



UNIVERSITY OF KENTUCKY • 2020 FINANCIAL STATEMENTS

UK HealthCare Hospital System

UK HealthCare Hospital System
An Organizational Unit of the University of Kentucky
Financial Statements
Years Ended June 30, 2020 and 2019

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Independent Auditor's Report

Board of Trustees
UK HealthCare Hospital System
University of Kentucky
Lexington, Kentucky

We have audited the accompanying financial statements of the UK HealthCare Hospital System (System), an organizational unit of the University of Kentucky (University), as of and for the years ended June 30, 2020 and 2019, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the System as of June 30, 2020 and 2019, and the changes in its financial position and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of the System are intended to present the financial position, the changes in financial position and cash flows of only that portion of the business-type activities that is attributable to the transactions of the System. They do not purport to, and do not, present fairly the financial position of the University as of June 30, 2020 and 2019, the changes in its financial position or its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context.

We have applied certain limited procedures to the required supplementary information, in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

BKD, LLP

Louisville, Kentucky
October 1, 2020

**UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED JUNE 30, 2020 AND 2019**

The following Management's Discussion and Analysis (MD&A) provides an overview of the financial position and activities of the UK HealthCare Hospital System for the years ended June 30, 2020 and 2019. UK HealthCare Hospital System includes Albert B. Chandler University Hospital, including Kentucky Children's Hospital (collectively Chandler); UK HealthCare Good Samaritan Hospital (Good Samaritan); Kentucky Healthcare Enterprise, Inc. (KHE), a wholly owned for-profit subsidiary; and Surgery Blue LLC, a wholly owned for-profit subsidiary, and its for-profit subsidiary, Surgery Center of Lexington, LLC (51% ownership); (collectively, the System). Management has prepared this discussion, and we encourage you to read it in conjunction with the financial statements and the notes appearing in this report.

About UK HealthCare System

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 percent of academic medical centers. In July 2020, UK HealthCare was listed number one in Kentucky in the latest U.S. News Best Hospitals ranking for the fifth year in a row. 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.

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 1,265 licensed beds with an average daily census of 754 patients. On a monthly basis, the system provides over 1,355 inpatient surgeries, 1,318 outpatient surgeries, 35,481 radiology procedures, 8,676 emergency department visits, and 184,459 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. The psychiatric facility, opened in September 2013, 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 the University'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 a 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.

Financial Highlights

The System's overall financial position remains strong with assets of \$2.53 billion and liabilities of \$826.4 million. Net position, which represents the System's residual interest in assets after liabilities are deducted, was \$1.71 billion or 67.5% of total assets. For the fiscal year ended June 30, 2020, the System reported net income before other revenues, expenses, gains and losses of \$434.9 million, generating a margin of 20.2%.

Financial results for fiscal year 2020 exceeded prior year revenues with net outpatient revenues, including the provision for doubtful accounts, increasing approximately \$165.6 million or 23.4% over the prior fiscal year and net inpatient revenues, including the provision for doubtful accounts, which increased \$233.1 million or 26.3% over the previous fiscal year. The primary driver was that the System was able to recognize \$391.6 million of Medicaid Directed Payments revenue during the current fiscal year.

- Total assets increased \$327.0 million or 14.8%. This increase is due to increases in cash and cash equivalents of \$301.1 million, inventories and other assets of \$7.0 million, capital assets, net, of \$44.6 million, and estimated third-party payer settlements of \$7.8 million. This increase was offset by decreases in accounts receivable, net, of \$30.4 million and long-term investments of \$3.1 million.
- Deferred outflows of resources decreased \$1.3 million, which represents the unamortized difference between the reacquisition price and the net carrying amount of the refunded debt.
- Total liabilities increased \$48.7 million or 6.3% as a result in an increase of accounts payable and accrued expenses of \$19.2 million, unearned revenue of \$38.4 million, capital lease obligations of \$2.0 million, and other long-term liabilities of \$169 thousand. This was offset by a decrease of long-term debt of \$11.0 million.
- Total net position increased \$277.0 million or 19.4% primarily due to the current year net income.
- Operating revenues increased \$390.4 million or 22.2% primarily due to an increase in net patient revenue of \$360.7 million.
- Operating expenses increased \$201.2 million or 13.3%. The largest increases came from supplies of \$88.4 million, purchased services of \$31.4 million, and personnel costs of \$51.5 million.
- The net nonoperating revenues decrease of \$18.5 million primarily resulted from decreases of \$16.5 million in investment income and \$6.7 million in other nonoperating revenues. These decreases were offset by a reduction of interest expense of \$5.3 million and an increase of \$330 thousand in gifts and non-exchange grants.

Operating Statistics

The following table presents utilization statistics for the System for fiscal years ended 2020, 2019 and 2018:

| Discharges: | 2020 | 2019 | 2018 |
|------------------------|----------------|----------------|----------------|
| Medicare | 14,330 | 15,058 | 14,566 |
| Medicaid | 13,912 | 14,778 | 15,023 |
| Commercial/Blue Cross | 10,323 | 10,734 | 10,574 |
| Patient/Charity | 801 | 1,019 | 746 |
| Total discharges | <u>39,366</u> | <u>41,589</u> | <u>40,909</u> |
| Average daily census | 754.44 | 773.61 | 754.69 |
| Average length of stay | 7.01 | 6.79 | 6.73 |
| Outpatient visits: | | | |
| Hospital clinics | 585,697 | 600,712 | 565,903 |
| Emergency visits | 104,116 | 111,819 | 112,093 |
| Total visits | <u>689,813</u> | <u>712,531</u> | <u>677,996</u> |

2020. Total discharges decreased by 2,223 or 1.7% compared to the prior fiscal year. The decrease occurred primarily due to decreases in Medicaid discharges of 866, Medicare discharges of 728, Commercial/Blue Cross of 411, and Patient/Charity of 218. Overall, the Diagnosis-Related Group case mix index increased to 2.0850 from 1.9833 and the average length of stay increased by 0.22 days to 7.01 days. The case mix for Chandler was at 2.2340 while Good Samaritan was at 1.3500. Total outpatient visits decreased by 22,718 or 3.2% over the prior year.

Using the Financial Statements

The System presents its financial reports in a “business type activity” format, in accordance with Governmental Accounting Standards Board Statement (GASB) 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*. In addition to this MD&A section, the financial report includes a Statement of Net Position, a Statement of Revenues, Expenses and Changes in Net Position, a Statement of Cash Flows and Notes to the Financial Statements. GASB requires that statements be presented on a System-wide basis.

Reporting Entity

The System is an organizational unit of the University of Kentucky (the University), which 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 System include Kentucky Healthcare Enterprise, Inc. (KHE), a wholly owned for-profit subsidiary; and Surgery Blue, LLC, a wholly owned for-profit subsidiary, and its for-profit subsidiary, Surgery Center of Lexington, LLC (51% ownership). The System provides inpatient, outpatient, and emergency care services for residents of the Commonwealth.

Statement of Net Position

The Statement of Net Position is the System’s balance sheet. It reflects the total assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (equity) of the System as of June 30, 2020, with comparative information as of June 30, 2019. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as non-current. Net position, the difference between total assets plus deferred outflows of resources and total liabilities plus deferred inflows of resources, is an important indicator of the System’s current financial condition, while the change in net position is an indicator of whether the overall financial position has improved or worsened during the year. Generally, assets, deferred outflows of resources, liabilities, and deferred inflows of resources are reported using current values. A major exception is capital assets, which are stated at historical cost, less accumulated depreciation.

A summarized comparison of the System's assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position at June 30, 2020, 2019 and 2018 follows:

Condensed Statements of Net Position (in thousands)

| | <u>2020</u> | <u>2019</u> | <u>2018</u> |
|--|---------------------|---------------------|---------------------|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | | |
| Current assets | \$ 1,062,117 | \$ 685,118 | \$ 604,871 |
| Capital asset, net | 1,058,839 | 1,014,284 | 1,023,252 |
| Other noncurrent assets | 408,310 | 502,866 | 510,812 |
| Deferred outflows of resources | 5,549 | 6,806 | 8,143 |
| Total assets and deferred outflows of resources | <u>2,534,815</u> | <u>2,209,074</u> | <u>2,147,078</u> |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | |
| Current liabilities | 272,377 | 212,943 | 245,992 |
| Noncurrent liabilities | 553,974 | 564,693 | 591,716 |
| Deferred inflows of resources | 66 | 64 | 62 |
| Total liabilities and deferred inflows of resources | <u>826,417</u> | <u>777,700</u> | <u>837,770</u> |
| NET POSITION | | | |
| Net investment in capital assets | 535,054 | 509,782 | 514,863 |
| Nonexpendable other | 1,616 | 1,590 | 1,255 |
| Restricted expendable | 11,748 | 14,667 | 19,668 |
| Unrestricted | 1,159,980 | 905,335 | 773,522 |
| Total net position | <u>\$ 1,708,398</u> | <u>\$ 1,431,374</u> | <u>\$ 1,309,308</u> |

Assets. As of June 30, 2020, the System's total assets amounted to approximately \$2.53 billion. Capital assets, net of depreciation, of \$1.06 billion or 41.9% of total assets represented the System's largest asset. Cash and cash equivalents of \$881.9 million or 34.9% of total assets is the second largest asset, and long-term investments of \$311.8 million or 12.3% of total assets were the System's third largest asset. Accounts receivable, primarily patient-related, of \$201.7 million or 8.0% represents another significant asset of the System.

Total assets increased by \$327.0 million during the year ended June 30, 2020. The increase was the result of several factors: cash and cash equivalents increased \$301.1 million, inventories and other assets increased \$7.0 million, capital assets, net, increased \$44.6 million, and estimated third-party payer settlements increased \$7.8 million. These increases were offset by decreases in accounts receivable, net, of \$30.4 million and long-term investments decreased \$3.1 million.

Deferred Outflows of Resources. Deferred outflows of resources totaled \$5.5 million and decreased \$1.3 million, which represents the unamortized difference between the reacquisition price and the net carrying amount of the refunded debt. The System refunded General Receipts 2005 Notes Series A, and General Receipts 2007 Notes Series A and B during the fiscal year 2015.

Liabilities. As of June 30, 2020, the System's liabilities totaled approximately \$826.4 million. Long-term debt (current and non-current), which consists of general receipts project notes and note payable to the University, comprised the largest liability of \$527.7 million or 63.9% of total liabilities. Capital lease obligations totaled \$25.2 million or 3.1% of liabilities while accounts payable and accrued expenses represented approximately \$144.6 million or 17.5% of liabilities. Long-term liabilities, other totaled \$26.5 million or 3.2% of liabilities and consisted primarily of unamortized bond premium. Unearned revenue accounted for \$102.3 million or 12.4%.

Total liabilities increased \$48.7 million or 6.3% as a result of an increase in accounts payable and accrued expenses of \$19.2 million, unearned revenue of \$38.4 million, capital lease obligations of \$2.0 million, and other long-term liabilities of \$169 thousand. This was offset by a decrease of long-term debt of \$11.0 million.

Deferred Inflows of Resources. The System is the residual principal and income beneficiary of an irrevocable trust that is held and controlled by external trustees. For the years ended June 30, 2020 and 2019, the System received income from this trust of approximately \$500 and \$400, respectively. The market value of the irrevocable external trust assets as of June 30, 2020 and 2019 was approximately \$66,000 and \$64,000, respectively.

Net Position. Net position at June 30, 2020 totaled approximately \$1.71 billion, or 67.5% of total assets. Net investment in capital assets totaled \$535.1 million or 31.3% of total net position. Restricted net position totaled approximately \$13.4 million or 0.8% of total net position. Unrestricted net position accounted for \$1.16 billion or 67.9% of total net position. Total net position increased \$277.0 million or 19.4%.

Restricted net position is subject to externally imposed restrictions governing its use. Although unrestricted net position is not subject to externally imposed stipulations, substantially all of the unrestricted net position has been internally designated for capital projects and working capital requirements.

