1,093 | 1,003,243 |
| Fixed equipment - communications | 72,643 | 8,042 | — | 80,685 |
| Infrastructure | 40,515 | 4,203 | — | 44,718 |
| Equipment | 369,204 | 39,554 | 16,682 | 392,076 |
| Vehicles | 18,674 | 1,654 | 1,341 | 18,987 |
| Library materials | 139,490 | 1,967 | — | 141,457 |
| Capitalized software | 107,953 | 11,085 | — | 119,038 |
| | <u>1,734,223</u> | <u>151,445</u> | <u>19,116</u> | <u>1,866,552</u> |
| Capital assets, net | <u>\$ 2,709,638</u> | <u>\$ 521,781</u> | <u>\$ 197,993</u> | <u>\$ 3,033,426</u> |

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 | 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> |

At June 30, 2017, the University had commitments in construction in progress for capital projects totaling approximately \$986.9 million in scope. The estimated cost to complete these projects was approximately \$686.2 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 \$9.9 million for fiscal year 2017 and \$11.9 million for fiscal year 2016.

During fiscal years 2017 and 2016, the University utilized capital leases to acquire various items of equipment. As of June 30, 2017 and 2016, the net book value of land, buildings, equipment and software acquired through capital leases included in the above schedules totaled \$87.1 million and \$98.0 million, respectively.

During fiscal year 2017, 14 properties were demolished with an original cost of \$1.3 million and accumulated depreciation of \$59,000, for a total net book value written off of \$1.3 million. As of June 30, 2017, two buildings, most notably, Hagan Baseball Stadium, were scheduled for demolition in a subsequent fiscal year and were changed to estimated useful lives to record depreciation expense. A portion of the net book value of each building was written off with the remainder to be written off in the subsequent fiscal year. The total original cost was \$4.5 million with accumulated depreciation of \$3.0 million, and a total net book value written off in fiscal year 2017 of \$714,000.

Non-cash capital asset and related financing activities as of June 30, 2017 and 2016 are summarized below (in thousands):

| | <u>2017</u> | <u>2016</u> |
|---|-------------|-------------|
| Capital lease additions | \$ 20,165 | \$ 7,106 |
| Gifts of capital assets | \$ 3,515 | \$ 1,932 |
| Capital asset change in accounts payable | \$ (2,170) | \$ (17,992) |
| Capital asset additions by service concession arrangements | \$ 87,196 | \$ 147,749 |
| Capitalized interest, net of investment income | \$ 9,886 | \$ 11,886 |
| Amortized bond discount and premium | \$ 7,084 | \$ 6,528 |
| Amortized difference between reacquisition price and net carrying amount of refunded debt | \$ 1,621 | \$ 1,592 |
| Capital asset trade in | \$ 814 | \$ 734 |

5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2017 and 2016 are as follows (in thousands):

| | <u>2017</u> | <u>2016</u> |
|---|-------------------|-------------------|
| Payable to vendors and contractors | \$ 202,992 | \$ 183,371 |
| Accrued expenses, including vacation and sick leave | 84,742 | 84,977 |
| Employee withholdings and deposits payable to third parties | 47,909 | 58,469 |
| Total | <u>\$ 335,643</u> | <u>\$ 326,817</u> |

6. UNEARNED REVENUE

Unearned revenues as of June 30, 2017 and 2016 are as follows (in thousands):

| | <u>June 30, 2016</u> | <u>Additions</u> | <u>Reductions</u> | <u>June 30, 2017</u> | <u>Current Portion</u> | <u>Noncurrent Portion</u> |
|---------------------------------------|--------------------------|-------------------|-------------------|--------------------------|----------------------------|-------------------------------|
| Unearned summer school revenue | \$ 9,282 | \$ 9,325 | \$ 9,282 | \$ 9,325 | \$ 9,325 | \$ — |
| Unearned hospital revenue | 7,030 | 92,187 | 82,714 | 16,503 | 16,503 | — |
| Unearned grants and contracts revenue | 30,551 | 65,144 | 62,718 | 32,977 | 32,977 | — |
| Unearned multimedia rights revenue | 193,584 | 14,036 | 28,073 | 179,547 | 14,036 | 165,511 |
| Prepaid athletics ticket sales | 10,716 | 14,482 | 12,807 | 12,391 | 12,391 | — |
| Other | 8,338 | 10,874 | 11,976 | 7,236 | 6,148 | 1,088 |
| Total | <u>\$ 259,501</u> | <u>\$ 206,048</u> | <u>\$ 207,570</u> | <u>\$ 257,979</u> | <u>\$ 91,380</u> | <u>\$ 166,599</u> |

| | <u>June 30, 2015</u> | <u>Additions</u> | <u>Reductions</u> | <u>June 30, 2016</u> | <u>Current Portion</u> | <u>Noncurrent 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 athletics 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> |

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, 2017 and long-term liability activity for the year ended June 30, 2017 are summarized below (in thousands):

| | June 30, 2016 | Additions | Reductions | June 30, 2017 | Current Portion | Noncurrent Portion |
|--|---------------------|-------------------|-------------------|---------------------|--------------------|-----------------------|
| <u>Bonds, notes and capital leases</u> | | | | | | |
| General receipts notes | \$ 52,755 | \$ — | \$ 42,615 | \$ 10,140 | \$ 6,950 | \$ 3,190 |
| General receipts bonds | 892,670 | 36,805 | 29,385 | 900,090 | 32,310 | 867,780 |
| Capital leases and other | | | | | | |
| long-term obligations | 79,301 | 20,165 | 16,499 | 82,967 | 12,310 | 70,657 |
| Notes payable | 18,929 | 19,750 | 19,127 | 19,552 | 730 | 18,822 |
| Total bonds, notes and capital leases | <u>1,043,655</u> | <u>76,720</u> | <u>107,626</u> | <u>1,012,749</u> | <u>52,300</u> | <u>960,449</u> |
| <u>Other liabilities</u> | | | | | | |
| Annuities payable | 3,639 | 296 | 536 | 3,399 | 539 | 2,860 |
| Automobile and property self insurance | 478 | 187 | 184 | 481 | 481 | — |
| Compensated absences | 7,200 | — | 300 | 6,900 | 889 | 6,011 |
| Federal loan programs | 20,460 | 474 | 337 | 20,597 | — | 20,597 |
| Health insurance | 10,019 | 51,370 | 50,353 | 11,036 | 11,036 | — |
| Insurance executory costs | 11,305 | 1,991 | 182 | 13,114 | 182 | 12,932 |
| Long-term disability | — | — | — | — | — | — |
| Medical malpractice | 33,293 | 7,850 | 8,457 | 32,686 | 6,230 | 26,456 |
| Unamortized bond premium | 59,247 | 3,083 | 7,093 | 55,237 | 6,910 | 48,327 |
| Unemployment compensation | 563 | 634 | 751 | 446 | 446 | — |
| Workers' compensation | 22,604 | 5,016 | 6,513 | 21,107 | 6,273 | 14,834 |
| Other | 15,908 | 22,007 | 14,151 | 23,764 | 3,759 | 20,005 |
| Total other liabilities | <u>184,716</u> | <u>92,908</u> | <u>88,857</u> | <u>188,767</u> | <u>36,745</u> | <u>152,022</u> |
| Total | <u>\$ 1,228,371</u> | <u>\$ 169,628</u> | <u>\$ 196,483</u> | <u>\$ 1,201,516</u> | <u>\$ 89,045</u> | <u>\$ 1,112,471</u> |

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 | Noncurrent 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 |
| 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>173,146</u> | <u>93,068</u> | <u>81,498</u> | <u>184,716</u> | <u>34,200</u> | <u>150,516</u> |
| Total | <u>\$ 1,103,589</u> | <u>\$ 256,081</u> | <u>\$ 131,299</u> | <u>\$ 1,228,371</u> | <u>\$ 102,069</u> | <u>\$ 1,126,302</u> |

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 consists of general receipts bonds and general receipts notes in the original amount of \$1.21 billion dated October 6, 2006 through February 21, 2017, 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, General Receipts 2014 Bonds Series C and General Receipts 2017 Bonds Series A and B, totaling \$852.0 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 21, 2017, approximately \$36.8 million of University of Kentucky General Receipts 2017 Bonds Series A and B at a true interest cost of 1.6% and 1.9%, respectively, were issued for the purpose of fully refunding General Receipts 2006 Notes Series A and General Receipts 2010 Bonds Series A.

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 for both fiscal years 2017 and 2016, 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, President Barack Obama signed an executive order reducing the budgetary authority in accounts subject to sequestration. As a result, the BAB subsidy was reduced to approximately 33% in 2017 and 2016. The QECB subsidy was reduced to approximately 72% and 74% in 2017 and 2016, respectively.

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, 2017, are as follows (in thousands):

| | Principal | Interest | Total |
|-----------|---------------------|-------------------|---------------------|
| 2018 | \$ 52,300 | \$ 42,355 | \$ 94,655 |
| 2019 | 48,505 | 40,414 | 88,919 |
| 2020 | 50,086 | 38,439 | 88,525 |
| 2021 | 49,173 | 36,343 | 85,516 |
| 2022 | 49,352 | 34,146 | 83,498 |
| 2023-2027 | 280,058 | 141,903 | 421,961 |
| 2028-2032 | 142,440 | 87,037 | 229,477 |
| 2033-2037 | 130,445 | 59,747 | 190,192 |
| 2038-2042 | 132,470 | 31,134 | 163,604 |
| 2043-2046 | 77,920 | 6,591 | 84,511 |
| Total | <u>\$ 1,012,749</u> | <u>\$ 518,109</u> | <u>\$ 1,530,858</u> |

At June 30, 2017, assets with a fair market value of approximately \$109.8 million have been placed on deposit with trustees to totally defease bonds with a par amount of approximately \$107.6 million. The liability for these fully defeased bonds is not included in the financial statements.

8. DEFERRED INFLOWS OF RESOURCES

As of June 30, 2017 and 2016, deferred inflows of resources are as follows (in thousands):

| | 2017 | 2016 |
|---|-------------------|-------------------|
| Aramark service concession arrangement | \$ 131,465 | \$ 140,306 |
| Barnes and Noble service concession arrangement | 3,245 | 4,084 |
| EdR service concession arrangement | 299,019 | 222,356 |
| Total | <u>\$ 433,729</u> | <u>\$ 366,746</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, Phase II-B and Phase II-C, which opened in August 2014, August 2015 and August 2016 respectively, included the development of 10 residence halls at a cost of \$321.2 million. The residence halls are reported as a capital asset with a carrying value of \$311.9 million at June 30, 2017 and deferred inflows of resources in the amount of \$299.0 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 III-A for the construction of one residence hall at an approximate cost of \$74.0 million opening in August 2017. This is a 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 new 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 \$58.1 million at June 30, 2017 and deferred inflows of resources in the amount of \$49.9 million pursuant to the service concession arrangement. The present value of the guaranteed minimum payments over the remaining 12 years of the contract is reported as a receivable of \$83.8 million and deferred inflows of resources in the amount of \$81.6 million pursuant to the service concession arrangement.