2019 Versus 2018. When comparing the fiscal year ended June 30, 2019 to the year ended June 30, 2018:

- Total assets increased by \$63.3 million during the year ended June 30, 2019. The increase was the result of several factors: cash and cash equivalents increased \$54.8 million, long-term investments increased \$11.4 million, inventories and other assets increased \$4.8 million, and accounts receivable, net, of \$5.9 million. These increases were offset by decreases in capital assets, net, of \$9.0 million and estimated third-party payer settlements of \$6.0 million.
- Deferred outflows of resources decreased \$1.3 million, which represents the unamortized difference between the reacquisition price and the net carrying amount of the refunded debt. The System refunded General Receipts 2005 Notes Series A, and General Receipts 2007 Notes Series A and B during the fiscal year 2015.
- Total liabilities decreased \$60.1 million primarily due to a decrease in estimated third-party settlements of \$58.3 million, long-term debt of \$18.9 million, capital lease obligations of \$3.7 million, and long-term liabilities, other of \$3.8 million. These decreases were offset by increases of unearned revenue of \$24.0 million and accounts payable and accrued expenses of \$527,000.
- Deferred inflows of resources as of June 30, 2019 and 2018 were approximately \$64,000 and \$62,000, respectively, which presents the gain in net position by the System that is applicable to a future reporting period.
- Total net position increased \$122.1 million, primarily due to a net gain for the year related to net income from continuing operations.

Statement of Revenues, Expenses and Changes in Net Position

The Statement of Revenues, Expenses and Changes in Net Position is the System's income statement. It details how net position has fluctuated during the year ended June 30, 2020, with comparative information for the year ended June 30, 2019. 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. All items that increase or decrease net position must 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. 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.

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

| | <u>2020</u> | <u>2019</u> | <u>2018</u> |
|--|----------------------------|----------------------------|----------------------------|
| OPERATING REVENUES | | | |
| Net patient service revenues | \$ 2,008,383 | \$ 1,647,676 | \$ 1,524,925 |
| Sales and services | 98,679 | 69,760 | 69,868 |
| Management contract revenue | 41,930 | 41,177 | 44,488 |
| Total operating revenues | <u>2,148,992</u> | <u>1,758,613</u> | <u>1,639,281</u> |
| OPERATING EXPENSES | | | |
| Salaries and benefits | 731,176 | 679,646 | 644,239 |
| Supplies and purchased services | 647,006 | 527,145 | 484,739 |
| Other expenses | 222,405 | 195,586 | 186,340 |
| Depreciation | 69,025 | 66,959 | 62,117 |
| Management contract expenses | 38,970 | 38,032 | 41,195 |
| Total operating expenses | <u>1,708,582</u> | <u>1,507,368</u> | <u>1,418,630</u> |
| NET INCOME FROM CONTINUING OPERATIONS | <u>440,410</u> | <u>251,245</u> | <u>220,651</u> |
| NONOPERATING REVENUES (EXPENSES) | | | |
| State appropriations | — | — | 1,053 |
| Additions to permanent endowments | 26 | 335 | 454 |
| Grants and gifts | 4,770 | 4,395 | 6,486 |
| Investment income | 10,638 | 27,125 | 22,786 |
| Interest expense | (18,223) | (23,535) | (18,060) |
| Transfers to the University of Kentucky | (157,918) | (142,217) | (136,685) |
| Other, net | (2,679) | 4,718 | 806 |
| Total nonoperating expenses | <u>(163,386)</u> | <u>(129,179)</u> | <u>(123,160)</u> |
| TOTAL INCREASE IN NET POSITION | 277,024 | 122,066 | 97,491 |
| NET POSITION, beginning of year | <u>1,431,374</u> | <u>1,309,308</u> | <u>1,211,817</u> |
| NET POSITION, end of year | <u><u>\$ 1,708,398</u></u> | <u><u>\$ 1,431,374</u></u> | <u><u>\$ 1,309,308</u></u> |

Operating Revenues

Total operating revenues were approximately \$2.15 billion for the year ended June 30, 2020, an increase of \$390.4 million or 22.2% over fiscal year 2019. The most significant source of operating revenue for the System was net patient service revenues of \$2.01 billion, an increase of \$360.7 million or 21.9% in fiscal year 2020 over 2019.

The calculation methodology for Medicaid supplemental payments was adjusted during fiscal year 2020 and is now referred to as "Directed Payments". These new payments replace the Medicaid Managed Care Organization's portion of Intensity Operating Allowance and Physician Supplemental Payments. The Directed Payments are the difference between the System's average commercial rate and the rates Medicaid Managed Care Organizations pay for healthcare services. The payments are applicable to both inpatient and outpatient hospital services. A per day and per visit gap has been calculated and is applied to Medicaid Managed Care volume.

Inpatient net revenue, including bad debt, increased \$233.1 million or 26.3% over prior year. The primary driver of the increase was Directed Payments of \$300.1 million, offset by unfavorable volume and payer mix changes of \$114.5 million driven by a decrease of 866 Medicaid cases. In 2019, the System was able to recognize \$50 million in prior year's settlements of Medicaid Disproportionate Share Hospital (DSH) revenue. The System did not recognize Medicaid DSH revenue in fiscal year 2020.

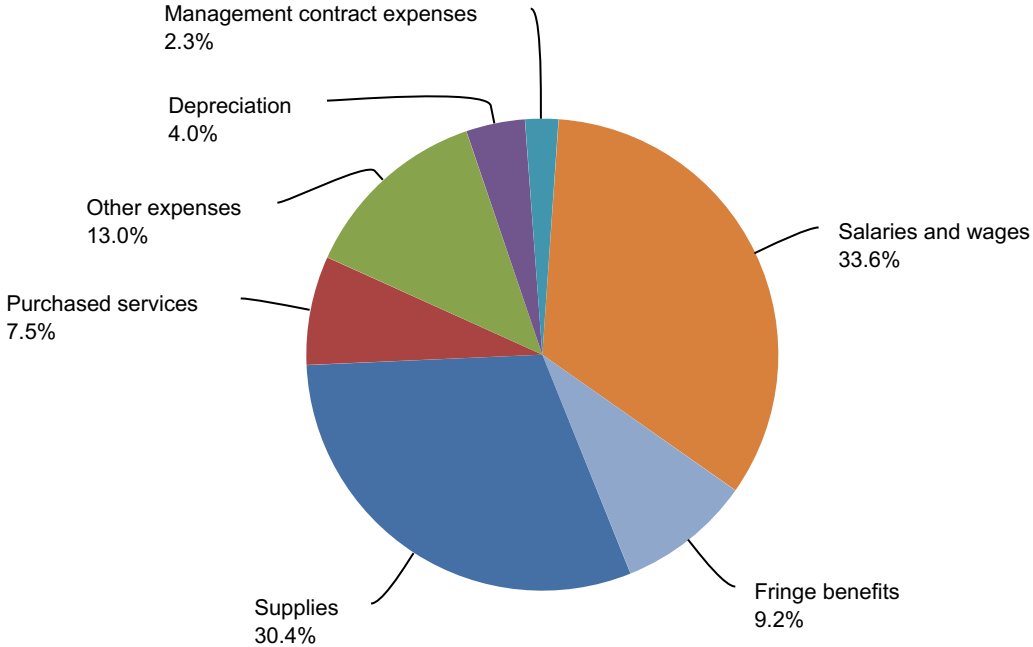
Surgery Blue had a net patient revenue increase over last year of \$9.5 million due to having a full year of operations.

Outpatient net revenue, including bad debt, increased by \$165.6 million or 23.4% over prior year. The primary driver was Directed Payments of \$91.5 million. Outpatient activity decreased by 15,015 hospital clinic visits and a decrease of 7,703 emergency room visits at the end of the year versus last year due to the COVID-19 pandemic. However, strong performance earlier in the year resulted in an increase in revenue of \$74.1 million.

The System was able to recognize \$391.6 million of Directed Payments revenue during the current fiscal year.

Bad debt provision increased by \$580,000 or 0.7% over the prior year as the Enterprise has seen more accounts referred to bad debt.

TOTAL OPERATING EXPENSES



Operating Expenses

Total operating expenses, including \$69.0 million of depreciation, were \$1.71 billion, an increase of \$201.2 million or 13.3% over the prior year.

Salaries and wages increased \$42.0 million over the prior fiscal year. The increase in salary and wages was driven by a Full-Time Equivalent (FTE) increase of 980, a 10.5% increase over prior year. The majority of this increase, 176 FTEs, was new staff in finance working on the electronic health records project. FTEs of 106 were for patient support areas due to volume before the COVID-19 pandemic. Employees were furloughed during the pandemic as necessary to meet volume decline. Volume has rebounded as of early fiscal year 2021. The other FTE drivers were pharmacy at 84 FTEs, graduate medical education at 45 FTEs, information technology at 24 FTEs, COVID-19 command center at 55 FTEs, and administration and support at 53 FTEs. Fringe benefits increased \$9.5 million or 6.5%.

Supplies expenses increased by \$88.4 million or 20.5% primarily due to increases in drugs, antibiotics, variable hospital supplies, and an increase in the inpatient population. Purchased services increased by \$31.4 million or 32.7% primarily due to the increase in contract labor expenses of \$51.3 million. Other expenses increased by \$26.8 million or 13.7%, which were a result of increases in Surgery Blue full year expenses of \$1.4 million over prior year. Fiscal year 2019 Surgery Blue financials were only for a partial year.

Nonoperating Revenues (Expenses)

Total nonoperating expenses were \$5.5 million in fiscal year 2020 compared to \$13.0 million in total nonoperating revenues during the prior fiscal year, a decrease of \$18.5 million. This decrease was mainly due to a reduction in investment income of \$16.5 million because of capital market downturn and a decrease of \$6.7 million in other nonoperating revenues. These decreases were offset by a reduction of interest expense of \$5.3 million and an increase of \$330 thousand in gifts and non-exchange grants.

Transfers to the University of Kentucky increased to \$157.9 million in 2020 compared to \$142.2 million in 2019 primarily because of a decrease in noncapital transfers of \$25.5 million. The increases in provider cost along with the challenges in payor reimbursement and increased supporting staff has resulted in the increased investment from UK HealthCare to the clinical practice. In addition, there was a decrease in transfers to the University of Kentucky for capital purposes of \$9.8 million.

2019 Versus 2018. Total operating revenues were \$1.76 billion for the fiscal year ended June 30, 2019, an increase of \$119.3 million over the year ended June 30, 2018. The increase in operating revenues was primarily due to increased net patient service revenues.

Operating expenses totaled \$1.51 billion, an increase of \$88.7 million over 2018. The increase was caused primarily by higher costs for personnel and supplies.

Nonoperating revenues amounted to \$13.0 million in fiscal year 2019 compared to nonoperating revenues of \$13.5 million in the prior year, a decrease of \$487,000. This decrease is primarily due to an increase in interest expense of \$5.5 million and a decrease in state appropriations of \$1.1 million. These expenses were offset by increases of \$4.3 million in investment income, \$3.9 million in other nonoperating revenues, and \$558,000 in gifts and non-exchange grants.

Statement of Cash Flows

The Statement of Cash Flows details how cash has increased or decreased during the year ended June 30, 2020, with comparative financial information for the year ended June 30, 2019. It classifies the sources and uses of cash into the following categories:

- Operating activities
- Noncapital financing activities

- Capital and related financing activities
- Investing activities

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

The primary purpose of the Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the System during the year that will allow financial statement readers to assess the System's:

- Ability to generate future net cash flows
- Ability to meet obligations as they become due
- Possible need for external financing

Condensed Statements of Cash Flows (in thousands)

| | <u>2020</u> | <u>2019</u> | <u>2018</u> |
|---|--------------------------|--------------------------|--------------------------|
| CASH PROVIDED (USED) BY: | | | |
| Operating activities | \$ 553,347 | \$ 287,166 | \$ 248,174 |
| Noncapital financing activities | (124,234) | (128,937) | (121,431) |
| Capital and related financing activities | (141,775) | (117,904) | (4,046) |
| Investing activities | <u>13,787</u> | <u>14,524</u> | <u>10,252</u> |
| Net increase in cash and cash equivalents | 301,125 | 54,849 | 132,949 |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>580,783</u> | <u>525,934</u> | <u>392,985</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u><u>\$ 881,908</u></u> | <u><u>\$ 580,783</u></u> | <u><u>\$ 525,934</u></u> |

2020. The major sources of cash included in operating activities were patient service revenues of \$2.03 billion, sales and services of \$98.7 million, and management contract services of \$39.5 million. Cash payments for operating activities were \$870.3 million to suppliers, \$713.1 million to employees for salaries, wages and fringe benefits, and \$34.1 million for management contract services.

Cash used by noncapital financing consists of transfers to the University of Kentucky for noncapital purposes of \$159.8 million offset by an inflow of cash from the provider relief fund of \$30.3 million, gifts of \$4.8 million, and payments on load from University departmental units of \$426 thousand.

Cash used by capital and related financing activities included purchases of capital assets of \$102.9 million and principal and interest payments on long-term obligations of \$47.7 million.

Investing activities included proceeds from sales and maturities of investments of \$168.0 million and interest and dividends of \$14.0 million. Cash of \$168.2 million was used to purchase investments.

2019 Versus 2018. Cash balances increased when comparing fiscal year 2019 versus fiscal year 2018 with a net increase in cash of approximately \$54.8 million. The net increase was the result of more cash provided by operating activities and cash provided by investing activities than the cash used by noncapital financing activities and capital and related financing activities.

Key Ratios

The following table shows key liquidity and capital ratios for fiscal years 2020, 2019 and 2018:

| | 2020 | 2019 | 2018 |
|--|------|------|------|
| Days cash on hand | 196 | 147 | 142 |
| Days of revenue in accounts receivable | 37 | 51 | 54 |
| Debt service coverage (times) | 8.4 | 4.5 | 3.7 |

Days cash on hand increased to 196 days in fiscal year 2020 from 147 days in fiscal year 2019. Days cash on hand measures the average number of days' expenses the System maintains in cash. In addition, the System has access to working capital from the University and quasi-endowment investments of \$311.8 million.

The days of revenue in accounts receivable measures the average number of days it takes to collect accounts receivable. In fiscal year 2020, days in accounts receivable were 37 compared to 51 days in fiscal year 2019. The decrease is primarily due to the remediation of delays in receiving payment from our Medicaid Managed Care Organizations. Daily net patient service revenue increased from \$4.5 million in 2019 to \$5.5 million in 2020, also contributing to the reduction of days of revenue in accounts receivable.

Debt service coverage ratio measures the amount of funds available to cover the principal and interest on long-term debt. The System's ratio for fiscal year 2020 is 8.4 versus 4.5 in fiscal year 2019 due to the increase in change in net position in fiscal year 2020 compared to fiscal year 2019.

Capital Asset and Debt Administration

Capital Assets. Capital assets, net of accumulated depreciation, totaled approximately \$1.06 billion at June 30, 2020, a net increase of \$44.6 million over the prior year end. Significant changes in capital assets during fiscal 2019-2020 included (in millions):

| | |
|---|-----------------------|
| Land, buildings and structures, net additions | \$ 42.8 |
| Equipment and vehicles, net additions | 15.2 |
| Capitalized software additions | 28.7 |
| Construction in process, net additions | 14.8 |
| Increase in accumulated depreciation, net | <u>(56.9)</u> |
| Total | <u><u>\$ 44.6</u></u> |

Debt. At June 30, 2020, the System had \$509.3 million in general receipts project notes outstanding and a \$10.0 million loan due to the University; \$23.3 million is included in current liabilities with the remainder long term. In addition, the System had \$25.2 million in capital leases. On February 28, 2019, approximately \$8.4 million of Surgery Blue promissory note was issued at a variable interest rate between 3.2% and 4.5%. These notes were issued for the purpose of funding construction and development Lexington Surgery Center projects. This note is a multi-draw term loan payable in full upon the maturity date and upon the terms and conditions provided in the promissory note.

Economic Factors Impacting Future Periods

The following are known facts and circumstances that will affect future financial results:

- Chandler Hospital remains No. 1 in Kentucky for the fifth consecutive year in the U.S. News & World Report's Best Hospitals rankings. Additionally, we are nationally ranked in five adult specialties. The Best Hospital designation is derived from a stringent data-driven ratings system that gauges performance in multiple clinical specialties, procedures and conditions. Scores are based on a variety of patient-outcome and care-related factors, such as mortality, patient safety and reputation. High performance in these national indicators is representative of our commitment to being an elite academic medical center dedicated to providing complex medical care in Kentucky and beyond. Annual inpatient discharges from the System are projected to be 41,744 for fiscal year 2021, an increase of 28.2% over fiscal year 2011. The annual total outpatient visits to the System are projected to be 2,303,920 in fiscal year 2021, an increase of 155.0% over fiscal year 2011.
- In 2019, the System entered into a joint venture with Lexington Surgery Center, an affiliate of Surgical Care Affiliates, LLC. This venture frees up additional surgical capacity within the System's existing surgical facilities, which helps to better serve all of our patients on a timelier basis. Flexibility with space and capacity was needed to satisfy patient demand and support faculty and clinical teams.
- Health Care systems were challenged in unprecedented ways in 2020 due to the COVID-19 outbreak. The pandemic has the potential to impact our future financial situation until the threat of the virus is controlled. COVID-19 economic challenges include lost revenue due to cancelled services, purchasing and availability of personal protective equipment, drug costs and shortages, labor costs and capital costs incurred with set up of the Nutter Field Hospital. There are also other indirect costs associated with COVID-19 which include providing child care, housing, transportation, medical screening and treatment to employees, particularly front line workers.
- COVID-19 funding opportunities like the CARES Act, Provider Relief Fund, FEMA, and other grant sources have been allocated, requested, awarded, or received for eligible expenses or lost revenue related to the disruption of the System's operation due to COVID-19 crisis. The System received \$30.3 million in Provider Relief Fund in fiscal year 2020 which are currently recognized as unearned revenue. In addition, the System is in the process of requesting FEMA reimbursement of the Nutter Field Hospital that was built in preparation of COVID-19 outbreak.

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF NET POSITION (in thousands)
JUNE 30, 2020 AND 2019

| | 2020 | 2019 |
|--|--------------|--------------|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | |
| Current Assets | | |
| Cash and cash equivalents | \$ 791,770 | \$ 399,044 |
| Accounts receivable (less allowance for doubtful accounts of \$66,221 in 2020 and \$63,724 in 2019) | 201,674 | 232,095 |
| Inventories and other assets | 50,170 | 43,204 |
| Estimated third-party payer settlements | 15,896 | 8,104 |
| Notes receivable | 2,607 | 2,671 |
| Total current assets | 1,062,117 | 685,118 |
| Noncurrent Assets | | |
| Restricted cash and cash equivalents | 90,138 | 181,739 |
| Long-term investments | 311,826 | 314,969 |
| Capital assets, net | 1,058,839 | 1,014,284 |
| Notes receivable | 3,067 | 2,963 |
| Other assets | 3,279 | 3,195 |
| Total noncurrent assets | 1,467,149 | 1,517,150 |
| Total assets | 2,529,266 | 2,202,268 |
| Deferred Outflows of Resources | | |
| Total assets and deferred outflows of resources | 2,534,815 | 2,209,074 |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | |
| Current Liabilities | | |
| Accounts payable and accrued liabilities | 144,602 | 125,439 |
| Unearned revenue | 102,339 | 63,966 |
| Long-term debt - current portion | 23,286 | 19,404 |
| Capital lease obligations - current portion | 2,150 | 4,134 |
| Total current liabilities | 272,377 | 212,943 |
| Noncurrent Liabilities | | |
| Long-term liabilities - other | 26,487 | 26,318 |
| Long-term liabilities - debt | 504,421 | 519,281 |
| Capital lease obligations | 23,066 | 19,094 |
| Total noncurrent liabilities | 553,974 | 564,693 |
| Total liabilities | 826,351 | 777,636 |
| Deferred Inflows of Resources | | |
| Total liabilities and deferred inflows of resources | 66 | 64 |
| NET POSITION | | |
| Net investment in capital assets | 535,054 | 509,782 |
| Restricted | | |
| Nonexpendable other | 1,616 | 1,590 |
| Expendable | | |
| Debt Service | — | 5 |
| Capital projects | 1,635 | 6,303 |
| Other | 10,113 | 8,359 |
| Total restricted expendable | 11,748 | 14,667 |
| Total restricted | 13,364 | 16,257 |
| Unrestricted | 1,159,980 | 905,335 |
| Total net position | \$ 1,708,398 | \$ 1,431,374 |

See notes to financial statements.

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION (in thousands)
FOR THE YEARS ENDED JUNE 30, 2020 AND 2019

| | <u>2020</u> | <u>2019</u> |
|---|---------------------|---------------------|
| OPERATING REVENUES | | |
| Net patient service revenues, less provision for doubtful accounts of \$88,388 in 2020 and \$87,808 in 2019 | \$ 2,008,383 | \$ 1,647,676 |
| Sales and services | 98,679 | 69,760 |
| Management contract revenue | <u>41,930</u> | <u>41,177</u> |
| Total operating revenues | <u>2,148,992</u> | <u>1,758,613</u> |
| OPERATING EXPENSES | | |
| Salaries and wages | 574,766 | 532,752 |
| Fringe benefits | 156,410 | 146,894 |
| Supplies | 519,551 | 431,111 |
| Purchased services | 127,455 | 96,034 |
| Other expenses | 222,405 | 195,586 |
| Depreciation | 69,025 | 66,959 |
| Management contract expenses | <u>38,970</u> | <u>38,032</u> |
| Total operating expenses | <u>1,708,582</u> | <u>1,507,368</u> |
| Net income from continuing operations | <u>440,410</u> | <u>251,245</u> |
| NONOPERATING REVENUES (EXPENSES) | | |
| Additions to permanent endowments | 26 | 335 |
| Gifts and non-exchange grants | 4,666 | 4,336 |
| Capital gifts | 104 | 59 |
| Investment income | 10,638 | 27,125 |
| Interest expense | (18,223) | (23,535) |
| Loss on disposal of capital assets | (1,510) | (861) |
| Other | <u>(1,169)</u> | <u>5,579</u> |
| Net nonoperating revenues | <u>(5,468)</u> | <u>13,038</u> |
| Net income before other revenues, expenses, gains or losses | <u>434,942</u> | <u>264,283</u> |
| Transfers to the University of Kentucky for noncapital purposes | (159,464) | (133,993) |
| Transfers from (to) the University of Kentucky for capital purposes | 1,546 | (8,224) |
| Total other expenses | <u>(157,918)</u> | <u>(142,217)</u> |
| INCREASE IN NET POSITION | 277,024 | 122,066 |
| NET POSITION, beginning of year | <u>1,431,374</u> | <u>1,309,308</u> |
| NET POSITION, end of year | <u>\$ 1,708,398</u> | <u>\$ 1,431,374</u> |

See notes to financial statements.

**UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF CASH FLOWS (in thousands)
FOR THE YEARS ENDED JUNE 30, 2020 AND 2019**

| | 2020 | 2019 |
|--|-------------------|-------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net patient service revenues | \$ 2,033,397 | \$ 1,611,041 |
| Sales and services | 98,679 | 69,760 |
| Management contract services | 39,519 | 40,644 |
| Payments to vendors and contractors | (870,254) | (721,176) |
| Salaries, wages and fringe benefits | (713,110) | (674,713) |
| Payments on management contract services | (34,143) | (38,294) |
| Other payments | (741) | (96) |
| Net cash provided by operating activities | <u>553,347</u> | <u>287,166</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | |
| Provider relief fund | 30,261 | — |
| Gifts | 4,817 | 4,247 |
| Additions to permanent endowments | 26 | 335 |
| Payments on loans from University of Kentucky departmental units | 426 | — |
| Payments to the University of Kentucky for noncapital purposes | — | 391 |
| Transfers to the University of Kentucky for noncapital purposes | (159,764) | (133,910) |
| Net cash used by noncapital financing activities | <u>(124,234)</u> | <u>(128,937)</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | |
| Purchases of capital assets | (102,942) | (69,841) |
| Principal payments-capital leases and long-term obligations | (23,673) | (22,884) |
| Interest payments-capital leases and long-term obligations | (20,020) | (25,145) |
| Proceeds from long-term obligations | 8,415 | — |
| Other capital and related financing payments | (5,101) | (836) |
| Transfers from the University of Kentucky for capital purposes | 1,546 | 802 |
| Net cash used by capital and related financing activities | <u>(141,775)</u> | <u>(117,904)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Proceeds from sales and maturities of investments | 167,995 | 154,947 |
| Purchase of investments | (168,198) | (152,671) |
| Interest and dividends on investments | 13,990 | 12,248 |
| Net cash provided by investing activities | <u>13,787</u> | <u>14,524</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | <u>301,125</u> | <u>54,849</u> |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>580,783</u> | <u>525,934</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 881,908</u> | <u>\$ 580,783</u> |
| Reconciliation of net income from continuing operations to net cash provided by operating activities: | | |
| Net income from continuing operations | \$ 440,410 | \$ 251,245 |
| Adjustments to reconcile net income from continuing operations to net cash provided by operating activities: | | |
| Depreciation | 69,025 | 66,959 |
| Write off of principal note/lease receivable | 633 | 1,031 |
| Provision for doubtful accounts | (88,388) | (87,808) |
| Change in assets and liabilities: | | |
| Accounts receivable | 118,809 | 90,563 |
| Inventories and other | (6,965) | (4,755) |
| Estimated third-party payer settlements receivable and payable | (7,791) | (60,267) |
| Other assets | (1,236) | 752 |
| Accounts payable and accrued liabilities | 20,751 | 5,397 |
| Unearned revenue | 8,110 | 24,049 |
| Long-term liabilities | (11) | — |
| Net cash provided by operating activities | <u>\$ 553,347</u> | <u>\$ 287,166</u> |
| NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES: | | |
| Transfer of capital assets (to) from UK | \$ 2,777 | \$ (9,026) |
| Capital lease additions | \$ 6,267 | \$ 290 |
| Capital lease additions by Lexington Surgery Center | \$ 1,811 | \$ — |
| Capital asset change in accounts payable | \$ 2,791 | \$ (4,299) |
| Capitalized interest, net of investment income | \$ 1,584 | \$ 806 |
| Amortized bond premium | \$ 3,986 | \$ 4,195 |
| Amortized difference between reacquisition price and net carrying amount of refunded debt | \$ 1,257 | \$ 1,337 |
| Investment unrealized gains (losses) | \$ (6,682) | \$ 10,507 |

See notes to financial statements.

**UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2020 AND 2019**

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The UK HealthCare Hospital System (the System) is an organizational unit of the University of Kentucky (the University) which 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 System include Albert B. Chandler University Hospital including Kentucky Children's Hospital (collectively Chandler); UK HealthCare Good Samaritan Hospital (Good Samaritan); Kentucky Healthcare Enterprise, Inc. (KHE), a wholly owned for-profit subsidiary, which has no balances or transactions as or and for the years ended June 30, 2020 or 2019; and Surgery Blue, LLC, a wholly owned for-profit subsidiary, and its for-profit subsidiary, Surgery Center of Lexington, LLC (51% ownership). Surgery Blue, LLC was established in August 2018. The Surgery Center of Lexington, LLC has a calendar-year basis fiscal year from January 1 through December 31. Therefore, the financial statements of Surgery Center of Lexington, LLC as of December 31, 2019 and 2018 are included in the System's financial statements as of June 30, 2020 and 2019, respectively.

The System provides inpatient, outpatient, and emergency care services for residents of the Commonwealth.

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 Governmental Accounting Standards Board (GASB). GASB establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following 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 it be maintained permanently by the System.
Expendable - Net position whose use by the System is subject to externally imposed stipulations that can be fulfilled by actions of the System pursuant to those stipulations or that expire by the passage of time.
- Unrestricted: Net position whose use by the System 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 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 System's assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues, expenses, changes in net position, and cash flows.

Summary of Significant Accounting Policies

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

Cash and Cash Equivalents. The System considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. The System also considers investments held in the Commonwealth's investment pools to be cash equivalents.

Noncurrent cash and cash equivalents include the System's plant funds allocated for capital projects, with the exception of unrestricted renewal and replacement cash, which is included in current cash and cash equivalents, and endowment fund cash pending transfer to the custodian for investment. Cash and cash equivalents held by the University's endowment fund managers are included in long-term investments.

Accounts Receivable. The System reports patient accounts receivable for services rendered at net realizable amounts from third-party payers and others. The System provides an allowance for doubtful accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

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

Long-term Investments. The System's endowment investments are administered as part of the University's pooled endowment funds and held in external trusts. All endowments are managed in a consolidated investment pool which consists of more than 2,300 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 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.

Pooled Endowment 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 whose long-term objective is 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" spending policy, which includes both the market value of the endowment and the current level of inflation in determining spending each year. Annual spending will be 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 will be constrained so that the calculated rate is at least 3.5 percent, and not more than five percent, of the current endowment market value.

The University also utilized an endowment management fee to support internal management and fundraising costs related to the endowment. The 2020 University's annual endowment management fee was 0.90%. This is an increase from the 2019 management fee of 0.82%.

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.

For each of the years ended June 30, 2020 and 2019, management elected to retain the spending distribution in the quasi-endowment and the amounts available for spending in accordance with the University's endowment spending policy were \$11.5 million and \$11.0 million, respectively.

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

The System 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 System 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 borrowings.

Equipment with a unit cost of \$5,000 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 40 years for buildings, 10 - 25 years for land and building improvements and infrastructure, 3 - 20 years for equipment and vehicles and 10 years for capitalized software.

Title to all capital assets of the System belongs to the University. The financial information relating to capital assets represents assets that the System occupies and uses. Transfer of capital assets to/from the University represents changes in control of individual assets within divisions of the University from one period to another.

The System evaluates capital assets for impairment whenever events or circumstances indicate a significant, unexpected decline in the service utility of a capital asset has occurred. If a capital asset is tested for impairment and the magnitude of the decline in service utility is significant and unexpected, the accumulated depreciation will be accelerated. The amount of the impairment loss will be recorded as the net book value divided proportionately over its remaining years of useful life. No asset impairment was recognized during the years ended June 30, 2020 and 2019.

Deferred Outflows of Resources. A deferred outflow of resources is a loss in net position by the System 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 \$5.5 million and \$6.8 million as of June 30, 2020 and 2019, respectively, consisted of the unamortized difference between the reacquisition price and the net carrying amount of the refunded debt. The System issued General Receipts 2014 Bonds Series D to refund General Receipts 2005 Notes Series A which was originally issued to fund the construction of the Patient

Care Facility. General Receipts Notes 2007 Series A and B originally issued to fund construction of the Patient Care Facility were refunded by the General Receipts 2015 Bond Series B.

Unearned Revenue. Unearned revenue consists of funds generated from the Kentucky AIDS Drug Assistance Program (KADAP) to be used for allowable costs within the program, and other unearned amounts. KADAP is governed by the Public Health office and administered by the System. The funds are to support the operations of KADAP Income Reinvestment Program.

Compensated Absences. The amount of vacation leave earned but not taken by employees at June 30, 2020 is recorded as a liability by the System. Temporary disability leave payable upon termination under the University's payout policy is also recorded as a liability on the University's financial statements. 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 System 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. Deferred inflows of resources of \$66,000 as of June 30, 2020 and \$64,000 as of June 30, 2019 consisted of the beneficial interest from an irrevocable external trust that the system will receive in future years.

Net Patient Service Revenues. Net patient service 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 and include 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 39% and 20%, respectively, of the System's net patient service revenues before the provision for doubtful accounts for the year ended June 30, 2020 and approximately 24% and 26%, respectively, for the year ended June 30, 2019. 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 the impact of COVID and unemployment, more Kentuckians applied and received presumptive Medicaid. These changes have an impact on both Medicaid and Medicaid Disproportionate Share Hospital (DSH) payments. Fiscal year 2019 Medicaid DSH payments were recognized during that fiscal year as the amount was adjusted for dual eligible patient payments that were ruled to be applicable to the Medicaid DSH survey. Prior year audits were completed and the System was able to recognize \$61.4 million of DSH revenue and other settlements during fiscal year 2019, of which \$51.5 million was previously reserved in estimated third-party payer

settlements in 2018 statement of net position. The calculation methodology for supplemental payments was adjusted during fiscal year 2020 and is now referred to as "Directed Payments". These new payments replace the Managed Care Organization's portion of Intensity Operating Allowance and Physician Supplemental Payment. With Directed Payments, there is no longer an uncompensated gap that is typically filled with Medicaid DSH payments. Therefore, the System does not qualify for Medicaid DSH payments for fiscal year 2020. The Directed Payments are the difference between the System's average commercial rate and the rates Medicaid Managed Care Organizations pay for healthcare services. The payments are applicable to both inpatient and outpatient hospital services. A per day and per visit gap has been calculated and is applied to Medicaid Managed Care volume. The program is based upon data two years in arrears. The payments are based upon two components: access and quality. For fiscal year 2020, access is 95% of the program and quality is 5%. The Commonwealth withholds the quality component as well as an additional 5% for reconciliation, which occurs 14 months following the end of the first quarter, i.e., November 2020 for July through September 2019. A receivable for these dollars has been applied to the third party liability account for fiscal year 2020. Directed Payments of \$391.6 million was recognized in net patient service revenue in fiscal year 2020.

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.

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 \$35.9 million, and \$2.1 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, 2020 to June 30, 2021 with substantially the same terms.

Charity Care. 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 services and supplies furnished under the System's charity care policy aggregated to approximately \$65.1 million and \$73.7 million in 2020 and 2019, respectively. The costs of charity care provided under the System's charity care policy were \$17.2 million and \$19.5 million for 2020 and 2019, respectively. The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges.

Provider Relief Funds. The Coronavirus Aid, Relief, and Economic Security (CARES) Act was passed by Congress and signed into law by President Donald Trump on March 27, 2020. This over \$2 trillion economic relief package delivers on the federal government's commitment to protecting the American people from the public health and economic impacts of COVID-19. Based on the CARES Act, the federal government distributed direct payments through the Provider Relief Fund to the System in the amount of \$30.3 million which was recognized as unearned revenue in the Statement of Net Position. To receive from the Provider Relief Fund, a provider must have billed Medicare fee-for-services and provide diagnoses, testing, or care for individuals with possible or actual cases of COVID-19. Provider Relief Funds, if used within the terms and conditions of the program, do not need to be repaid to the federal government. The provider is required to use the payments for healthcare related expenses or lost revenues that are attributable to coronavirus. If the System has unused funds at the earlier of either the end of the pandemic or June 30, 2021, those funds will need to be returned. Appropriate expenses include healthcare-related expenses or lost revenue due to the coronavirus, which includes prevention, preparation, training, reporting, treatment, and declined services. The Provider Relief Funds are subject to government oversight, including potential audits. On September 19, 2020, additional guidance was released by the U.S. Department of Health and Human Services related to the CARES Act which could impact the amount recognized by the System in the near term.

Income Taxes. The University, of which the System is an organizational unit, 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.

Restricted Asset Spending Policy. The System's policy is that restrictions on assets cannot be fulfilled by the expenditure of unrestricted funds for similar purposes. The determination of 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 System 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 System's revenues and expenses are from exchange transactions. Certain revenues relied upon for operations, such as state appropriations, gifts and investment income, are recorded as non-operating revenues, in accordance with GASB Statement No. 35.

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 contractual allowances, allowances for doubtful accounts, estimated third-party payer settlements and estimated medical claims payable.

Recent Accounting Pronouncements. As of June 30, 2020, the GASB has issued the following applicable statements to the System but are not yet implemented.

- 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). Due to the COVID-19 pandemic, GASB issued statement No. 95 thus extending the provisions of this statement by one year to fiscal year 2021. This statement provides guidance regarding the identification of fiduciary activities for accounting and financial reporting purposes; and will require the System to include fiduciary fund financial statements for material fiduciary activities before the notes to the financial statements. The University has determined GASB Statement No. 84 will have no material impact on its financial statements. As an organizational unit of the University, the System has no fiduciary activities and statement No. 84 will have no 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). Due to the COVID-19 pandemic, GASB issued statement No. 95 thus extending the provisions of this statement by 18 months to fiscal year 2022. 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 System has yet to determine the impact statement No. 87 will have on its financial statements.
- GASB Statement No. 89, *Accounting for Interest Cost Incurred before the end of a Construction Period*, issued June 2018. The provisions of the statement are effective for fiscal years beginning after December 15, 2019 (fiscal year 2021). Due to the COVID-19 pandemic, GASB issued statement No. 95 thus extending the provisions of this statement by one year to fiscal year 2022. This statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest cost incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-

type activity or enterprise fund. The System has yet to determine the impact statement No. 89 will have on its financial statements.