In June 2015, the University entered into a contract with Barnes and Noble College Booksellers, LLC (Barnes and Noble) to operate and provide services for the bookstore for 10 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 13 years of the contract period is reported as a receivable of \$3.4 million and deferred inflows of resources in the amount of \$3.2 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, 2017 and 2016, restricted expendable net position is composed of the following (in thousands):

| | 2017 | 2016 |
|--|------------|------------|
| Appreciation on permanent endowments | \$ 166,647 | \$ 123,005 |
| Term endowments | 7,880 | 7,432 |
| Quasi-endowments initially funded with restricted assets | 127,641 | 50,090 |
| Funds restricted for capital projects and debt service | 170,433 | 186,185 |
| Funds restricted for noncapital purposes | 62,785 | 115,987 |
| Loan funds (primarily University funds required for federal match) | 12,111 | 11,455 |
| Total | \$ 547,497 | \$ 494,154 |

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 with outside parties. Commitments for the use of unrestricted net position as of June 30, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|--|---------------------|---------------------|
| Working capital requirements | \$ 70,929 | \$ 92,944 |
| Designated for future year fiscal operations | 232,551 | 209,665 |
| Designated for capital projects | 37,987 | 43,930 |
| Designated for renewal and replacement of capital assets | 59,605 | 52,368 |
| UK HealthCare Hospital System | 693,070 | 647,928 |
| Affiliated corporations and component units | 58,337 | 56,801 |
| Total | <u>\$ 1,152,479</u> | <u>\$ 1,103,636</u> |

11. PLEDGED REVENUES

Pledged revenues for the years ended 2017 and 2016 as defined by the General Receipts Trust Indenture, are as follows (in thousands):

| | 2017 | 2016 |
|---|---------------------|---------------------|
| Student tuition and fees | \$ 339,665 | \$ 319,627 |
| Nongovernmental grants and contracts | 1,217 | 1,145 |
| Recoveries of facilities and administrative costs | 54,507 | 51,088 |
| Sales and services | 50,696 | 49,399 |
| Hospital services | 1,492,388 | 1,417,243 |
| Auxiliary enterprises - housing and dining | 37,578 | 39,103 |
| Auxiliary enterprises - athletics | 102,341 | 102,995 |
| Auxiliary enterprises - other | 52,278 | 49,434 |
| Other operating revenue | 825 | 838 |
| State appropriations | 267,029 | 279,611 |
| Gifts and grants | 4,350 | 4,583 |
| Investment income (loss) | 10,969 | 10,761 |
| Total | <u>\$ 2,413,843</u> | <u>\$ 2,325,827</u> |

The University has substantially pledged all of the unrestricted operating and nonoperating revenues to repay the general receipts bonds and notes issued during 2006 to 2017. 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 \$1.40 billion and \$1.47 billion in fiscal years 2017 and 2016, respectively. Principal and interest paid for fiscal years 2017 and 2016 was \$70.8 million and \$64.6 million, respectively.

12. INVESTMENT INCOME (LOSS)

Components of investment income (loss) for the years ended June 30, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|---|-------------------|-------------------|
| Interest and dividends earned on endowment investments | \$ 17,170 | \$ 14,497 |
| Realized and unrealized gains (losses) on endowment investments | 88,995 | (26,808) |
| Interest and dividends on cash and non-endowment investments | 9,381 | 7,463 |
| Realized and unrealized gains (losses) on non-endowment investments | (3,120) | (49) |
| Investment income from external trusts | 1,592 | 1,656 |
| Total | <u>\$ 114,018</u> | <u>\$ (3,241)</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, 2017 and 2016, the University received income from these trusts of approximately \$1.6 million and \$1.7 million, respectively. The market value of the external trust assets as of June 30, 2017 and 2016 was approximately \$40.1 million and \$37.4 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. For the years ended June 30, 2017 and 2016, the University received income from these self-administered trusts of approximately \$87,000 and \$42,000, respectively. The market value of the self-administered trusts as of June 30, 2017 and 2016 was approximately \$1.9 million and \$1.8 million, respectively, and included in endowment investments.

14. GRANTS AND CONTRACTS AWARDED

At June 30, 2017 and 2016, grants and contracts of approximately \$226.5 million and \$201.4 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 fiscal years 2017 and 2016 were approximately \$112.6 million and \$107.1 million, respectively. Employees contributed approximately \$56.2 million in fiscal year 2017 and \$53.3 million in fiscal year 2016. The University's total payroll costs were approximately \$1.46 billion and \$1.37 billion for the years ended June 30, 2017 and 2016, respectively. The payroll for employees covered by the retirement plan was approximately \$1.44 billion and \$1.07 billion for the years ended June 30, 2017 and 2016, respectively.

Regular full-time KMSF employees become eligible to participate in a defined contribution plan on the employee's regular full-time hire date coinciding with or next following attainment of age 20 1/2. KMSF contributes 10% of the employee's earnings and employees do not contribute to this plan. KMSF contributions for 2017 and 2016 were approximately \$1.0 million and \$863,000, respectively. The total payroll costs for employees covered by the defined contribution plan were approximately \$9.7 million and \$8.7 million for the years ended June 30, 2017 and 2016, respectively. Participants become vested in the plan according to years of service, with 100% vesting after one year of service.

16. UNIVERSITY OF KENTUCKY OTHER POSTEMPLOYMENT BENEFIT (OPEB) PLAN TRUST

The University's OPEB plan is administered through the University's OPEB trust fund as an irrevocable trust. The single-employer defined benefit OPEB plan provides medical and prescription drug benefits. The trust is not a separate legal entity and is governed by the University's Board.

The plan provides lifetime health care 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 health care 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 actuarial valuation as of July 1, 2017 was based upon the following plan members as of January 1, 2017:

| | |
|--|--------------|
| Inactive members receiving benefits | 3,119 |
| Inactive members entitled not yet receiving benefits | 351 |
| Active plan members | 5,660 |
| Total plan members | <u>9,130</u> |

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 2017, the University contributed \$24.0 million to the plan. Plan members receiving benefits contributed 31.6% of the premium costs, an average for combined single and family coverage. In fiscal year 2017, total member contributions were approximately \$5.5 million.

The OPEB plan follows the deposit and investment policies established by the University's Board of Trustees. Such policies are developed to establish and maintain sound financial management practices for the investment and management of the OPEB funds. The fair value of deposits and investments, by statement of net position classification, at June 30, 2017 and 2016 are as follows (in thousands):

| | <u>2017</u> | <u>2016</u> |
|---|-------------------|-------------------|
| <u>Statement of Fiduciary Net Position classification</u> | | |
| Cash and cash equivalents | \$ 1,460 | \$ 205 |
| Investments | <u>142,484</u> | <u>119,807</u> |
| Total deposits and investments | <u>\$ 143,944</u> | <u>\$ 120,012</u> |

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 generally accepted accounting principles 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 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 Statements of Net Position.

The OPEB has the following valuation measurements, by type, at June 30, 2017 and 2016 (in thousands):

| 2017 | | | | | | | |
|---|--|---|---|------------------------------|-----------------------|------------------------------|-----------------|
| Fair Value Measurement Using | | | | | | | |
| Total value | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total measured at fair value | Net asset value (NAV) | Amortized or historical cost | |
| Cash and cash equivalents | \$ 2,009 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 2,009 |
| Diversifying strategies | 26,829 | — | — | — | — | 26,829 | — |
| Global equity - hedged fund | 11,872 | — | — | — | — | 11,872 | — |
| Global equity - international | 19,712 | 3,800 | 109 | 1 | 3,910 | 15,802 | — |
| Global equity - private | 20,234 | — | — | 78 | 78 | 20,156 | — |
| Global equity - U.S. | 13,524 | 732 | 154 | — | 886 | 12,638 | — |
| Global fixed income - high quality/rate sensitive | 11,692 | 4,225 | 5,562 | — | 9,787 | 1,905 | — |
| Global fixed income - private credit | 4,327 | — | — | — | — | 4,327 | — |
| Global fixed income - public credit | 6,905 | 3 | 248 | — | 251 | 6,654 | — |
| Real assets - private | 13,665 | — | — | — | — | 13,665 | — |
| Real assets - public | 13,175 | 4,268 | — | — | 4,268 | 8,907 | — |
| Total deposits and investments | \$ 143,944 | \$ 13,028 | \$ 6,073 | \$ 79 | \$ 19,180 | \$ 122,755 | \$ 2,009 |

| 2016 | | | | | | | |
|---|--|---|---|------------------------------|-----------------------|------------------------------|-----------------|
| Fair Value Measurement Using | | | | | | | |
| Total value | Quoted prices in active markets for identical assets (Level 1) | Significant other observable inputs (Level 2) | Significant unobservable inputs (Level 3) | Total measured at fair value | Net asset value (NAV) | Amortized or historical cost | |
| Cash and cash equivalents | \$ 1,078 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 1,078 |
| Diversifying strategies | 19,438 | — | — | — | — | 19,438 | — |
| Global equity - hedged fund | 16,186 | — | — | — | — | 16,186 | — |
| Global equity - international | 16,646 | 3,385 | 69 | 1 | 3,455 | 13,191 | — |
| Global equity - private | 17,022 | — | — | 80 | 80 | 16,942 | — |
| Global equity - U.S. | 16,259 | 629 | 138 | — | 767 | 15,492 | — |
| Global fixed income - high quality/rate sensitive | 4,482 | — | 2,343 | — | 2,343 | 2,139 | — |
| Global fixed income - private credit | 2,410 | — | — | — | — | 2,410 | — |
| Global fixed income - public credit | 4,920 | — | 290 | — | 290 | 4,630 | — |
| Real assets - private | 12,936 | — | — | — | — | 12,936 | — |
| Real assets - public | 8,635 | 3,838 | — | — | 3,838 | 4,797 | — |
| Total deposits and investments | \$ 120,012 | \$ 7,852 | \$ 2,840 | \$ 81 | \$ 10,773 | \$ 108,161 | \$ 1,078 |

Cash on deposit with the University, included in cash and cash equivalents above, is managed based on the University's Operating Fund Investment Policy established by the Treasurer of the University. All other OPEB trust investments are managed within guidelines established by the University's Endowment Investment Policy, as approved by the Investment Committee of the University's Board, which governs the University's pooled endowment fund. Significant investment policy changes occurred during the fiscal year ended June 30, 2017, including adoption of new asset allocation targets and ranges; adoption of liquidity tiers and related guidelines; and adoption of an alternative search process for investment managers intended to have long-term role in the portfolio.