2. DEPOSITS AND INVESTMENTS

The fair value of deposit and investment, by Statement of Net Position classification, at June 30, 2020 and 2019 are as follows (in thousands):

| | 2020 | 2019 |
|---|--------------|------------|
| Statement of Net Position classification: | | |
| Cash and cash equivalents | \$ 791,770 | \$ 399,044 |
| Restricted cash and cash equivalents | 90,138 | 181,739 |
| Total cash and cash equivalents | 881,908 | 580,783 |
| Long-term investments | 311,826 | 314,969 |
| Total Deposits and Investments | \$ 1,193,734 | \$ 895,752 |

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

The System has the following valuation measurements, by type, at June 30, 2020 and 2019 (in thousands):

| | 2020 | | | | | |
|---|------------------------------|---|---|--|------------------------------------|------------------------------------|
| | 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 | Amortized or Historical Cost |
| Cash and cash equivalents | \$ 881,908 | \$ — | \$ — | \$ — | \$ — | \$ 881,908 |
| Cash surrender value of life insurance policies | 651 | — | — | — | — | 651 |
| University's pooled endowment fund | 311,175 | — | — | 311,175 | 311,175 | — |
| Total deposits and investments | \$ 1,193,734 | \$ — | \$ — | \$ 311,175 | \$ 311,175 | \$ 882,559 |

| | 2019 | | | | | |
|---|------------------------------|---|---|--|------------------------------------|------------------------------------|
| | 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 | Amortized or Historical Cost |
| Cash and cash equivalents | \$ 580,783 | \$ — | \$ — | \$ — | \$ — | \$ 580,783 |
| Cash surrender value of life insurance policies | 658 | — | — | — | — | 658 |
| University's pooled endowment fund | 314,311 | — | — | 314,311 | 314,311 | — |
| Total deposits and investments | \$ 895,752 | \$ — | \$ — | \$ 314,311 | \$ 314,311 | \$ 581,441 |

Where quoted market prices are available in an active market, securities are classified within level 1 of the valuation hierarchy. If quoted 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.

The investment in University pooled endowment fund is derived based on the per unit calculation as described in footnote 1, thus is deemed to be a level 3 investment. For more information regarding the fair value measurements, refer to the University's financial statements, footnote 2. There have been no significant changes in the valuation techniques during the year ended June 30, 2020.

The composition of the University's pooled endowment fund based upon fair value at June 30, 2020 and 2019 is as follows:

| | 2020 | 2019 |
|---|---------|---------|
| Cash and cash equivalents | 0.3 % | 0.2 % |
| Diversifying strategies | 14.0 % | 14.9 % |
| Global equity - hedged | 5.9 % | 6.0 % |
| Global equity - international | 14.8 % | 17.6 % |
| Global equity - private | 19.9 % | 16.1 % |
| Global equity - U.S. | 15.2 % | 12.4 % |
| Global fixed income - high quality/rate sensitive | 6.0 % | 6.9 % |
| Global fixed income - private credit | 2.8 % | 3.1 % |
| Global fixed income - public credit | 5.0 % | 5.8 % |
| Real assets - private | 10.5 % | 10.0 % |
| Real assets - public | 5.6 % | 7.0 % |
| Total | 100.0 % | 100.0 % |

Deposit and Investment Policies. The System 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 System's funds.

For purposes of investment management, the System's deposits and investments can be grouped into two significant categories:

- Cash and cash equivalents on deposit with the University, which the University invests in deposits with banks and the Commonwealth. The University also invests cash on deposit in money market funds and the University's pooled endowment fund.
- Endowment investments in the University's pooled endowment fund.

Cash and cash equivalents on deposit with the University are managed based on the University's Operating Fund Investment Policy established by the Treasurer of the University.

Endowment investments are managed within the guidelines established by the University's Endowment Investment Policy, as approved by the Investment Committee of the University's Board of Trustees, which governs the University's pooled endowment fund.

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

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligation, causing the System 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:

- Cash and cash equivalents on deposit with the University are governed by policy that minimizes risk in several ways. The University's deposits in Federal Deposit Insurance Corporation (FDIC) insured financial institutions are covered up to \$250,000 at each FDIC insured institution. State law requires that deposits in excess of this coverage be fully collateralized, therefore depository institutions issue a pledge of specific U.S. Treasury or agency securities, held in the name of the University by the

Federal Reserve Bank, to cover all amounts over the \$250,000 coverage.

- Deposits with the Commonwealth consist of securities eligible for short-term investments under state law. The University invests a portion of its operating cash in a diversified pool of money market funds. Fund investments include U.S. Treasury and agency securities, certificates of deposit, commercial paper, repurchase agreements and other short-term fixed income securities.
- Endowment managers are permitted to use derivative instruments to limit credit risk.

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of the failure of the counterparty, the System 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:

- Cash and cash equivalents on deposit with the University invested in deposits and money market funds are held in the University's name by various financial institutions. Deposits with the Commonwealth are held in the Commonwealth's name. The University maintains records evidencing the System's ownership interest in such balances.
- Endowment investments are held in the University's name by the University's custodian. The University maintains records of the System's ownership interest (units) in the University's pooled endowment fund.

Concentrations of Credit Risk. The System's 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:

- Cash and cash equivalents on deposit with the University are not limited as to the maximum amount that may be invested in one issuer. However, the University's cash 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.
- The University's 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 to the Organization for Economic Cooperation and Development and U.S. agencies.

At June 30, 2020 and 2019, the System had no investments in any one issuer that represented five percent or more of total investments, other than U.S. Treasury and agency obligations.

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:

- Cash and cash equivalents on deposit with the University 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.
- Endowment managers are permitted to use derivative instruments to limit interest rate risk. Additionally, endowment investments held by the University's core-plus fixed income manager are limited to a duration that is within two years of the duration of the Barclays U.S. Intermediate Aggregate Bond Index and unconstrained fixed income strategies have been implemented to further mitigate interest rate risk.

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 System's exposure to foreign currency risk derives from certain endowment investments of the University's pooled endowment fund. The University's 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.

3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, as of June 30, 2020 and 2019 are as follows (in thousands):

| | 2020 | | |
|--|---------------------|--------------------|-------------------|
| | Gross Receivable | Allowance | Net Receivable |
| Medicare, Medicaid and other third parties | \$ 252,307 | \$ (59,767) | \$ 192,540 |
| Private pay | 15,259 | (6,280) | 8,979 |
| Pledges receivable (less discount of \$12) | 329 | (174) | 155 |
| Total | <u>\$ 267,895</u> | <u>\$ (66,221)</u> | <u>\$ 201,674</u> |

| | 2019 | | |
|--|---------------------|--------------------|-------------------|
| | Gross Receivable | Allowance | Net Receivable |
| Medicare, Medicaid and other third parties | \$ 278,441 | \$ (57,134) | \$ 221,307 |
| Private pay | 17,030 | (6,442) | 10,588 |
| Pledges receivable (less discount of \$10) | 348 | (148) | 200 |
| Total | <u>\$ 295,819</u> | <u>\$ (63,724)</u> | <u>\$ 232,095</u> |

The above pledges receivable are shown net of present value discount.

In accordance with GASB Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions, the System is required to record operating and capital pledges as revenue when all eligibility requirements have been met. For the years ended June 30, 2020 and 2019, the System recorded the discounted value of operating and capital pledges using a rate of two percent.

The System has recorded an allowance for uncollectible patient accounts receivable equal to 27.0% and 22.4% of patient accounts receivable as of June 30, 2020 and 2019, respectively. A summary of the changes in the allowance for uncollectible patient accounts receivable is as follows:

| | 2020 | 2019 |
|--|------------------|------------------|
| Balance, beginning of year | \$ 63,724 | \$ 89,030 |
| Provision for bad debts | 88,388 | 87,808 |
| Receivables charged off, net of recoveries | (85,891) | (113,114) |
| Balance, end of year | <u>\$ 66,221</u> | <u>\$ 63,724</u> |

4. CAPITAL ASSETS, NET

Capital assets as of June 30, 2020 and capital asset activity for the year ended June 30, 2020 are summarized as follows (in thousands):

| | Beginning Balance | Additions | Deletions | Ending Balance |
|-----------------------------------|----------------------|------------------|------------------|---------------------|
| Land | \$ 31,406 | \$ — | \$ — | \$ 31,406 |
| Non-depreciable land improvements | 17,859 | 950 | — | 18,809 |
| Depreciable land improvements | 9,081 | 251 | — | 9,332 |
| Buildings | 999,438 | 38,346 | 792 | 1,036,992 |
| Fixed equipment | 41,433 | 3,997 | — | 45,430 |
| Infrastructure | 31,859 | — | — | 31,859 |
| Equipment | 321,389 | 29,621 | 14,734 | 336,276 |
| Vehicles | 1,281 | 322 | 36 | 1,567 |
| Capitalized software | 112,001 | 28,710 | — | 140,711 |
| Artwork | 2,863 | 25 | — | 2,888 |
| Construction in process | 22,200 | 31,159 | 16,375 | 36,984 |
| Certificate of need | 11,609 | — | — | 11,609 |
| | <u>1,602,419</u> | <u>133,381</u> | <u>31,937</u> | <u>1,703,863</u> |
| <u>Accumulated Depreciation:</u> | | | | |
| Depreciable land improvements | 6,251 | 321 | — | 6,572 |
| Buildings | 274,564 | 26,281 | 656 | 300,189 |
| Fixed equipment | 23,858 | 3,335 | — | 27,193 |
| Infrastructure | 10,944 | 1,275 | — | 12,219 |
| Equipment | 204,599 | 30,770 | 13,255 | 222,114 |
| Vehicles | 908 | 172 | 36 | 1,044 |
| Capitalized software | 67,011 | 8,682 | — | 75,693 |
| | <u>588,135</u> | <u>70,836</u> | <u>13,947</u> | <u>645,024</u> |
| Capital assets, net | <u>\$ 1,014,284</u> | <u>\$ 62,545</u> | <u>\$ 17,990</u> | <u>\$ 1,058,839</u> |

Capital assets as of June 30, 2019 and capital asset activity for the year ended June 30, 2019 are summarized as follows (in thousands):

| | Beginning Balance | Additions | Deletions | Ending Balance |
|-----------------------------------|----------------------|-------------------|-----------------|---------------------|
| Land | \$ 30,861 | \$ 545 | \$ — | \$ 31,406 |
| Non-depreciable land improvements | 17,859 | — | — | 17,859 |
| Depreciable land improvements | 9,081 | — | — | 9,081 |
| Buildings | 991,876 | 8,676 | 1,114 | 999,438 |
| Fixed equipment | 39,868 | 1,574 | 9 | 41,433 |
| Infrastructure | 31,859 | — | — | 31,859 |
| Equipment | 301,296 | 34,871 | 14,778 | 321,389 |
| Vehicles | 1,137 | 144 | — | 1,281 |
| Capitalized software | 111,235 | 766 | — | 112,001 |
| Artwork | 2,805 | 58 | — | 2,863 |
| Construction in process | 9,720 | 16,732 | 4,252 | 22,200 |
| Certificate of need | 11,609 | — | — | 11,609 |
| | <u>1,559,206</u> | <u>63,366</u> | <u>20,153</u> | <u>1,602,419</u> |
| <u>Accumulated Depreciation:</u> | | | | |
| Depreciable land improvements | 5,937 | 314 | — | 6,251 |
| Buildings | 250,019 | 24,545 | — | 274,564 |
| Fixed equipment | 20,685 | 3,173 | — | 23,858 |
| Infrastructure | 9,669 | 1,275 | — | 10,944 |
| Equipment | 191,118 | 28,259 | 14,778 | 204,599 |
| Vehicles | 699 | 209 | — | 908 |
| Capitalized software | 57,827 | 9,184 | — | 67,011 |
| | <u>535,954</u> | <u>66,959</u> | <u>14,778</u> | <u>588,135</u> |
| Capital assets, net | <u>\$ 1,023,252</u> | <u>\$ (3,593)</u> | <u>\$ 5,375</u> | <u>\$ 1,014,284</u> |

Additions to equipment and depreciation included equipment purchased by the Surgery Center of Lexington, LLC, of \$1,811 thousand for both cost and depreciation in fiscal year 2020.

At June 30, 2020, the System has commitments in construction projects in progress totaling approximately \$192.1 million in scope. The estimated cost to complete these projects was approximately \$151.2 million. Such construction is principally financed by the System's cash reserves, loans from the University and proceeds from the System general receipts bonds.

Interest costs incurred during construction, net of related investment income, are capitalized. Total interest capitalized was \$1.6 million for 2020 and \$806,000 for 2019.

During 2020 and 2019, the System utilized capital leases to acquire various items of equipment. The net book value for capitalized leased land, buildings and equipment is \$50.0 million and \$38.3 million at June 30, 2020 and 2019, respectively. The net book value for capitalized leased land, buildings and equipment for the Surgery Center of Lexington, LLC, is \$14.0 million and \$0 at June 30, 2020 and 2019, respectively.

5. NOTES RECEIVABLE

Notes receivable at June 30, 2020 and 2019 are as follows (in thousands):

| | <u>2020</u> | <u>2019</u> |
|---|-----------------|-----------------|
| Non-interest bearing, unsecured receivable from UK College of Pharmacy | \$ 3,367 | \$ 3,734 |
| Non-interest bearing, unsecured receivable from UK College of Nursing | 2,307 | 1,900 |
| Total | <u>\$ 5,674</u> | <u>\$ 5,634</u> |
| Current portion | \$ 2,607 | \$ 2,671 |
| Noncurrent portion | 3,067 | 2,963 |
| Total | <u>\$ 5,674</u> | <u>\$ 5,634</u> |

6. OTHER ASSETS

Other assets at June 30, 2020 and 2019 are as follows (in thousands):

| | <u>2020</u> | <u>2019</u> |
|--|-----------------|-----------------|
| Amounts on deposit with trustee | \$ 67 | \$ 72 |
| Noncurrent portion of prepaid expenses | 490 | 339 |
| Pledges receivable noncurrent, net | 553 | 601 |
| Goodwill | 2,169 | 2,183 |
| Total | <u>\$ 3,279</u> | <u>\$ 3,195</u> |

The amounts on deposit with the trustee represent cash equivalents, measured as a level 1 on the fair value hierarchy as discussed in note 2.

7. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2020 and 2019 are summarized as follows (in thousands):

| | <u>2020</u> | <u>2019</u> |
|--|-------------------|-------------------|
| Payable to vendors and contractors | \$ 71,188 | \$ 58,385 |
| Due to the University of Kentucky | 6,244 | 5,676 |
| Accrued expenses, including vacation leave | 67,170 | 61,378 |
| Total | <u>\$ 144,602</u> | <u>\$ 125,439</u> |

8. LONG-TERM DEBT

Long-term debt as of June 30, 2020 and 2019 are summarized as follows (in thousands):

| | 2020 | | | | | |
|-----------------------------------|-------------------|-----------------|------------------|-------------------|------------------|--------------------|
| | Beginning Balance | Additions | Reductions | Ending Balance | Current Portion | Noncurrent Portion |
| General Receipts | | | | | | |
| Project Notes | \$ 525,537 | \$ — | \$ 16,270 | \$ 509,267 | \$ 19,325 | \$ 489,942 |
| Note Payable | — | 8,415 | 6 | 8,409 | 733 | 7,676 |
| Due to the University of Kentucky | 13,148 | — | 3,117 | 10,031 | 3,228 | 6,803 |
| Total | <u>\$ 538,685</u> | <u>\$ 8,415</u> | <u>\$ 19,393</u> | <u>\$ 527,707</u> | <u>\$ 23,286</u> | <u>\$ 504,421</u> |
| | | | | | | |
| | 2019 | | | | | |
| | Beginning Balance | Additions | Reductions | Ending Balance | Current Portion | Noncurrent Portion |
| General Receipts | | | | | | |
| Project Notes | \$ 541,403 | \$ — | \$ 15,866 | \$ 525,537 | \$ 16,271 | \$ 509,266 |
| Due to the University of Kentucky | 16,183 | — | 3,035 | 13,148 | 3,133 | 10,015 |
| Total | <u>\$ 557,586</u> | <u>\$ —</u> | <u>\$ 18,901</u> | <u>\$ 538,685</u> | <u>\$ 19,404</u> | <u>\$ 519,281</u> |

Principal maturities and interest on long-term debt for the next five years and in subsequent five-year periods as of June 30, 2020 are as follows (in thousands):

| | Principal | Interest | Total |
|-----------|-------------------|-------------------|-------------------|
| 2021 | 23,286 | 22,259 | 45,545 |
| 2022 | 31,287 | 21,157 | 52,444 |
| 2023 | 24,700 | 20,007 | 44,707 |
| 2024 | 22,380 | 18,801 | 41,181 |
| 2025-2029 | 117,689 | 76,870 | 194,559 |
| 2030-2034 | 99,255 | 53,295 | 152,550 |
| 2035-2039 | 118,350 | 31,624 | 149,974 |
| 2040-2044 | 73,450 | 10,160 | 83,610 |
| 2045-2048 | 17,310 | 824 | 18,134 |
| Total | <u>\$ 527,707</u> | <u>\$ 254,997</u> | <u>\$ 782,704</u> |

Bond premiums, which are included in current and noncurrent accrued liabilities, are amortized over the life of the bond using the effective interest method.

The general receipts project notes consist of bonds in the original amount of \$552.4 million dated November 24, 2009 through February 20, 2018, which bear interest at 2.34% to 3.65%. The bonds are payable in annual installments through June 30, 2048. The System is required to make semi-annual deposits of varying amounts to the debt service funds held by the trustees. The bonds are secured by pledged revenues of the University, which include the net revenues of the System.

On November 24, 2009, \$100.6 million of the University of Kentucky General Receipts 2009 Bonds Series B were issued at a net interest cost of 3.59%. These bonds were issued as Build America Bonds (BAB)

as authorized under the American Recovery and Reinvestment Act of 2009. The System will receive an annual cash subsidy from the U.S. Treasury equal to 35% of the interest payable on the bonds. This subsidy, which was approximately \$1.7 million and \$1.7 million during fiscal years 2020 and 2019, respectively, is 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 on reducing the budgetary authority in accounts subject to sequestration. As a result, the BAB subsidy was reduced to approximately 33% in 2020 and 2019.

On July 30, 2010, the System entered into an unsecured internal loan agreement with the University to acquire funding for construction of a suite of operating rooms in the newly constructed patient care facility. Funds were transferred to the construction project as needed and will be repaid over a ten year period. Interest shall be charged based on the historical performance of the two-year U.S. Treasury note plus (1.0%). The total effective rate was 3.56% for interest payments in 2020 and 3.21% in 2019. The annual interest rate will be determined March 1 and be effective for the following fiscal year.

On February 28, 2019, approximately \$8.4 million of Surgery Blue promissory note was issued at a variable interest rate between 3.2% and 4.5%. These notes were issued for the purpose of funding construction and development Lexington Surgery Center projects. This note is a multi-draw term loan payable in full upon the maturity date and upon the terms and conditions provided in the promissory note.

9. CAPITAL LEASE OBLIGATIONS

Capital lease obligations as of June 30, 2020 and 2019 are summarized as follows (in thousands):

| 2020 | | | | | |
|-------------------|-----------|------------|----------------|-----------------|--------------------|
| Beginning Balance | Additions | Reductions | Ending Balance | Current Portion | Noncurrent Portion |
| \$ 23,228 | \$ 6,267 | \$ 4,279 | \$ 25,216 | \$ 2,150 | \$ 23,066 |
| 2019 | | | | | |
| Beginning Balance | Additions | Reductions | Ending Balance | Current Portion | Noncurrent Portion |
| \$ 26,921 | \$ 290 | \$ 3,983 | \$ 23,228 | \$ 4,134 | \$ 19,094 |

Scheduled payments of capital lease obligations are as follows (in thousands):

| Years ended June 30 | |
|---|-----------|
| 2021 | \$ 3,316 |
| 2022 | 3,315 |
| 2023 | 3,270 |
| 2024 | 3,226 |
| 2025 | 3,163 |
| 2026 and later | 17,224 |
| Total | 33,514 |
| Less amount representing interest | (8,298) |
| Present value of net minimum lease payments | \$ 25,216 |

Capital lease obligations are at varying rates of imputed interest of 0.95% to 4.45%.

10. LONG-TERM LIABILITIES - OTHER

Other long-term liabilities as of June 30, 2020 and 2019 are summarized as follows (in thousands):

| | 2020 | | | |
|-------------------------------------|-------------------|---------------|---------------|------------------|
| | Beginning Balance | Additions | Reductions | Ending Balance |
| Refundable deposits | \$ 21 | \$ — | \$ 11 | \$ 10 |
| Workers compensation | 339 | — | 119 | 220 |
| Noncurrent construction retainage | 85 | 384 | 85 | 384 |
| Noncurrent unamortized bond premium | 25,873 | — | — | 25,873 |
| Long-term liabilities - other | <u>\$ 26,318</u> | <u>\$ 384</u> | <u>\$ 215</u> | <u>\$ 26,487</u> |

| | 2019 | | | |
|-------------------------------------|-------------------|---------------|-----------------|------------------|
| | Beginning Balance | Additions | Reductions | Ending Balance |
| Refundable deposits | \$ 10 | \$ 11 | \$ — | \$ 21 |
| Workers compensation | 240 | 99 | — | 339 |
| Noncurrent construction retainage | — | 85 | — | 85 |
| Noncurrent unamortized bond premium | 29,859 | — | 3,986 | 25,873 |
| Long-term liabilities - other | <u>\$ 30,109</u> | <u>\$ 195</u> | <u>\$ 3,986</u> | <u>\$ 26,318</u> |

11. DESIGNATIONS OF UNRESTRICTED NET POSITION

Unrestricted net position is designated for specific purposes by action of the University's Board of Trustees or management or may otherwise be limited by contractual obligations. Commitments for the use of unrestricted net position at June 30, 2020 and 2019 are as follows (in thousands):

| | 2020 | 2019 |
|------------------------------|---------------------|-------------------|
| Working capital requirements | \$ 757,586 | \$ 442,113 |
| Future capital expenditures | 402,394 | 463,222 |
| Total | <u>\$ 1,159,980</u> | <u>\$ 905,335</u> |

12. INVESTMENT INCOME (LOSS)

Components of investment income for the years ended June 30, 2020 and 2019 are as follows (in thousands):

| | 2020 | 2019 |
|---|------------------|------------------|
| Interest and dividends earned on endowment investments | \$ 3,542 | \$ 5,076 |
| Realized and unrealized gains (losses) on endowment investments | (4,385) | 12,572 |
| Interest and dividends on cash and non-endowment investments | 11,040 | 9,446 |
| Realized and unrealized gains on non-endowment investments | 441 | 31 |
| Total | <u>\$ 10,638</u> | <u>\$ 27,125</u> |

13. PLEDGED REVENUES

The University has substantially pledged all of the unrestricted operating and nonoperating revenues, including the System revenues, to repay the general receipts bonds and notes issued during 2009 to 2018. Only the General Receipts 2009 Bonds Series B, General Receipts Bonds 2014 Series D, General Receipts Bonds 2015 Series A and B and General Receipts 2018 Bonds Series A are reflected as the System debt. Proceeds from the bonds and notes provided funding for the construction of the new patient care facility and the refunding of previously issued notes. The bonds and notes are payable from unrestricted operating and nonoperating revenues and are payable through 2048. Annual principal and interest payments on bonds and notes are expected to require less than three percent of pledged revenues. The total principal and interest remaining to be paid on the bonds and notes is \$763.5 million and \$802.6 million in 2020 and 2019, respectively. Principal and interest paid for each of the years ended June 30, 2020 and 2019 was \$37.2 million and \$38.3 million, respectively.