The OPEB's deposits and investments are exposed to various risks. 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.

Endowment managers are permitted to use derivative instruments to limit credit risk, interest rate risk and foreign currency risk. For more information regarding the policies in place to mitigate these and other risks see note 2.

The following reflects the approved asset allocation as of June 30, 2017:

| Asset Category | Target Allocation |
|-------------------------|-------------------|
| Diversifying strategies | 20% |
| Global equity | 40% |
| Global fixed income | 20% |
| Real assets | 20% |

The components of the net OPEB liability of the University at June 30, 2017, were as follows (in thousands):

| | |
|---|-------------------|
| Total OPEB liability | \$ 376,521 |
| Plan fiduciary net position | (143,944) |
| University of Kentucky net OPEB liability | <u>\$ 232,577</u> |

Plan fiduciary net position as a percentage of the total OPEB liability 38.2%

The University adopted GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* during the year ended June 30, 2017. Statement No. 74, among other things, requires changes in OPEB plan financial statements, footnote disclosures and required supplemental information and is applicable to the University's OPEB plan financial statements. Because of the differences in reporting requirements under GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which is not yet effective for the University, and under GASB Statement No. 45, amounts reported and disclosures herein under the two pronouncements will differ. The amount of net OPEB liability equals the difference between the plan fiduciary net position and total OPEB liability. The net OPEB obligation in note 18 is calculated reflecting GASB Statement No. 45. The amount of net OPEB obligation in note 18 equals the cumulative difference between plan contribution and the annual OPEB cost.

The total OPEB liability in the July 1, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | |
|------------------------|---|
| Health Care trend rate | Post-65 10.5% for 2017, decreasing .5% per year to an ultimate rate of 5%. Pre-65 8.25%, decreasing .31% - .39% per year to an ultimate rate of 2.20% in 2022. |
| Salary Scale | 3% per year |
| Discount rate | 7.5% based on the University's funding policy and the expected long-term nominal return on the separate trust assets that will be used to finance the payment of plan benefits. The University has stated a funding policy to contribute an amount to the segregated and protected trust fund, such that the assets available will always be sufficient to cover the expected benefit payments. |
| Mortality | Aggregate base rates for healthy lives from the Retirement Plan-2014 mortality study with a fully generational projection from 2006 using scale Mortality Plan-2016. |
| Plan participation | 80% elect coverage |

The actuarial assumptions used in the July 1, 2017 valuation were based on the results of an actuarial experience study for the period July 1, 2016 to June 30, 2017.

The annual money-weighted rate of return on the OPEB plan investments, net of OPEB plan investment expense was 10.3% for the year ended June 30, 2017. The money-weighted rate of return expresses investment performance, net of investment expenses, adjusted for the changing amounts actually invested.

The long-term expected rate of return on OPEB plan investments was determined using efficient frontier modeling software for Monte Carlo simulations that analyze risk, return and the probability of meeting return objectives over multi-year periods. The modeling, which incorporates forward-looking return forecasts as well as historical risk and correlation data, identifies portfolios with the highest expected return at each level of risk.

The following reflects the expected rates of return, presented as geometric means, by asset allocation as of June 30, 2017:

| Asset Category | Long-term Expected Real Rate of Return |
|-------------------------|--|
| Diversifying strategies | 3.3% |
| Global equity | 6.7% |
| Global fixed income | 3.3% |
| Real assets | 7.2% |

The following presents the net OPEB liability of the University, as well as what the University's net OPEB liability would be if it were calculated using a discount rate that is one-percentage-point lower (6.5%) or one-percentage-point higher (8.5%) than the current discount rate (in thousands):

| | 1% Decrease (6.5%) | Current Rate (7.5%) | 1% Increase (8.5%) |
|-----------------------------|-----------------------|------------------------|-----------------------|
| Total OPEB liability | \$ 433,788 | \$ 376,521 | \$ 330,017 |
| Plan fiduciary net position | (143,944) | (143,944) | (143,944) |
| Net OPEB liability | <u>\$ 289,844</u> | <u>\$ 232,577</u> | <u>\$ 186,073</u> |

The following presents what the net OPEB liability would be if it was calculated using health care cost trend rate that is one-percentage-point lower or one-percentage-point higher than the current health care cost trend rates (in thousands):

| | 1% Decrease | Trend Rate | 1% Increase |
|-----------------------------|-------------------|-------------------|-------------------|
| Total OPEB liability | \$ 326,436 | \$ 376,521 | \$ 438,623 |
| Plan fiduciary net position | (143,944) | (143,944) | (143,944) |
| Net OPEB liability | <u>\$ 182,492</u> | <u>\$ 232,577</u> | <u>\$ 294,679</u> |

17. UNIVERSITY OF KENTUCKY LONG TERM DISABILITY (LTD) PLAN TRUST

The University of Kentucky LTD plan is administered through the University's LTD trust fund as an irrevocable trust. The trust pays claims and establishes necessary reserves. The trust is not a separate legal entity and is governed by the University's Board. The coverage of the LTD benefits is established and may be amended by the President of the University.

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 actuarial valuation as of July 1, 2017 was based upon the following plan participants as of January 1, 2017:

| | |
|--|-----------|
| Disabled members | |
| Count of members | 146 |
| Average age at valuation date | 56.1 |
| Average duration since disability (in years) | 9.2 |
| Average monthly income net benefit | \$ 610.16 |
| Active (healthy) members | |
| Count of members | 17,919 |
| Average age at valuation date | 43.3 |
| Average years of service | 8.9 |

The contribution requirements of the University are established and may be amended by the President of the University. The University contributes to the LTD trust based on an actuarially determined rate. For the year ended June 30, 2017 the University's contribution was approximately \$2.0 million.

LTD Trust investment policy guidelines are established by the LTD Employee Benefits Amended and Restated Trust Agreement. Investment objectives and targeted asset allocations are reviewed and approved by the University Treasurer. Investment objectives and asset allocations are developed to establish and maintain sound financial management practices for the investment and management of LTD funds. There were no significant investment policy changes during the fiscal year ended June 30, 2017.

The fair value of deposits and investments, by statement of net position classification, at June 30, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|---|------------------|------------------|
| <u>Statement of Fiduciary Net Position classification</u> | | |
| Cash and cash equivalents | \$ 818 | \$ 492 |
| Investments | 17,961 | 16,137 |
| Total deposits and investments | <u>\$ 18,779</u> | <u>\$ 16,629</u> |

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 generally accepted accounting principles 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 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 Statements of Net Position.

The LTD trust has the following valuation measurements, by type, at June 30, 2017 and 2016 (in thousands):

| | 2017 | | | |
|-------------------------------------|------------------------------|--|------------------------------|------------------------------|
| | Fair Value Measurement Using | | | |
| | Total value | Quoted prices in active markets for identical assets (Level 1) | Total measured at fair value | Amortized or historical cost |
| Cash and cash equivalents | \$ 818 | \$ — | \$ — | \$ 818 |
| Global equity - international | 1,684 | 1,684 | 1,684 | — |
| Global equity - U.S. | 9,944 | 9,944 | 9,944 | — |
| Global fixed income - public credit | 6,333 | 6,333 | 6,333 | — |
| Total deposits and investments | <u>\$ 18,779</u> | <u>\$ 17,961</u> | <u>\$ 17,961</u> | <u>\$ 818</u> |

| | 2016 | | | |
|-------------------------------------|------------------------------|--|------------------------------|------------------------------|
| | Fair Value Measurement Using | | | |
| | Total value | Quoted prices in active markets for identical assets (Level 1) | Total measured at fair value | Amortized or historical cost |
| Cash and cash equivalents | \$ 492 | \$ — | \$ — | \$ 492 |
| Diversifying strategies | 47 | 47 | 47 | — |
| Global equity - international | 1,919 | 1,919 | 1,919 | — |
| Global equity - U.S. | 8,301 | 8,301 | 8,301 | — |
| Global fixed income - public credit | 5,719 | 5,719 | 5,719 | — |
| Real assets - public | 151 | 151 | 151 | — |
| Total deposits and investments | <u>\$ 16,629</u> | <u>\$ 16,137</u> | <u>\$ 16,137</u> | <u>\$ 492</u> |

The LTD trust investments are exposed to various risks. Due to the level of risk associated with certain investments 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.

The Trustee of the LTD trust diversifies the investments to minimize the risk of losses due to credit risk, interest rate risk, currency and other risks, as appropriate, based on market conditions. At June 30, 2017, the LTD trust had no underlying investments in any one issuer which represented more than five percent of total investments, other than U.S. Treasury and agency obligations, as a way to limit concentration of credit risks. For a description of credit, interest rate, foreign currency and concentration of credit risks see note 2.

The following reflects the approved asset allocation as of June 30, 2017:

| <u>Asset Category</u> | <u>Target Allocation</u> |
|-------------------------|--------------------------|
| Diversifying strategies | 5.0% |
| Global equity | 57.5% |
| Global fixed income | 37.5% |

The annual money-weighted rate of return on the LTD plan investments, net of LTD plan investment expense was 12.0% for the year ended June 30, 2017. The money weighted rate of return expresses investment performance, net of investment expenses, adjusted for the changing amounts actually invested.

The long-term expected rate of return on LTD plan investments was determined by combining market-implied equilibrium returns with the Trustee's subjective views using a Black-Litterman technique.

The following reflects the expected rates of return, presented as arithmetic means, by asset allocation as of June 30, 2017:

| <u>Asset Category</u> | <u>Long-term Expected Real Rate of Return</u> |
|-------------------------|---|
| Diversifying strategies | 5.8% |
| Global equity | 5.5% |
| Global fixed income | 0.8% |

The total LTD liability in July 1, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | |
|--|---|
| Discount rate | 6.5% based on the University's funding policy and the expected long-term nominal return on the separate trust assets that will be used to finance the payment of plan benefits. The University has stated a funding policy to contribute an amount to the segregated and protected trust fund, such that the assets available will always be sufficient to cover the expected benefit payments. |
| Elimination period | 6 month |
| Termination (mortality and recovery from disability) | 2012 Society of Actuaries (SOA) group long-term disability table |
| Mortality (only for life benefit) | Canadian Institute of Actuaries (CIA) 1988-94 LTD table |
| Incidence of disability | Gender and age-related disability incidence rates based on 1987 Commissioner's Group Long-term Disability table |
| Duration of payment | Payments are assumed to be made until the later of i) age 65 and ii) five years after date of disability |
| LTD income benefit | |
| Disability benefit | Actual net benefit currently being paid (if currently disabled) |
| Social Security offset | Assume that 90% of the members who have been disabled for less than 24 months and currently not entitled to a Social Security offset will immediately receive an offset |
| Future salary increase for active members | 3% |

The actuarial assumptions used in the July 1, 2017 valuation were based on the results of an actuarial experience study for the period July 1, 2016 to June 30, 2017.