14. RETIREMENT PLANS

Regular full-time employees of the System are participants in the University of Kentucky Retirement Plan, a defined contribution plan. System employees participate in one of the following three groups of the University of Kentucky Retirement Plan:

| | |
|-----------|--|
| 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. |

Participation in these groups of the University of Kentucky Retirement Plan is mandatory for all regular full-time employees age 30 and older. Participation is voluntary until age 30. The System contributes 10% and each employee contributes five percent of eligible compensation. 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. Due to the COVID-19 pandemic and fiscal responsibility, the University has decided to lower the retirement plan contributions to 5% for fiscal year 2021.

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

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

In addition to retirement benefits provided from the group retirement plan, the University provides supplemental retirement income benefits to certain eligible employees of the University.

The total contributions charged to operations for the various retirement plans were approximately \$40.4 million and \$38.0 million for the years ended June 30, 2020 and 2019, respectively. Employees contributed \$20.2 million and \$19.0 million during 2020 and 2019, respectively. The payroll for employees covered by the retirement plans was \$403.9 million and \$379.7 million for 2020 and 2019, respectively.

15. HEALTH INSURANCE BENEFITS FOR RETIREES

The University administers a single-employer defined-benefit healthcare plan including medical and prescription drug benefits. The plan provides lifetime healthcare insurance benefits for eligible retirees and their surviving spouses. Human Resources Policies and Procedures define retiree health benefits and can be amended by the President of the University as delegated by the University's Board of Trustees.

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 percent of the “true retiree” cost of the post-65 medical plan. However, retirees must pay the greater of \$25 per month or 10% of total plan cost.

The University has established a trust fund to segregate plan assets, and the contribution requirements of plan members and the University are established and may be amended by the President of the University. The University contributed to the OPEB trust based on a funding policy supported by an actuarial study in accordance with the parameters of GASB Statement No. 75.

As an organizational unit of the University, the System has recognized its share of the contribution in employee benefit costs and has no additional liability for this benefit at June 30, 2020.

16. RISK MANAGEMENT

The University, of which the System is an organizational unit, is exposed to various risks of loss related to torts; theft of, damage to, and 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 Fund), (2) Sovereign Immunity and the State Board of Claims, or (3) in the case of risks not covered by the Fund and Sovereign Immunity, commercial insurance, participation in insurance risk retention groups or self-insurance.

The 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 \$1.5 billion per occurrence. Buildings and contents are insured at replacement cost. As a state agency, the University is vested with Sovereign Immunity and is subject to the provisions of the Board of Claims Act, under which the University's liability for certain negligence claims is limited to \$200,000 for any one person or \$350,000 for all persons damaged by a single act of negligence. Claims against educators' errors and omissions and wrongful acts are insured through a reciprocal risk retention group. There have been no significant reductions in insurance coverage from 2019 to 2020. Settlements have not exceeded insurance coverage during the past five 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 of Kentucky. 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 three and a half percent. The malpractice liability at June 30, 2020, 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 liability 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 at June 30, 2020. All assets and liabilities related to medical malpractice are recorded in the financial records of the University and, accordingly, no assets or liabilities related to medical malpractice are recorded on the System's financial statements. However, the System does fund its required share of the actuarially determined medical malpractice expense.

The University is self-insured for the long-term disability income program and has established a 501(c)(9) trust for purposes of paying claims and establishing necessary reserves. The University currently plans to contribute to the trust based on an amount actuarially determined in accordance with the parameters of GASB Statement No. 75. As an organizational unit of the University, the System has recognized its share of the contribution in employee benefit costs and has no additional liability for this benefit at June 30, 2020.

The University also self-insures certain employee benefits, including health insurance, worker's compensation and unemployment claims. The University has recorded an estimate for asserted claims at June 30, 2020.

17. TRANSACTIONS WITH RELATED PARTIES

Due to the nature of the relationship of the System with the University, the System has substantial transactions with the University, including purchases of various supplies and services. Additionally, the University and its affiliates provide certain administrative support functions to the System. The System paid approximately \$19.9 million and \$16.3 million, respectively, in 2020 and 2019 to the University as reimbursement for various educational and support functions. The System also recognized income from the University for providing medical services to employees under a capitation health plan. During 2020 and 2019, the System received payments of approximately \$36.4 million and \$35.9 million, respectively, from the University for the capitation health plan. Noncapital transfers between the System and the University were \$159.5 million and \$134.0 million, respectively, for fiscal years 2020 and 2019. In addition, capital transfers from the University were \$1.5 million for fiscal year 2020 and \$8.2 million in transfers from the System to the University in fiscal year 2019.

18. FUNDS HELD IN TRUST BY OTHERS

The System is the residual principal and income beneficiary of an irrevocable trust that is held and controlled by external trustees. For the years ended June 30, 2020 and 2019, the System received income from this trust of approximately \$500 and \$400, respectively. The market value of the irrevocable external trust assets as of June 30, 2020 and 2019 was approximately \$66,000 and \$64,000, respectively.

19. CURRENT ECONOMIC UNCERTAINTIES

As a result of the spread of the SARS-COV-2 Virus and the incidence of COVID-19, economic uncertainties have arisen, which may negatively affect the financial position, results of operations, and cash flow of the System. The duration of these uncertainties and the ultimate financial effects cannot be reasonably estimated at this time.

20. COMBINED STATEMENTS

The System and its blended component unit's statements were summarized as follows for the years ended June 30, 2020 and 2019:

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED STATEMENT OF NET POSITION (in thousands)
AS OF JUNE 30, 2020

| | University of Kentucky Healthcare | Surgery Blue, LLC | Eliminations | Total |
|--|---|----------------------|-------------------|---------------------|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | | | |
| Current Assets | | | | |
| Cash and cash equivalents | \$ 790,957 | \$ 813 | \$ — | \$ 791,770 |
| Accounts receivable (less allowance for doubtful accounts) | 200,312 | 1,362 | — | 201,674 |
| Inventories and other assets | 50,110 | 60 | — | 50,170 |
| Estimated third-party payor settlements | 15,896 | — | — | 15,896 |
| Notes receivable | 2,607 | — | — | 2,607 |
| Total current assets | <u>1,059,882</u> | <u>2,235</u> | <u>—</u> | <u>1,062,117</u> |
| Noncurrent Assets | | | | |
| Restricted cash and cash equivalents | 90,138 | — | — | 90,138 |
| Long-term investments | 313,292 | — | (1,466) | 311,826 |
| Capital assets, net | 1,043,979 | 14,860 | — | 1,058,839 |
| Notes receivable | 3,067 | — | — | 3,067 |
| Other assets | 1,110 | 2,169 | — | 3,279 |
| Total noncurrent assets | <u>1,451,586</u> | <u>17,029</u> | <u>(1,466)</u> | <u>1,467,149</u> |
| Total assets | <u>2,511,468</u> | <u>19,264</u> | <u>(1,466)</u> | <u>2,529,266</u> |
| Deferred Outflows of Resources | 5,549 | — | — | 5,549 |
| Total assets and deferred outflows of resources | <u>2,517,017</u> | <u>19,264</u> | <u>(1,466)</u> | <u>2,534,815</u> |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | | |
| Current Liabilities | | | | |
| Accounts payable and accrued liabilities | 143,236 | 1,366 | — | 144,602 |
| Unearned revenue | 102,339 | — | — | 102,339 |
| Long-term debt - current portion | 22,553 | 733 | — | 23,286 |
| Capital lease obligations - current portion | 1,880 | 270 | — | 2,150 |
| Total current liabilities | <u>270,008</u> | <u>2,369</u> | <u>—</u> | <u>272,377</u> |
| Noncurrent Liabilities | | | | |
| Long-term liabilities - other | 26,487 | — | — | 26,487 |
| Long-term liabilities - debt | 496,745 | 7,676 | — | 504,421 |
| Capital lease obligations | 17,065 | 6,001 | — | 23,066 |
| Total noncurrent liabilities | <u>540,297</u> | <u>13,677</u> | <u>—</u> | <u>553,974</u> |
| Total liabilities | <u>810,305</u> | <u>16,046</u> | <u>—</u> | <u>826,351</u> |
| Deferred Inflows of Resources | 66 | — | — | 66 |
| Total liabilities and deferred inflows of resources | <u>810,371</u> | <u>16,046</u> | <u>—</u> | <u>826,417</u> |
| NET POSITION | | | | |
| Net investment in capital assets | 534,874 | 180 | — | 535,054 |
| Restricted | | | | |
| Nonexpendable other | 1,616 | — | — | 1,616 |
| Expendable | 11,748 | — | — | 11,748 |
| Total restricted | <u>13,364</u> | <u>—</u> | <u>—</u> | <u>13,364</u> |
| Unrestricted | 1,158,408 | 3,038 | (1,466) | 1,159,980 |
| Total net position | <u>\$ 1,706,646</u> | <u>\$ 3,218</u> | <u>\$ (1,466)</u> | <u>\$ 1,708,398</u> |

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED STATEMENT OF NET POSITION (in thousands)
AS OF JUNE 30, 2019

| | University of Kentucky Healthcare | Surgery Blue, LLC | Eliminations | Total |
|--|---|----------------------|-------------------|---------------------|
| ASSETS AND DEFERRED OUTFLOWS OF RESOURCES | | | | |
| Current Assets | | | | |
| Cash and cash equivalents | \$ 398,913 | \$ 131 | \$ — | \$ 399,044 |
| Accounts receivable (less allowance for doubtful accounts) | 231,449 | 646 | — | 232,095 |
| Inventories and other assets | 43,156 | 48 | — | 43,204 |
| Estimated third-party payor settlements | 8,104 | — | — | 8,104 |
| Notes receivable | 2,671 | — | — | 2,671 |
| Total current assets | <u>684,293</u> | <u>825</u> | <u>—</u> | <u>685,118</u> |
| Noncurrent Assets | | | | |
| Restricted cash and cash equivalents | 181,739 | — | — | 181,739 |
| Long-term investments | 316,217 | — | (1,248) | 314,969 |
| Capital assets, net | 1,013,400 | 884 | — | 1,014,284 |
| Notes receivable | 2,963 | — | — | 2,963 |
| Other assets | 1,012 | 2,183 | — | 3,195 |
| Total noncurrent assets | <u>1,515,331</u> | <u>3,067</u> | <u>(1,248)</u> | <u>1,517,150</u> |
| Total assets | <u>2,199,624</u> | <u>3,892</u> | <u>(1,248)</u> | <u>2,202,268</u> |
| Deferred Outflows of Resources | 6,806 | — | — | 6,806 |
| Total assets and deferred outflows of resources | <u>2,206,430</u> | <u>3,892</u> | <u>(1,248)</u> | <u>2,209,074</u> |
| LIABILITIES AND DEFERRED INFLOWS OF RESOURCES | | | | |
| Current Liabilities | | | | |
| Accounts payable and accrued liabilities | 124,598 | 841 | — | 125,439 |
| Unearned revenue | 63,966 | — | — | 63,966 |
| Long-term debt - current portion | 19,404 | — | — | 19,404 |
| Capital lease obligations - current portion | 4,034 | 100 | — | 4,134 |
| Total current liabilities | <u>212,002</u> | <u>941</u> | <u>—</u> | <u>212,943</u> |
| Noncurrent Liabilities | | | | |
| Long-term liabilities - other | 26,307 | 11 | — | 26,318 |
| Long-term liabilities - debt | 519,281 | — | — | 519,281 |
| Capital lease obligations | 18,945 | 149 | — | 19,094 |
| Total noncurrent liabilities | <u>564,533</u> | <u>160</u> | <u>—</u> | <u>564,693</u> |
| Total liabilities | <u>776,535</u> | <u>1,101</u> | <u>—</u> | <u>777,636</u> |
| Deferred Inflows of Resources | 64 | — | — | 64 |
| Total liabilities and deferred inflows of resources | <u>776,599</u> | <u>1,101</u> | <u>—</u> | <u>777,700</u> |
| NET POSITION | | | | |
| Net investment in capital assets | 509,047 | 735 | — | 509,782 |
| Restricted | | | | |
| Nonexpendable other | 1,590 | — | — | 1,590 |
| Expendable | 14,667 | — | — | 14,667 |
| Total restricted | <u>16,257</u> | <u>—</u> | <u>—</u> | <u>16,257</u> |
| Unrestricted | 904,527 | 2,056 | (1,248) | 905,335 |
| Total net position | <u>\$ 1,429,831</u> | <u>\$ 2,791</u> | <u>\$ (1,248)</u> | <u>\$ 1,431,374</u> |