The components of the net OPEB liability of the University at June 30, 2017, were as follows (in thousands):

| | |
|---|-----------------|
| Total OPEB liability | \$ 22,780 |
| Plan fiduciary net position | (18,784) |
| University of Kentucky net OPEB liability | <u>\$ 3,996</u> |

Plan fiduciary net position as a percentage of the total OPEB liability 82.5%

The University adopted GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* during the year ended June 30, 2017. Statement No. 74, among other things, requires changes in OPEB plan financial statements, footnote disclosures and required supplemental information and is applicable to the University's OPEB plan financial statements. Because of the differences in reporting requirements under GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which is not yet effective for the University, and under GASB Statement No. 45, amounts reported and disclosures herein under the two pronouncements will differ. The amount of net OPEB liability equals the difference between the plan fiduciary net position and total OPEB liability. The net OPEB obligation in note 19 is calculated reflecting GASB Statement No. 45. The amount of net OPEB obligation in note 19 equals the cumulative difference between plan contribution and the annual OPEB cost.

The following presents the net OPEB liability of the University, as well as what the University's net OPEB liability would be if it were calculated using a discount rate that is one- percentage-point lower (5.5%) or one-percentage-point higher (7.5%) than the current discount rate (in thousands):

| | 1% Decrease (5.5%) | Current Rate (6.5%) | 1% Increase (7.5%) |
|-----------------------------|-----------------------|------------------------|-----------------------|
| Total OPEB liability | \$ 23,849 | \$ 22,780 | \$ 21,757 |
| Plan fiduciary net position | (18,784) | (18,784) | (18,784) |
| Net OPEB liability | <u>\$ 5,065</u> | <u>\$ 3,996</u> | <u>\$ 2,973</u> |

18. HEALTH INSURANCE BENEFITS FOR RETIREES

As described in note 16, the University administers a single-employer defined benefit health care plan including medical and prescription drug benefits.

The University established a trust fund in November 2007 to segregate plan assets, and contributed amounts during the fiscal years 2008 -2017 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 current ARC of \$24.5 million is 4.9% of annual covered payroll. There are no long-term contracts for contributions to the plan.

As of June 30, 2017, the Plan's actuary applied the requirements of GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans* and GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* in preparing the actuarial valuation. These statements changed the actuarial cost method from Projected Unit Credit to Entry Age Normal. Also as required by GASB No. 75, the amortization of liability gain/loss and assumption changes changed from a closed 30 years to the Average Future Working Life Expectancy; the amortization of plan changes changed from a closed 30 years to an immediate recognition; and the amortization of asset gain/loss from a closed 30 years to a closed 5 years. The total OPEB liability in note 16 differs from the actuarially accrued liability discussed below by these differences.

The following table presents the components of the University's OPEB cost for the year under GASB Statement No. 45, the amount contributed and changes in the OPEB Plan for fiscal year 2017 (in thousands):

| | |
|--|-----------------|
| Annual required contribution | \$ 24,454 |
| Contributions made | (23,987) |
| Increase (decrease) in net OPEB obligation/(asset) | 467 |
| Net OPEB obligation/(asset) - beginning of year | (1,019) |
| Net OPEB obligation/(asset) - end of year | <u>\$ (552)</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 2017, 2016 and 2015 are as follows (in thousands):

| Fiscal Year Ended | Annual OPEB Cost | Percentage of Annual OPEB Cost Contributed | Net OPEB Obligation/(Asset) |
|-------------------|------------------|--|-----------------------------|
| 6/30/2015 | \$20,395 | 100.7% | (\$387) |
| 6/30/2016 | \$23,741 | 102.7% | (\$1,019) |
| 6/30/2017 | \$24,454 | 98.1% | (\$552) |

As of July 1, 2017, the actuarial accrued liability (AAL) under GASB Statement No. 45 for benefits was \$343.5 million, with an actuarial value of assets of \$143.9 million, resulting in an UAAL of \$199.5 million. The covered payroll (annual payroll of active employees covered by the plan) was \$494.2 million and the ratio of the UAAL to the covered payroll was 40.4% at June 30, 2017. The University implemented the University of Kentucky OPEB Trust in July 2007, after the July 1, 2007 actuarial valuation date. As of June 30, 2017, net trust fund assets totaled \$143.9 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 health care 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 health care 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 health care 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, 2016 was 21 years.

19. LONG-TERM DISABILITY BENEFIT

As described in note 17, the University is self-funded for a LTD benefit plan and has established a trust for the purpose of paying claims and establishing necessary reserves.

The University contributed amounts during fiscal years 2008-2017 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 current ARC of \$2.0 million is 0.2% of annual covered payroll. There are no long-term contracts for contributions to the plan.

As of June 30, 2017, the Plan's actuary applied the requirements of GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans* and GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* in preparing the actuarial valuation. These statements changed the actuarial cost method from Projected Unit Credit to Entry Age Normal. Also, as required by GASB Statement No. 75, the amortization of liability gain/loss and assumption changes changed from a closed 30 years to the Average Future Working Life Expectancy; the amortization of plan changes changed from a closed 30 years to an immediate recognition; and the amortization of asset gain/loss changed from a closed 30 years to a closed five years. The total OPEB liability in note 17 differs from the actuarially accrued liability discussed below by these differences.

The following table presents the components of the OPEB cost under GASB Statement No. 45, the amount contributed and changes in the OPEB plan for fiscal year 2017 (in thousands):

| | | |
|--|----|---------|
| Annual required contribution | \$ | 1,984 |
| Contributions made | | (2,020) |
| Increase (decrease) in net OPEB obligation/(asset) | | (36) |
| Net OPEB obligation/(asset) - beginning of year | | (1) |
| Net OPEB obligation/(asset) - end of year | \$ | (37) |

The University's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation/(asset) for fiscal year 2017, 2016 and 2015 are as follows (in thousands):

| Fiscal Year Ended | Annual OPEB Cost | Percentage of Annual OPEB Cost Contributed | Net OPEB Obligation/(Asset) |
|-------------------|------------------|--|-----------------------------|
| 6/30/2015 | \$2,203 | 99.7% | \$2 |
| 6/30/2016 | \$1,926 | 100.2% | (\$1) |
| 6/30/2017 | \$1,984 | 101.8% | (\$37) |

As of July 1, 2017, the AAL for benefits under GASB Statement No. 45 was \$25.3 million and the actuarial value of assets was \$18.8 million, resulting in an UAAL of \$6.5 million. The July 1, 2017 valuation reflects updates in mortality rates to better anticipate future experience under the plan. The covered payroll (annual payroll of active employees covered by the plan) was \$941.0 million and the ratio of the UAAL to the covered payroll was 0.7% at June 30, 2017.

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% |
| 12-23 | 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, 2016 was 21 years.

20. 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 \$5,000 and \$1.0 million per occurrence. Losses in excess of \$1.0 million are insured by commercial carriers up to \$1.50 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 \$250,000 for any one person or \$400,000 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 fiscal years 2016 to 2017. 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, 2017 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, 2017.

The University also self-insures certain employee benefits, including health insurance, workers' compensation and unemployment claims to the extent not covered by insurance. The University has recorded an estimate for asserted claims at June 30, 2017.

21. 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.

22. 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, 2017 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, 2017, all private gifts and pledges matched by the RCTF program have been received.

23. 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, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|---|-----------------|-----------------|
| Funds from private sources approved for match | \$ 7,480 | \$ 7,761 |
| Cigarette excise tax funds distributed | 1,907 | 1,925 |
| Total cancer research matching fund revenues | <u>\$ 9,387</u> | <u>\$ 9,686</u> |
| Cancer research matching fund expenses | <u>\$ 8,669</u> | <u>\$ 7,524</u> |

24. NATURAL CLASSIFICATION

The University's operating expenses by natural classification for the years ended June 30, 2017 and 2016 are as follows (in thousands):

| | 2017 | 2016 |
|--|---------------------|---------------------|
| Salaries and wages | \$ 1,471,564 | \$ 1,382,346 |
| Employee benefits | 396,090 | 365,932 |
| Supplies and services | 761,953 | 740,199 |
| Depreciation | 151,445 | 148,109 |
| Student scholarships and financial aid | 64,862 | 60,477 |
| Purchased utilities | 50,661 | 49,421 |
| Other, various | 141,321 | 141,555 |
| Total | <u>\$ 3,037,896</u> | <u>\$ 2,888,039</u> |

25. COMBINED CONDENSED STATEMENTS

The University of Kentucky and its blended component units' condensed statements for the years ended June 30, 2017 and 2016 are summarized as follows (in thousands):

UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
COMBINED CONDENSED STATEMENT OF NET POSITION AS OF JUNE 30, 2017
(in thousands)

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

| | UK | Research Foundation | Gluck Equine Research Foundation | Humanities Foundation | Mining Engineering Foundation | Center on Aging Foundation | Central Kentucky Management Services | Kentucky Medical Services Foundation | Eliminations | Total |
|--|--------------|---------------------|----------------------------------|-----------------------|-------------------------------|----------------------------|--------------------------------------|--------------------------------------|--------------|--------------|
| Current Assets | | | | | | | | | | |
| Cash and cash equivalents | \$ 620,418 | \$ 62,975 | \$ 60 | \$ 59 | \$ 23 | \$ 310 | \$ 816 | \$ 32 | \$ — | \$ 684,693 |
| Notes, loans and accounts receivable, net | 297,643 | 32,358 | — | — | — | — | 379 | 48,109 | (50,878) | 327,611 |
| Investments | — | — | — | — | — | — | — | 6,794 | — | 6,794 |
| Inventories and other assets | 49,611 | 2,789 | — | — | — | — | 18 | 451 | (90) | 52,779 |
| Total current assets | 967,672 | 98,122 | 60 | 59 | 23 | 310 | 1,213 | 55,386 | (50,968) | 1,071,877 |
| Noncurrent Assets | | | | | | | | | | |
| Restricted cash and cash equivalents | 240,979 | 2 | — | — | — | — | — | — | — | 240,981 |
| Endowment investments | 1,242,255 | 13,888 | 8,956 | 1,385 | 1,932 | — | — | — | — | 1,268,396 |
| Other long-term investments | 234,640 | 765 | — | — | — | — | — | 42,816 | (241) | 277,980 |
| Notes, loans and accounts receivable, net | 300,876 | 35 | — | — | — | — | — | 772 | — | 301,683 |
| Other noncurrent assets | 772 | — | — | — | — | — | — | — | (361) | 411 |
| Capital assets, net | 2,926,963 | 8,611 | — | — | — | — | 62 | 97,790 | — | 3,033,426 |
| Total noncurrent assets | 4,946,485 | 23,281 | 8,956 | 1,385 | 1,932 | 310 | 62 | 141,378 | (602) | 5,122,877 |
| Total assets | 5,914,157 | 121,403 | 9,016 | 1,444 | 1,955 | 310 | 1,275 | 196,764 | (51,570) | 6,194,754 |
| 10,808 | — | — | — | — | — | — | — | — | — | 10,808 |
| 5,924,965 | 121,403 | 9,016 | 1,444 | 1,955 | 310 | 1,275 | 196,764 | (51,570) | 6,205,562 | |
| Deferred Outflows of Resources | | | | | | | | | | |
| Total assets and deferred outflows of resources | | | | | | | | | | |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | | | | | | | | |
| Current Liabilities | | | | | | | | | | |
| Accounts payable and accrued liabilities | 330,826 | 6,478 | — | — | — | 33 | 1,213 | 96,341 | (99,248) | 335,643 |
| Unearned revenue | 56,273 | 32,925 | — | — | — | — | — | 2,633 | (451) | 91,380 |
| Long-term liabilities - current portion | 85,667 | — | — | — | — | — | — | 3,378 | — | 89,045 |
| Total current liabilities | 472,766 | 39,403 | — | — | — | 33 | 1,213 | 102,352 | (99,699) | 516,068 |
| Noncurrent Liabilities | | | | | | | | | | |
| Unearned revenue | 166,599 | — | — | — | — | — | — | — | — | 166,599 |
| Long-term liabilities | 1,051,856 | 384 | — | — | — | — | — | 60,231 | — | 1,112,471 |
| Total noncurrent liabilities | 1,218,455 | 384 | — | — | — | — | — | 60,231 | — | 1,279,070 |
| Total liabilities | 1,691,221 | 39,787 | — | — | — | 33 | 1,213 | 162,583 | (99,699) | 1,795,138 |
| 433,729 | — | — | — | — | — | — | — | — | — | 433,729 |
| 2,124,950 | 39,787 | — | — | — | — | 33 | 1,213 | 162,583 | (99,699) | 2,228,867 |
| 1,620,343 | 8,611 | — | — | — | — | — | 62 | 34,181 | — | 1,663,197 |
| Net investment in capital assets | | | | | | | | | | |
| Restricted | | | | | | | | | | |
| Nonexpendable | 606,794 | 840 | 4,607 | 618 | 663 | — | — | — | — | 613,522 |
| Expendable | 536,486 | 4,207 | 4,409 | 826 | 1,292 | 277 | — | — | — | 547,497 |
| Total restricted | 1,143,280 | 5,047 | 9,016 | 1,444 | 1,955 | 277 | — | — | — | 1,161,019 |
| Unrestricted | 1,036,392 | 67,958 | — | — | — | — | — | — | — | 1,104,350 |
| Total net position | \$ 3,800,015 | \$ 81,616 | \$ 9,016 | \$ 1,444 | \$ 1,955 | \$ 277 | \$ 62 | \$ 34,181 | \$ 48,129 | \$ 3,976,695 |

UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
COMBINED CONDENSED STATEMENT OF NET POSITION AS OF JUNE 30, 2016
(in thousands)

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

| | UK | Research Foundation | Gluck Equine Research Foundation | Humanities Foundation | Mining Engineering Foundation | Center on Aging Foundation | Central Kentucky Management Services | Kentucky Medical Services Foundation | Eliminations | Total |
|--|------------|---------------------|----------------------------------|-----------------------|-------------------------------|----------------------------|--------------------------------------|--------------------------------------|--------------|------------|
| Current Assets | | | | | | | | | | |
| Cash and cash equivalents | \$ 636,815 | \$ 54,566 | \$ 338 | \$ 86 | \$ 26 | \$ 167 | \$ 1,493 | \$ 252 | \$ — | \$ 693,743 |
| Notes, loans and accounts receivable, net | 289,410 | 30,796 | — | — | — | — | 428 | 48,177 | (51,191) | 297,620 |
| Investments | — | — | — | — | — | — | — | 16,977 | — | 16,977 |
| Inventories and other assets | 46,357 | 3,889 | — | — | — | — | 18 | 370 | (174) | 50,460 |
| Total current assets | 952,582 | 89,251 | 338 | 86 | 26 | 167 | 1,939 | 65,776 | (51,365) | 1,058,800 |
| Noncurrent Assets | | | | | | | | | | |
| Restricted cash and cash equivalents | 398,364 | — | — | — | — | — | — | — | — | 398,364 |
| Endowment investments | 1,077,555 | 12,817 | 8,286 | 1,282 | 1,832 | — | — | — | — | 1,101,772 |
| 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 | 892 | — | — | — | — | — | — | — | (451) | 441 |
| Capital assets, net | 2,618,461 | 9,035 | — | — | — | — | 87 | 82,055 | — | 2,709,638 |
| Total noncurrent assets | 4,672,543 | 22,773 | 8,286 | 1,282 | 1,832 | — | 87 | 130,897 | (702) | 4,836,998 |
| Total assets | 5,625,125 | 112,024 | 8,624 | 1,368 | 1,858 | 167 | 2,026 | 196,673 | (52,067) | 5,895,798 |
| Total assets and deferred outflows of resources | 5,637,289 | 112,024 | 8,624 | 1,368 | 1,858 | 167 | 2,026 | 196,673 | (52,067) | 5,907,962 |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | | | | | | | | |
| Current Liabilities | | | | | | | | | | |
| Accounts payable and accrued liabilities | 315,240 | 10,436 | — | — | 8 | — | 1,939 | 111,763 | (112,569) | 326,817 |
| Unearned revenue | 44,642 | 32,784 | — | — | — | — | — | 2,847 | (625) | 79,648 |
| Long-term liabilities - current portion | 80,147 | — | — | — | — | — | — | 21,922 | — | 102,069 |
| Total current liabilities | 440,029 | 43,220 | — | — | 8 | — | 1,939 | 136,532 | (113,194) | 508,534 |
| Noncurrent Liabilities | | | | | | | | | | |
| Unearned revenue | 179,853 | — | — | — | — | — | — | — | — | 179,853 |
| Long-term liabilities | 1,101,853 | 404 | — | — | — | — | — | 24,045 | — | 1,126,302 |
| Total noncurrent liabilities | 1,281,706 | 404 | — | — | — | — | — | 24,045 | — | 1,306,155 |
| Total liabilities | 1,721,735 | 43,624 | — | — | 8 | — | 1,939 | 160,577 | (113,194) | 1,814,689 |
| Deferred inflows of Resources | | | | | | | | | | |
| Total liabilities and deferred inflows of resources | 366,746 | — | — | — | — | — | — | — | — | 366,746 |
| Total liabilities and deferred inflows of resources | 2,088,481 | 43,624 | — | — | 8 | — | 1,939 | 160,577 | (113,194) | 2,181,435 |
| NET POSITION | | | | | | | | | | |
| Net investment in capital assets | 1,481,816 | 9,035 | — | — | — | — | 87 | 36,096 | — | 1,527,034 |
| Restricted | | | | | | | | | | |
| Nonexpendable | 594,985 | 832 | 4,607 | 618 | 661 | — | — | — | — | 601,703 |
| Expendable | 484,048 | 3,983 | 4,017 | 750 | 1,189 | 167 | — | — | — | 494,154 |
| Total restricted | 1,079,033 | 4,815 | 8,624 | 1,368 | 1,850 | 167 | — | — | — | 1,095,857 |
| Unrestricted | 987,959 | 54,560 | — | — | — | — | — | — | 61,127 | 1,103,636 |
| Total net position | 3,548,808 | 68,400 | 8,624 | 1,368 | 1,850 | 167 | 87 | 36,096 | 61,127 | 3,726,527 |