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION (in thousands)
FOR THE YEAR ENDED JUNE 30, 2020

| | University of Kentucky Healthcare | Surgery Blue, LLC | Eliminations | Total |
|---|---|----------------------|-------------------|---------------------|
| OPERATING REVENUES | | | | |
| Net patient service revenues, less provision for doubtful accounts | \$ 1,996,086 | \$ 12,297 | \$ — | \$ 2,008,383 |
| Sales and services | 98,633 | 46 | — | 98,679 |
| Management contract revenue | 41,930 | — | — | 41,930 |
| Total operating revenues | <u>2,136,649</u> | <u>12,343</u> | <u>—</u> | <u>2,148,992</u> |
| OPERATING EXPENSES | | | | |
| Salaries and wages | 571,685 | 3,081 | — | 574,766 |
| Fringe benefits | 155,834 | 576 | — | 156,410 |
| Supplies | 514,711 | 4,840 | — | 519,551 |
| Purchased services | 127,205 | 250 | — | 127,455 |
| Other expenses | 220,556 | 1,849 | — | 222,405 |
| Depreciation | 68,336 | 689 | — | 69,025 |
| Management contract expenses | 38,970 | — | — | 38,970 |
| Total operating expenses | <u>1,697,297</u> | <u>11,285</u> | <u>—</u> | <u>1,708,582</u> |
| Net income from continuing operations | <u>439,352</u> | <u>1,058</u> | <u>—</u> | <u>440,410</u> |
| NONOPERATING REVENUES (EXPENSES) | | | | |
| Additions to permanent endowments | 26 | — | — | 26 |
| Gifts and non-exchange grants | 4,666 | — | — | 4,666 |
| Capital gifts | 104 | — | — | 104 |
| Investment income | 10,846 | 10 | (218) | 10,638 |
| Interest expense | (17,869) | (354) | — | (18,223) |
| Loss on disposal of capital assets | (1,523) | 13 | — | (1,510) |
| Other | (869) | (300) | — | (1,169) |
| Gain on sale of investment | — | — | — | — |
| Net nonoperating revenues (expenses) | <u>(4,619)</u> | <u>(631)</u> | <u>(218)</u> | <u>(5,468)</u> |
| Net income (loss) before other revenues, expenses, gains, or losses | <u>434,733</u> | <u>427</u> | <u>(218)</u> | <u>434,942</u> |
| Transfers to the University of Kentucky for noncapital purposes | (159,464) | — | — | (159,464) |
| Transfers from the University of Kentucky for capital purposes | 1,546 | — | — | 1,546 |
| Total other expenses | <u>(157,918)</u> | <u>—</u> | <u>—</u> | <u>(157,918)</u> |
| INCREASE (DECREASE) IN NET POSITION | <u>276,815</u> | <u>427</u> | <u>(218)</u> | <u>277,024</u> |
| NET POSITION, beginning of year | <u>1,429,831</u> | <u>2,791</u> | <u>(1,248)</u> | <u>1,431,374</u> |
| NET POSITION, end of year | <u>\$ 1,706,646</u> | <u>\$ 3,218</u> | <u>\$ (1,466)</u> | <u>\$ 1,708,398</u> |

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION (in thousands)
FOR THE YEAR ENDED JUNE 30, 2019

| | University of Kentucky Healthcare | Surgery Blue, LLC | Eliminations | Total |
|--|---|----------------------|-------------------|---------------------|
| OPERATING REVENUES | | | | |
| Net patient service revenues, less provision for doubtful accounts | \$ 1,644,912 | \$ 2,764 | \$ — | \$ 1,647,676 |
| Sales and services | 69,743 | 17 | — | 69,760 |
| Management contract revenue | 41,177 | — | — | 41,177 |
| Total operating revenues | <u>1,755,832</u> | <u>2,781</u> | <u>—</u> | <u>1,758,613</u> |
| OPERATING EXPENSES | | | | |
| Salaries and wages | 531,958 | 794 | — | 532,752 |
| Fringe benefits | 146,764 | 130 | — | 146,894 |
| Supplies | 429,988 | 1,123 | — | 431,111 |
| Purchased services | 95,955 | 79 | — | 96,034 |
| Other expenses | 195,086 | 500 | — | 195,586 |
| Depreciation | 66,892 | 67 | — | 66,959 |
| Management contract expenses | 38,032 | — | — | 38,032 |
| Total operating expenses | <u>1,504,675</u> | <u>2,693</u> | <u>—</u> | <u>1,507,368</u> |
| Net income from continuing operations | <u>251,157</u> | <u>88</u> | <u>—</u> | <u>251,245</u> |
| NONOPERATING REVENUES (EXPENSES) | | | | |
| Additions to permanent endowments | 335 | — | — | 335 |
| Gifts and non-exchange grants | 4,336 | — | — | 4,336 |
| Capital gifts | 59 | — | — | 59 |
| Investment income | 28,367 | 6 | (1,248) | 27,125 |
| Interest expense | (23,535) | — | — | (23,535) |
| Loss on disposal of capital assets | (861) | — | — | (861) |
| Other | 2,882 | 2,697 | — | 5,579 |
| Net nonoperating revenues (expenses) | <u>11,583</u> | <u>2,703</u> | <u>(1,248)</u> | <u>13,038</u> |
| Net income before other revenues, expenses, gains, or losses | <u>262,740</u> | <u>2,791</u> | <u>(1,248)</u> | <u>264,283</u> |
| Transfers to the University of Kentucky for noncapital purposes | (133,993) | — | — | (133,993) |
| Transfers to the University of Kentucky for capital purposes | (8,224) | — | — | (8,224) |
| Total other expenses | <u>(142,217)</u> | <u>—</u> | <u>—</u> | <u>(142,217)</u> |
| INCREASE (DECREASE) IN NET POSITION | <u>120,523</u> | <u>2,791</u> | <u>(1,248)</u> | <u>122,066</u> |
| NET POSITION, beginning of year | <u>1,309,308</u> | <u>—</u> | <u>—</u> | <u>1,309,308</u> |
| NET POSITION, end of year | <u>\$ 1,429,831</u> | <u>\$ 2,791</u> | <u>\$ (1,248)</u> | <u>\$ 1,431,374</u> |

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED STATEMENT OF CASH FLOWS (in thousands)
FOR THE YEAR ENDED JUNE 30, 2020

| | University of Kentucky Healthcare | Surgery Blue, LLC | Eliminations | Total |
|--|---|----------------------|--------------|-------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | | | |
| Net patient service revenues | \$ 2,021,816 | \$ 11,581 | \$ — | \$ 2,033,397 |
| Sales and services | 98,632 | 47 | — | 98,679 |
| Management contract services | 39,519 | — | — | 39,519 |
| Payments to vendors and contractors | (863,918) | (6,554) | 218 | (870,254) |
| Salaries, wages and fringe benefits | (709,583) | (3,527) | — | (713,110) |
| Payments on management contract services | (34,143) | — | — | (34,143) |
| Other payments | (741) | — | — | (741) |
| Net cash provided by operating activities | <u>551,582</u> | <u>1,547</u> | <u>218</u> | <u>553,347</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | | | |
| Provider relief fund | 30,261 | — | — | 30,261 |
| Gifts | 4,817 | — | — | 4,817 |
| Additions to permanent endowments | 26 | — | — | 26 |
| Payments on loans from University of Kentucky departmental units | 426 | — | — | 426 |
| Transfers to the University of Kentucky for noncapital purposes | (159,464) | (300) | — | (159,764) |
| Net cash used by noncapital financing activities | <u>(123,934)</u> | <u>(300)</u> | <u>—</u> | <u>(124,234)</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | | | |
| Purchases of capital assets | (94,540) | (8,402) | — | (102,942) |
| Principal payments-capital leases and long-term obligations | (23,421) | (252) | — | (23,673) |
| Interest payments-capital leases and long-term obligations | (19,666) | (354) | — | (20,020) |
| Proceeds from long-term obligations | — | 8,415 | — | 8,415 |
| Other capital and related financing payments | (5,119) | 18 | — | (5,101) |
| Transfers from the University of Kentucky for capital purposes | 1,546 | — | — | 1,546 |
| Net cash used by capital and related financing activities | <u>(141,200)</u> | <u>(575)</u> | <u>—</u> | <u>(141,775)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | |
| Proceeds from sales and maturities of investments | 167,995 | — | — | 167,995 |
| Interest and dividends on investments | 14,198 | 10 | (218) | 13,990 |
| Purchase of investments | (168,198) | — | — | (168,198) |
| Net cash provided (used) by investing activities | <u>13,995</u> | <u>10</u> | <u>(218)</u> | <u>13,787</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | <u>300,443</u> | <u>682</u> | <u>—</u> | <u>301,125</u> |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>580,652</u> | <u>131</u> | <u>—</u> | <u>580,783</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 881,095</u> | <u>\$ 813</u> | <u>\$ —</u> | <u>\$ 881,908</u> |

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED STATEMENT OF CASH FLOWS (in thousands)
FOR THE YEAR ENDED JUNE 30, 2019

| | University of Kentucky Healthcare | Surgery Blue, LLC | Eliminations | Total |
|---|---|----------------------|----------------|-------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | | | |
| Net patient service revenues | \$ 1,608,311 | \$ 2,730 | \$ — | \$ 1,611,041 |
| Sales and services | 69,743 | 17 | — | 69,760 |
| Management contract services | 40,644 | — | — | 40,644 |
| Payments to vendors and contractors | (719,644) | (1,532) | — | (721,176) |
| Salaries, wages and fringe benefits | (675,087) | (874) | 1,248 | (674,713) |
| Payments on management contract services | (38,318) | 24 | — | (38,294) |
| Other receipts (payments) | (96) | — | — | (96) |
| Net cash provided by operating activities | <u>285,553</u> | <u>365</u> | <u>1,248</u> | <u>287,166</u> |
| CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES | | | | |
| Gifts | 4,247 | — | — | 4,247 |
| Additions to permanent endowments | 335 | — | — | 335 |
| Payments on loan to University of noncapital purposes | 391 | — | — | 391 |
| Transfers to the University of Kentucky for noncapital purposes | (133,993) | 83 | — | (133,910) |
| Net cash used by noncapital financing activities | <u>(129,020)</u> | <u>83</u> | <u>—</u> | <u>(128,937)</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES | | | | |
| Purchases of capital assets | (69,559) | (282) | — | (69,841) |
| Principal payments-capital leases and long-term obligations | (22,844) | (40) | — | (22,884) |
| Interest payments-capital leases and long-term obligations | (25,145) | — | — | (25,145) |
| Other capital and related financing payments | (836) | — | — | (836) |
| Transfers to the University of Kentucky for capital purposes | 802 | — | — | 802 |
| Net cash used by capital and related financing activities | <u>(117,582)</u> | <u>(322)</u> | <u>—</u> | <u>(117,904)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | |
| Proceeds from sales and maturities of investments | 154,947 | — | — | 154,947 |
| Interest and dividends on investments | 12,291 | 5 | (48) | 12,248 |
| Purchase of investments | (151,471) | — | (1,200) | (152,671) |
| Net cash provided by investing activities | <u>15,767</u> | <u>5</u> | <u>(1,248)</u> | <u>14,524</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | <u>54,718</u> | <u>131</u> | <u>—</u> | <u>54,849</u> |
| CASH AND CASH EQUIVALENTS, beginning of year | <u>525,934</u> | <u>—</u> | <u>—</u> | <u>525,934</u> |
| CASH AND CASH EQUIVALENTS, end of year | <u>\$ 580,652</u> | <u>\$ 131</u> | <u>\$ —</u> | <u>\$ 580,783</u> |



UNIVERSITY FINANCIAL SERVICES
301 Peterson Service Building • Lexington, KY 40506-0005
www.uky.edu/ufs/financial-statements-and-investor-information