**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, 2017
(in thousands)**

| | UK | Research Foundation | Gluck Equine Research Foundation | Humanities Foundation | Mining Engineering Foundation | Center on Aging Foundation | Central Kentucky Management Services | Kentucky Medical Services Foundation | Eliminations | Total |
|---|--------------|---------------------|----------------------------------|-----------------------|-------------------------------|----------------------------|--------------------------------------|--------------------------------------|--------------|--------------|
| OPERATING REVENUES | | | | | | | | | | |
| Student tuition and fees, net | \$ 339,665 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 339,665 |
| Federal grants and contracts | 1,464 | 180,424 | — | — | — | — | — | — | — | 181,888 |
| State and local grants and contracts | 80,387 | 16,881 | — | — | — | — | — | — | — | 97,268 |
| Nongovernmental grants and contracts | 275,420 | 32,078 | — | — | — | — | — | (274,203) | — | 33,295 |
| Recoveries of facilities and administrative costs | 328 | 54,179 | — | — | — | — | — | — | — | 54,507 |
| Sales and services | 49,909 | 1,716 | 1 | — | — | 20 | 32,534 | (33,484) | — | 50,696 |
| Federal appropriations | 16,332 | — | — | — | — | — | — | — | — | 16,332 |
| County appropriations | 24,906 | — | — | — | — | — | — | — | — | 24,906 |
| Professional clinical service fees | — | — | — | — | — | — | — | 241,062 | (5,801) | 235,261 |
| Hospital services | 1,499,955 | — | — | — | — | — | — | (7,567) | — | 1,492,388 |
| Auxiliary enterprises: | | | | | | | | | | |
| Housing and dining, net | 37,672 | — | — | — | — | — | — | — | (94) | 37,578 |
| Athletics | 102,341 | — | — | — | — | — | — | — | — | 102,341 |
| Other auxiliaries | 52,278 | — | — | — | — | — | — | — | — | 52,278 |
| Other operating revenues | 824 | — | — | — | — | 20 | 32,534 | (80,243) | — | 10,668 |
| Total operating revenues | 2,481,481 | 285,278 | 1 | — | — | 20 | 32,534 | 331,149 | (401,392) | 2,729,071 |
| OPERATING EXPENSES | | | | | | | | | | |
| Educational and general: | | | | | | | | | | |
| Instruction | 304,585 | 10,041 | — | 2 | 62 | — | — | — | (184) | 314,506 |
| Research | 102,956 | 176,409 | 8 | — | — | — | — | — | (3,285) | 276,088 |
| Public service | 191,936 | 70,618 | — | — | — | — | — | — | (75,975) | 186,579 |
| Libraries | 22,637 | — | — | — | — | — | — | — | — | 22,637 |
| Academic support | 79,782 | 3,505 | — | — | — | — | — | — | (170) | 83,117 |
| Student services | 40,022 | 10 | — | 1 | — | — | — | — | (82) | 39,951 |
| Institutional support | 61,981 | 792 | 9 | — | — | 104 | 32,534 | (32,690) | — | 62,730 |
| Operations and maintenance of plant | 83,992 | 4 | — | — | — | — | — | — | (3,335) | 80,661 |
| Student financial aid | 36,895 | 2,489 | — | 40 | — | — | — | — | — | 39,424 |
| Depreciation | 64,774 | 421 | — | — | — | — | 25 | — | — | 65,220 |
| Total educational and general | 989,560 | 264,289 | 17 | 43 | 62 | 104 | 32,559 | — | (115,721) | 1,170,913 |
| Clinical operations (including depreciation of \$3,721) | — | — | — | — | — | — | — | 329,386 | (264,878) | 362,723 |
| Hospital and clinics (including depreciation of \$56,682) | 1,321,521 | — | — | — | — | — | — | — | (11,035) | 1,310,486 |
| Auxiliary enterprises: | | | | | | | | | | |
| Housing and dining (including depreciation of \$9,756) | 28,897 | — | — | — | — | — | — | — | 331 | 29,228 |
| Athletics (including depreciation of \$15,377) | 129,572 | — | — | — | — | — | — | — | 1,201 | 130,773 |
| Other auxiliaries (including depreciation of \$689) | 33,843 | — | — | — | — | — | — | — | (664) | 33,179 |
| Other operating expenses | 594 | — | — | — | — | — | — | — | — | 594 |
| Total operating expenses | 2,802,202 | 264,289 | 17 | 43 | 62 | 104 | 32,559 | 329,386 | (390,766) | 3,037,896 |
| Net income (loss) from operations | (320,721) | 20,989 | (16) | (43) | (62) | (84) | (25) | 1,763 | (10,626) | (308,625) |
| NONOPERATING REVENUES (EXPENSES) | | | | | | | | | | |
| State appropriations | 267,029 | — | — | — | — | — | — | — | — | 267,029 |
| Gifts and non-exchange grants | 113,811 | 240 | 1 | 3 | — | 193 | — | — | (1,330) | 112,918 |
| Investment income (loss) | 112,084 | 1,461 | 793 | 123 | 175 | 1 | — | 238 | (857) | 114,018 |
| Interest on capital asset-related debt | (31,172) | — | — | — | — | — | — | (3,914) | — | (35,086) |
| Grants to (from) the University for noncapital purposes | 12,833 | (12,442) | (375) | (7) | (9) | — | — | — | — | — |
| Other nonoperating revenues and expenses, net | 11,960 | 4,690 | — | (7) | (9) | — | — | — | — | 16,650 |
| Net nonoperating revenues (expenses) | 486,545 | (6,051) | 419 | 119 | 166 | 194 | — | (3,676) | (2,187) | 475,629 |
| Net income (loss) before other revenues, expenses, gains, or losses | 165,824 | 14,938 | 403 | 76 | 104 | 110 | (25) | (1,913) | (12,813) | 166,704 |
| Capital grants and gifts | 60,498 | 9,035 | — | — | — | — | — | — | (135) | 69,398 |
| Additions to permanent endowments | 9,801 | 8 | — | — | 1 | — | — | — | (50) | 9,760 |
| Grants to (from) the University for capital purposes | 10,260 | (10,249) | (11) | — | — | — | — | — | — | — |
| Other, net | 4,824 | (516) | — | — | — | — | — | (2) | — | 4,306 |
| Total other revenues (expenses) | 85,383 | (1,722) | (11) | — | 1 | — | — | (2) | (185) | 83,464 |
| INCREASE (DECREASE) IN NET POSITION | 251,207 | 13,216 | 392 | 76 | 105 | 110 | (25) | (1,915) | (12,998) | 250,168 |
| NET POSITION, beginning of year | 3,548,808 | 68,400 | 8,624 | 1,368 | 1,850 | 167 | 87 | 36,096 | 61,127 | 3,726,527 |
| NET POSITION, end of year | \$ 3,800,015 | \$ 81,616 | \$ 9,016 | \$ 1,444 | \$ 1,955 | \$ 277 | \$ 62 | \$ 34,181 | \$ 48,129 | \$ 3,976,695 |

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 | Gluck Equine Research Foundation | Humanities Foundation | Mining Engineering Foundation | Center on Aging Foundation | Central Kentucky Management Services | Kentucky Medical Services Foundation | Eliminations | Total |
|---|--------------|---------------------|----------------------------------|-----------------------|-------------------------------|----------------------------|--------------------------------------|--------------------------------------|--------------|--------------|
| OPERATING REVENUES | | | | | | | | | | |
| Student tuition and fees, net | \$ 319,627 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 319,627 |
| Federal grants and contracts | 1,459 | 167,832 | — | — | — | — | — | — | — | 169,291 |
| State and local grants and contracts | 74,757 | 16,459 | — | — | — | — | — | — | — | 91,216 |
| Nongovernmental grants and contracts | 246,869 | 33,803 | — | — | — | — | — | (245,693) | — | 34,979 |
| Recoveries of facilities and administrative costs | 200 | 50,888 | — | — | — | — | — | — | — | 51,088 |
| Sales and services | 47,042 | 3,160 | — | — | 31 | 31,404 | — | (32,238) | — | 49,399 |
| Federal appropriations | 19,266 | — | — | — | — | — | — | — | — | 19,266 |
| County appropriations | 23,717 | — | — | — | — | — | — | — | — | 23,717 |
| Professional clinical service fees | — | — | — | — | — | — | 233,590 | — | (4,515) | 229,075 |
| Hospital services | 1,423,292 | — | — | — | — | — | — | — | (6,049) | 1,417,243 |
| Auxiliary enterprises: | | | | | | | | | | |
| Housing and dining, net | 39,403 | — | — | — | — | — | — | — | (300) | 39,103 |
| Athletics | 102,995 | — | — | — | — | — | — | — | — | 102,995 |
| Other auxiliaries | 49,434 | — | — | — | — | — | — | — | — | 49,434 |
| Other operating revenues | 838 | — | — | — | — | 31 | — | — | (77,157) | 7,931 |
| Total operating revenues | 2,348,899 | 272,142 | — | — | — | 31 | 84,250 | — | (365,952) | 2,504,364 |
| OPERATING EXPENSES | | | | | | | | | | |
| Educational and general: | | | | | | | | | | |
| Instruction | 293,601 | 9,482 | — | 5 | 53 | — | — | — | (128) | 303,013 |
| Research | 96,941 | 166,756 | 38 | — | — | — | — | — | (2,564) | 261,171 |
| Public service | 182,234 | 72,314 | — | — | — | — | — | — | (69,966) | 184,582 |
| Libraries | 22,275 | — | — | — | — | — | — | — | (2) | 22,273 |
| Academic support | 75,279 | 1,803 | — | — | — | — | — | — | (3) | 77,079 |
| Student services | 42,144 | 5 | — | 3 | — | — | — | — | (69) | 42,083 |
| Institutional support | 57,848 | 857 | — | — | — | 31,399 | — | — | (31,595) | 58,643 |
| Operations and maintenance of plant | 91,168 | 11 | — | — | — | — | — | — | (7,759) | 83,420 |
| Student financial aid | 35,256 | 1,494 | — | 47 | — | — | — | — | (2) | 36,795 |
| Depreciation | 64,675 | 486 | — | — | — | 27 | — | — | (112,088) | 65,188 |
| Total educational and general | 961,421 | 253,208 | 38 | 55 | 53 | 134 | 31,426 | — | (240,066) | 1,134,247 |
| Clinical operations (including depreciation of \$8,390) | 262,749 | — | — | — | — | — | — | 314,412 | — | 337,095 |
| Hospital and clinics (including depreciation of \$53,603) | 1,242,204 | — | — | — | — | — | — | — | (3,086) | 1,239,118 |
| Auxiliary enterprises: | | | | | | | | | | |
| Housing and dining (including depreciation of \$6,259) | 27,026 | — | — | — | — | — | — | — | 201 | 27,227 |
| Athletics (including depreciation of \$13,071) | 121,352 | — | — | — | — | — | — | — | 507 | 121,859 |
| Other auxiliaries (including depreciation of \$1,598) | 28,568 | — | — | — | — | — | — | — | (645) | 27,923 |
| Other operating expenses | 570 | — | — | — | — | — | — | — | — | 570 |
| Total operating expenses | 2,643,890 | 253,208 | 38 | 55 | 53 | 134 | 31,426 | — | (355,177) | 2,888,039 |
| Net income (loss) from operations | (294,991) | 18,934 | (38) | (55) | (53) | (103) | (22) | 3,428 | (10,775) | (283,675) |
| NONOPERATING REVENUES (EXPENSES) | | | | | | | | | | |
| State appropriations | 279,611 | — | — | — | — | — | — | — | — | 279,611 |
| Gifts and non-exchange grants | 128,608 | 245 | 12 | 2 | — | 125 | — | — | (1,196) | 127,796 |
| Investment income (loss) | (2,781) | 135 | (119) | (18) | (25) | 1 | — | 162 | (596) | (3,241) |
| Interest on capital asset-related debt | (27,442) | — | — | — | — | — | — | (1,002) | — | (28,444) |
| Grants to (from) the University for noncapital purposes | 13,679 | (13,245) | (418) | (7) | (9) | — | — | — | — | — |
| Other nonoperating revenues and expenses, net | 4,185 | 8,366 | — | — | — | — | — | — | — | 12,551 |
| Net nonoperating revenues (expenses) | 395,860 | (4,499) | (525) | (23) | (34) | 126 | — | (840) | 4,102 | 16,653 |
| Net income (loss) before other revenues, expenses, gains, or losses | 100,869 | 14,435 | (563) | (78) | (87) | 23 | (22) | 2,588 | (638) | 108,700 |
| Capital grants and gifts | 161,859 | 4,675 | — | — | — | — | — | — | — | 166,534 |
| Additions to permanent endowments | 13,041 | 8 | — | — | 3 | — | — | — | — | 13,052 |
| Grants to (from) the University for capital purposes | 9,128 | (9,107) | — | — | — | (21) | — | — | — | — |
| Other, net | (18,328) | (21) | — | — | — | — | (28) | — | — | (18,379) |
| Total other revenues (expenses) | 165,700 | (4,445) | — | — | 3 | (21) | (28) | (2) | (638) | 160,569 |
| Net income (loss) before other revenues, expenses, gains, or losses | 266,569 | 9,990 | (563) | (78) | (84) | 2 | (50) | 2,586 | (9,103) | 269,269 |
| Capital grants and gifts | 3,282,239 | 58,410 | 9,187 | 1,446 | 1,934 | 165 | 137 | 33,510 | 70,230 | 3,457,258 |
| NET POSITION, beginning of year | \$ 3,548,808 | \$ 68,400 | \$ 8,624 | \$ 1,368 | \$ 1,850 | \$ 167 | \$ 87 | \$ 36,096 | \$ 61,127 | \$ 3,726,527 |
| NET POSITION, end of year | | | | | | | | | | |

UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
COMBINED CONDENSED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2017
(in thousands)

| | UK | Research Foundation | Gluck Equine Research Foundation | Humanities Foundation | Mining Engineering Foundation | Center on Aging Foundation | Central Kentucky Management Services | Kentucky Medical Services Foundation | Eliminations | Total |
|--|-------------------|---------------------|----------------------------------|-----------------------|-------------------------------|----------------------------|--------------------------------------|--------------------------------------|--------------|-------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | | | | | | | | | |
| Student tuition and fees | \$ 338,574 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 338,574 |
| Grants and contracts | 359,465 | 229,919 | — | — | — | — | — | — | (274,203) | 315,181 |
| Recoveries of facilities and administrative costs | 266 | 54,321 | — | — | — | — | — | — | — | 54,587 |
| Sales and services | 49,092 | 1,566 | 1 | — | — | 22 | 32,010 | (214) | (33,310) | 49,167 |
| Federal appropriations | 15,896 | — | — | — | — | — | — | — | — | 15,896 |
| County appropriations | 25,558 | — | — | — | — | — | — | — | — | 25,558 |
| Payments to vendors and contractors | (970,138) | (96,701) | (17) | (41) | (34) | (72) | (1,231) | (330,285) | 404,363 | (994,156) |
| Student financial aid | (1,636,982) | (170,528) | — | (2) | (36) | — | (31,456) | (13,241) | — | (39,478) |
| Salaries, wages and benefits | 451 | — | — | — | — | — | — | 241,171 | (6,595) | 235,027 |
| Professional clinical service fees | 1,492,597 | — | — | — | — | — | — | — | (7,537) | 1,485,060 |
| Hospital services | 194,942 | — | — | — | — | — | — | — | (94) | 194,848 |
| Auxiliary enterprises receipts | (5,880) | — | — | — | — | — | — | — | — | (5,880) |
| Loans issued to students | 4,315 | — | — | — | — | — | — | — | — | 4,315 |
| Collection of loans to students | 66,734 | — | — | — | — | — | — | 2,360 | — | 69,094 |
| Self-insurance receipts | (65,580) | — | — | — | — | — | — | — | — | (65,580) |
| Other receipts (payments) | 723 | — | — | — | — | — | — | 90,087 | (80,243) | 10,567 |
| Net cash provided (used) by operating activities | (169,445) | 18,577 | (16) | (43) | (70) | (50) | (677) | (10,122) | 2,381 | (159,465) |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | | | | | | | | | |
| State appropriations | 272,621 | — | — | — | — | — | — | — | — | 272,621 |
| Gifts and grants received for other than capital purposes: | | | | | | | | | | |
| Gifts received for endowment purposes | 9,801 | 8 | — | — | 1 | — | — | — | (50) | 9,760 |
| Gifts received for other purposes | 97,393 | 240 | 1 | 3 | — | 193 | — | — | (1,330) | 96,500 |
| Agency and loan program receipts | 237,142 | — | — | — | — | — | — | — | — | 237,142 |
| Agency and loan program payments | (238,110) | — | — | — | — | — | — | — | — | (238,110) |
| Grants (to) from the University for noncapital purposes | 12,833 | (12,442) | (375) | (7) | (9) | — | — | — | — | — |
| Other financing receipts (payments) | 13,783 | 3,587 | — | — | — | — | — | — | — | 17,370 |
| Net cash provided (used) by noncapital financing activities | 405,463 | (8,607) | (374) | (4) | (8) | 193 | — | (1,380) | — | 395,283 |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | | | | | | | | | |
| Capital grants and gifts | 73,099 | 9,035 | — | — | — | — | — | — | (135) | 81,999 |
| Purchases of capital assets | (350,976) | (489) | — | — | — | — | — | (19,418) | — | (370,883) |
| Proceeds from capital debt | 19,669 | — | — | — | — | — | — | 39,875 | — | 59,544 |
| Payments to refunding bond agents | (58,593) | — | — | — | — | — | — | — | — | (58,593) |
| Proceeds from sales of capital assets | 252 | — | — | — | — | — | — | — | — | 252 |
| Principal paid on capital debt and leases | (27,400) | — | — | — | — | — | — | (22,273) | — | (49,673) |
| Interest paid on capital debt and leases | (41,889) | — | — | — | — | — | — | (3,914) | — | (45,803) |
| Grants (to) from the University for capital purposes | 10,314 | (10,303) | (11) | — | — | — | — | — | — | — |
| Other financing receipts (payments) | 2,101 | (24) | — | — | — | — | — | (1) | — | 2,076 |
| Net cash provided (used) by capital and related financing activities | (373,423) | (1,781) | (11) | — | — | — | — | (5,731) | (135) | (381,081) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | | | | | | | |
| Proceeds from sales and maturities of investments | 797,749 | 8,173 | 5,154 | 797 | 1,160 | — | — | 17,342 | — | 830,375 |
| Interest and dividends on investments | 27,796 | 147 | 123 | 20 | 27 | — | — | (1,679) | (866) | 25,568 |
| Purchases of investments | (861,922) | (8,098) | (5,154) | (797) | (1,112) | — | — | (30) | — | (877,113) |
| Net cash provided (used) by investing activities | (36,377) | 222 | 123 | 20 | 75 | — | — | 15,633 | (866) | (21,170) |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (173,762) | 8,411 | (278) | (27) | (3) | 143 | (677) | (220) | — | (166,433) |
| CASH AND CASH EQUIVALENTS, beginning of year | 1,035,179 | 54,566 | 338 | 86 | 26 | 167 | 1,493 | 262 | — | 1,092,107 |
| CASH AND CASH EQUIVALENTS, end of year | \$ 861,397 | \$ 62,977 | \$ 60 | \$ 59 | \$ 23 | \$ 310 | \$ 816 | \$ 32 | \$ — | \$ 925,674 |

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 | Gluck Equine Research Foundation | Humanities Foundation | Mining Engineering Foundation | Center on Aging Foundation | Central Kentucky Management Services | Kentucky Medical Services Foundation | Eliminations | Total |
|--|--------------|---------------------|----------------------------------|-----------------------|-------------------------------|----------------------------|--------------------------------------|--------------------------------------|--------------|--------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | | | | | | | | | |
| Student tuition and fees | \$ 320,092 | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ — | \$ 320,092 |
| Grants and contracts | 323,326 | 221,584 | — | — | — | — | — | — | (245,693) | 299,217 |
| Recoveries of facilities and administrative costs | 215 | 52,098 | — | — | — | — | — | — | — | 52,313 |
| Sales and services | 47,153 | 3,185 | — | — | 31 | 31,391 | 2,847 | — | (32,863) | 51,744 |
| Federal appropriations | 18,630 | — | — | — | — | — | — | — | — | 18,630 |
| County appropriations | 22,869 | — | — | — | — | — | — | — | — | 22,869 |
| Payments to vendors and contractors | (892,713) | (91,828) | (10) | (55) | (17) | (138) | (1,482) | (301,716) | 363,993 | (923,966) |
| Student financial aid | (36,794) | — | — | — | — | — | — | — | — | (36,794) |
| Salaries, wages and benefits | (1,554,043) | (161,138) | (30) | — | (39) | — | (28,959) | (11,667) | — | (1,755,876) |
| Professional clinical service fees | — | — | — | — | — | — | — | 226,734 | (2,990) | 223,744 |
| Hospital services | 1,424,078 | — | — | — | — | — | — | — | (6,648) | 1,417,430 |
| Auxiliary enterprises 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 receipts (payments) | 1,225 | — | — | — | — | — | — | 64,203 | (77,159) | 8,289 |
| Net cash provided (used) by operating activities | (112,692) | 23,901 | (40) | (55) | (56) | (107) | 950 | (115) | (1,660) | (89,874) |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | | | | | | | | | |
| 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 |
| Gifts received for other purposes | 114,749 | 263 | 13 | 2 | — | 125 | — | — | (1,196) | 113,956 |
| Agency and loan program receipts | 232,673 | — | — | — | — | — | — | — | — | 232,673 |
| Agency and loan program payments | (229,244) | — | — | — | — | — | — | — | — | (229,244) |
| Grants (to) from the University for noncapital purposes | 13,678 | (13,245) | (418) | (6) | (9) | — | — | — | — | — |
| Other receipts (payments) | 7,425 | 6,824 | — | — | — | — | — | — | 4,102 | 18,351 |
| Net cash provided (used) by noncapital financing activities | 426,341 | (6,150) | (405) | (4) | (6) | 125 | — | — | 2,906 | 422,807 |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | | | | | | | | | |
| Capital grants and gifts | 160,117 | 4,675 | — | — | — | — | — | — | (638) | 164,154 |
| Purchases of capital assets | (408,788) | (81) | — | — | — | — | (6) | (7,957) | — | (416,832) |
| Proceeds from capital debt | 159,541 | — | — | — | — | — | — | — | — | 159,541 |
| Principal paid on capital debt and leases | (46,732) | — | — | — | — | — | — | (3,021) | — | (49,753) |
| Interest paid on capital debt and leases | (37,780) | — | — | — | — | — | — | (1,002) | — | (38,782) |
| Grants (to) from the University for capital purposes | 9,128 | (9,107) | — | — | — | (21) | — | — | — | — |
| Other receipts (payments) | 5,562 | (21) | — | — | — | — | — | — | — | 5,541 |
| Net cash provided (used) by capital and related financing activities | (158,952) | (4,534) | — | — | — | (21) | (6) | (11,980) | (638) | (176,131) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | | | | | | | |
| Proceeds from sales and maturities of investments, net | 604,925 | 4,311 | 2,847 | 440 | 578 | — | — | 14,448 | — | 627,549 |
| Interest and dividends on investments | 23,628 | 58 | 99 | 15 | 22 | — | — | 1,531 | (608) | 24,745 |
| Purchases of investments | (633,375) | (12,612) | (2,410) | (373) | (533) | — | — | (4,193) | — | (653,496) |
| Net cash provided (used) by investing activities | (4,822) | (8,243) | 536 | 82 | 67 | — | — | 11,786 | (608) | (1,202) |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | 149,875 | 4,974 | 91 | 23 | 5 | (3) | 944 | (309) | — | 155,600 |
| CASH AND CASH EQUIVALENTS, beginning of year | 885,304 | 49,592 | 247 | 63 | 21 | 170 | 549 | 561 | — | 936,507 |
| CASH AND CASH EQUIVALENTS, end of year | \$ 1,035,179 | \$ 54,566 | \$ 338 | \$ 86 | \$ 26 | \$ 167 | \$ 1,493 | \$ 252 | \$ — | \$ 1,092,107 |

**UNIVERSITY OF KENTUCKY
A COMPONENT UNIT OF THE COMMONWEALTH OF KENTUCKY
COMBINED STATEMENTS OF CHANGES IN FIDUCIARY NET POSITION (in thousands)
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016**

| | 2017 | | | 2016 | | |
|---|------------|-----------|------------|------------|-----------|------------|
| | OPEB Plan | LTD Plan | Total | OPEB Plan | LTD Plan | Total |
| Additions | | | | | | |
| Investment income: | | | | | | |
| Interest and dividend income | \$ 1,929 | \$ 403 | \$ 2,332 | \$ 1,364 | \$ 638 | \$ 2,002 |
| Net appreciation (depreciation) in fair value of investments | 10,579 | 1,553 | 12,132 | (2,627) | (623) | (3,250) |
| Less investment expense | — | — | — | — | — | — |
| Net investment income (loss) | 12,508 | 1,956 | 14,464 | (1,263) | 15 | (1,248) |
| Contributions: | | | | | | |
| University | 23,987 | 2,020 | 26,007 | 24,373 | 1,964 | 26,337 |
| Beneficiaries | 5,500 | — | 5,500 | 5,183 | — | 5,183 |
| Total contributions | 29,487 | 2,020 | 31,507 | 29,556 | 1,964 | 31,520 |
| Total additions | 41,995 | 3,976 | 45,971 | 28,293 | 1,979 | 30,272 |
| Deductions | | | | | | |
| Administrative expenses | 674 | 61 | 735 | 576 | 78 | 654 |
| Payments to retirees and beneficiaries | 17,389 | 1,763 | 19,152 | 16,520 | 1,849 | 18,369 |
| Total deductions | 18,063 | 1,824 | 19,887 | 17,096 | 1,927 | 19,023 |
| INCREASE (DECREASE) IN NET POSITION | 23,932 | 2,152 | 26,084 | 11,197 | 52 | 11,249 |
| NET POSITION restricted for the postemployment benefits other than pensions, beginning of year | 120,012 | 16,632 | 136,644 | 108,815 | 16,580 | 125,395 |
| NET POSITION restricted for the postemployment benefits other than pensions, end of year | \$ 143,944 | \$ 18,784 | \$ 162,728 | \$ 120,012 | \$ 16,632 | \$ 136,644 |

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

1. UNIVERSITY OF KENTUCKY OTHER POSTEMPLOYMENT BENEFIT (OPEB) PLAN

SCHEDULE OF CHANGE IN THE NET OPEB LIABILITY (in thousands) AND RELATED RATIOS

| | 2017 |
|--|------------|
| Total OPEB liability | |
| Service cost | \$ 4,356 |
| Interest cost | 28,667 |
| Change of benefit terms | — |
| Difference between expected and actual experiences | 12,087 |
| Changes of assumptions | (40,408) |
| Benefit payments | (11,889) |
| Net change in total OPEB liability | (7,187) |
| Total OPEB liability, beginning | 383,708 |
| Total OPEB liability, ending | 376,521 |
| Plan fiduciary net position | |
| Contributions - employer | 23,987 |
| Contributions - beneficiaries | 5,500 |
| Net investment income | 12,508 |
| Benefit payments | (17,389) |
| Administrative expense | (674) |
| Net change in plan fiduciary net position | 23,932 |
| Plan fiduciary net position, beginning | 120,012 |
| Plan fiduciary net position, ending | 143,944 |
| Net OPEB liability, ending | \$ 232,577 |
| Net position as a % of OPEB liability | 38.2% |

SCHEDULE OF OPEB INVESTMENT RETURNS

| Year | Annual money-weighted rate of return, net of investment expenses |
|------|---|
| 2017 | 10.3% |

SCHEDULE OF OPEB CONTRIBUTIONS (in thousands)

| | 2017 |
|---|------------|
| Actuarially determined contribution | \$ 24,454 |
| Contribution in relation to actuarially determined contribution | (23,987) |
| Contribution deficiency (excess) | \$ 467 |
| | |
| Covered employee payroll | \$ 494,158 |
| Contribution as a percentage of covered employee payroll | 4.9% |

Actuarially determined contribution rates are calculated as of June 30, two years prior to the end of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

| | |
|------------------------------|---|
| Actuarial cost method | Projected Unit Credit. (Attribution from date of hire to expected retirement ages). |
| Amortization method | Level percentage of payroll |
| Amortization period | 30 years |
| Asset valuation method | Market value |
| Health care cost trend rates | Post-65 medical 5% and post-65 prescription 10% for 2017, decreasing .5% per year to an ultimate rate of 5%. Pre-65 6.75%, decreasing .12% - 3.49% per year to an ultimate rate of 2.20% in 2024. |
| Salary increases | 3% per year |
| Discount rate | 7.5% based on the University's funding policy and the expected long-term nominal return on the separate trust assets that will be used to finance the payment of plan benefits. The University has stated a funding policy to contribute an amount to the segregated and protected trust fund, such that the assets available will always be sufficient to cover the expected benefit payments. |
| Mortality | Retirement Plan-2006 mortality table with fully generational projections using scale Mortality Plan-2015 |
| Plan participation | 80% elect coverage |

Ten years of data for the OPEB Plan is required and will be added as information becomes available.

2. UNIVERSITY OF KENTUCKY LONG-TERM DISABILITY (LTD) PLAN

SCHEDULE OF CHANGE IN THE NET OPEB LIABILITY (in thousands) AND RELATED RATIOS

| | 2017 |
|--|------------|
| Total OPEB liability | |
| Service cost | \$ 1,606 |
| Interest cost | 1,569 |
| Change of benefit terms | — |
| Difference between expected and actual experiences | 138 |
| Changes of assumptions | 1,042 |
| Benefit payments | (1,763) |
| Net change in total OPEB liability | 2,592 |
| Total OPEB liability, beginning | 20,188 |
| Total OPEB liability, ending | 22,780 |
| | |
| Plan fiduciary net position | |
| Contributions - employer | 2,020 |
| Net investment income | 1,956 |
| Benefit payments | (1,763) |
| Administrative expense | (61) |
| Net change in plan fiduciary net position | 2,152 |
| Plan fiduciary net position, beginning | 16,632 |
| Plan fiduciary net position, ending | 18,784 |
| | |
| Net OPEB liability, ending | \$ 3,996 |
| | |
| Net position as a % of OPEB liability | 82.5% |
| Covered-employee payroll | \$ 941,000 |
| Net OPEB liability as a % of payroll | 0.42% |

SCHEDULE OF OPEB INVESTMENT RETURNS

| Year | Annual money-weighted rate of return, net of investment expenses |
|------|---|
| 2017 | 12.0% |

SCHEDULE OF OPEB CONTRIBUTIONS (in thousands)

| | 2017 |
|---|------------|
| Actuarially determined contribution | \$ 1,984 |
| Contribution in relation to actuarially determined contribution | (2,020) |
| Contribution deficiency (excess) | \$ (36) |
| | |
| Covered employee payroll | \$ 940,951 |
| Contribution as a percentage of covered employee payroll | 0.2% |

Actuarially determined contribution rates are calculated as of July 1, two years prior to the end of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

| | |
|----------------------------|--|
| Actuarial cost method | Projected Unit Credit. (Attribution from date of hire to expected disability ages) |
| Amortization method | Level percentage of payroll |
| Amortization period | 30 years |
| Asset valuation method | Market value |
| Salary increases | 3% per year |
| Discount rate | 7.5% based on the University's funding policy (ARC funding) and the expected long-term return on the separate trust assets that will be used to finance the payment of plan benefits. The University has stated that its funding policy is to contribute the ARC each year to a segregated and protected trust fund. |
| Mortality rate | Canadian Institute of Actuaries (CIA) 1988-94 LTD table. |
| Mortality rate for actives | Retirement Plan-2006 mortality table with fully generational projections using scale Mortality Plan-2015 |
| Incidence of disability | Gender and age-related disability incidence rates based on 1987 Commissioner's Group Long-term Disability table |
| Duration of payment | Payments are assumed to be made until the later of: i) age 65 and ii) five years after date of disability. |
| LTD income benefit | |
| Disability benefit | Actual net benefit currently being paid (if currently disabled) |
| Social Security offset | Assume that 90% of the members who have been disabled for less than 24 months and currently not entitled to a Social Security offset will immediately receive an offset |

Ten years of data for the LTD Plan is required and will be added as information becomes available.

3. 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 |
|----------------|---------------------------|-----------------------------------|---|--------------|------------------------|---|
| June 30, 2015 | \$108,815 | \$337,665 | \$228,850 | 32.2% | \$509,627 | 44.9% |
| June 30, 2016 | \$120,012 | \$349,503 | \$229,491 | 34.3% | \$489,855 | 46.8% |
| June 30, 2017 | \$143,944 | \$343,484 | \$199,540 | 41.9% | \$494,158 | 40.4% |

Schedule of Employer Contributions
(in thousands)

| Year Ended | Annual Required Contributions | Percentage Contributed |
|---------------|-------------------------------|------------------------|
| June 30, 2015 | \$20,395 | 100.7% |
| June 30, 2016 | \$23,741 | 102.7% |
| June 30, 2017 | \$24,454 | 98.1% |

4. LONG-TERM DISABILITY BENEFIT

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.

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 |
|----------------|---------------------------|-----------------------------------|---|--------------|------------------------|---|
| June 30, 2015 | \$16,576 | \$22,730 | \$6,154 | 72.9% | \$813,205 | 0.8% |
| June 30, 2016 | \$16,632 | \$23,457 | \$6,825 | 70.9% | \$883,682 | 0.8% |
| June 30, 2017 | \$18,784 | \$25,310 | \$6,526 | 74.2% | \$940,951 | 0.7% |

Schedule of Employer Contributions
(in thousands)

| Year Ended | Annual Required Contributions | Percentage Contributed |
|---------------|-------------------------------|------------------------|
| June 30, 2015 | \$2,203 | 99.7% |
| June 30, 2016 | \$1,926 | 100.2% |
| June 30, 2017 | \$1,984 | 101.8% |

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