UK HealthCare Hospital System

UNIVERSITY OF KENTUCKY • 2023 FINANCIAL STATEMENTS

UK HealthCare Hospital System
An Organizational Unit of the University of Kentucky
Financial Statements
Year Ended June 30, 2023

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FORV/S

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Independent Auditor's Report

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

Opinion

We have audited the financial statements of the business-type activities and the fiduciary activities of UK HealthCare Hospital System (System), an organizational unit of the University of Kentucky (University), as of and for the year ended June 30, 2023, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the financial position of the of the business-type activities and the fiduciary activities of the System as of June 30, 2023, and the changes in financial position and, where applicable, cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

We did not audit the financial statements of Insure Blue, which is a blended component unit of the System, constituting 0.685%, 0.003% and 0.001%, respectively, of the assets, net position, and revenues of the System, as of and for the year ended June 30, 2023. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for Insure Blue, are based solely on the report of the other auditor.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the "Auditor's Responsibilities for the Audit of the Financial Statements" section of our report. We are required to be independent of the System and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis of Matters

As discussed in Note 1, the financial statements of the System are intended to present the financial position, 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, 2023, the changes in its financial position or its cash flows for the year 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.

As discussed in Note 21 to the financial statements, in 2023, the University entered into a membership substitution agreement to acquire Royal Blue Health LLC, which resulted in a government combination. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the System's ability to continue as a going concern for 12 months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.

- Obtain an understanding of internal control relevant to the audit 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 System's internal control. Accordingly, no such opinion is expressed.

- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.

- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the System's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and pension benefit information be presented to supplement the basic financial statements. Such information is the responsibility of management and, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our 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.

FORVIS, LLP

Louisville, Kentucky
October 6, 2023

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2023

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 year ended June 30, 2023. 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; Surgery Blue LLC, a wholly owned for-profit subsidiary, its for-profit subsidiary, Surgery Center of Lexington, LLC (51% ownership); and Beyond Blue Corporation (BBC), a wholly owned non-profit subsidiary, and its non-profit subsidiary Royal Blue Health, LLC (RBH or King's Daughters health system), and Insure Blue (IB), formerly Integrated Health Insurance, Ltd. (collectively, the System or UK HealthCare). 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 Hospital System

UK HealthCare, the University of Kentucky's (the University) advanced academic medical center and clinical care network, is uniquely equipped to provide advanced subspecialty care to the people of Kentucky. The academic medical center and health system provides patient care on par – in terms of both volume and complexity – with the nation's top 25% of academic medical centers. In August 2023, UK HealthCare was listed number one in Kentucky in the latest U.S. News and World Report's Best Hospital's ranking for the eighth 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 in Lexington, Kentucky, 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 1,086 licensed beds with an average daily census of 886 patients. On a monthly basis, the system provides on average 1,226 inpatient surgeries, 1,964 outpatient surgeries, 41,129 radiology procedures, 10,285 emergency department visits, and 108,367 ambulatory clinic visits. In fiscal year 2023, UK HealthCare was given a 3-star rating by the Centers for Medicare and Medicaid Services.

On December 1, 2022, Royal Blue Health, LLC became part of the UK HealthCare. RBH is the King's Daughters health system based in Ashland, Kentucky. RBH and UK HealthCare worked together as members of a joint venture for approximately two years before the acquisition. RBH is the largest employer of northeastern Kentucky, is comprised of two hospitals and 78 clinics with over 5,000 employees, and serves regions of Kentucky, Ohio, and West Virginia. In fiscal year 2023, the King's Daughters health system had 465 licensed beds with an average daily census of 223 patients. On a monthly basis, King's Daughters health system provides on average 1,161 inpatient surgeries, 3,571 outpatient surgeries, 10,138 radiology procedures, and 5,970 emergency department 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 medical centers in the United States that have an 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 $5.26 billion, deferred outflows of resources of $16.0 million, liabilities of $1.28 billion, and deferred inflows of resources of $1.0 million. Net position, which represents the System’s residual interest in assets after liabilities are deducted, was $3.99 billion or 76.0% of total assets. For the fiscal year ended June 30, 2023, the System reported net income before other revenues, expenses, gains and losses of $771.8 million, generating a margin of 20.4%.

Financial results for fiscal year 2023 exceeded prior year's revenues with net outpatient revenues, including the provision for doubtful accounts, increasing approximately $864.1 million or 69.9% over the prior fiscal year and net inpatient revenues, including the provision for doubtful accounts, which increased $159.1 million or 11.3% over the previous fiscal year. The primary driver was the acquisition of RBH at $581.5 million. Medicaid Directed Payments revenue was $814.6 million for fiscal year 2023, which was an increase from prior year by $259.8 million.

- On December 1, 2022, the System’s non-profit subsidiary Beyond Blue Corporation acquired RBH through member substitution. The entity is reported as part of BBC and the impact as of the date of acquisition resulted in an increase in assets of $1.08 billion, deferred outflows of resources of $1.0 million, liabilities of $387.2 million, deferred inflows of resources of $1.1 million and net position of $695.5 million. Consequently, on January 1, 2023 BBC acquired Insure Blue (IB), formerly Integrated Health Insurance, Ltd. That provides health care, physician professional and comprehensive general liability coverage and excess coverage to the King’s Daughters health system.
- Total assets increased $1.84 billion or 53.7%. This is due to increases in cash and cash equivalents of $491.9 million, long-term investments of $422.7 million, capital assets, net, of $416.2 million, estimated third-party payer settlements of $292.4 million, accounts receivable, net, of $112.8 million, leases, net of $32.4 million, inventories and other assets of $31.7 million, subscription assets, net, of $29.6 million, and other noncurrent assets of $6.9 million. These increases were offset by a decrease in notes receivable of $457 thousand.
- Deferred outflows of resources increased $12.6 million, out of which $13.5 million is RBH's reported deferred outflow of resources related to its Single Employer Defined Benefit Pension Plan. The remaining represents the unamortized difference between the reacquisition price and the net carrying amount of the refunded debt.
- Total liabilities increased $454.0 million or 55.1% as a result of increases in long-term debt of $204.4 million, accounts payable and accrued expenses of $102.2 million, subscription liabilities of $26.2 million, lease liabilities of $37.1 million, other long-term liabilities of $42.7 million, unearned revenue of $15.8 million, estimated third-party payer settlements of $15.7 million, and net pension liabilities of $9.9 million.
- Deferred inflows of resources increased $937 thousand, out of which $930 thousand is related to RBH and represents payments to be received under lease agreements. The remaining represents the beneficial interest from an irrevocable external trust that the system will receive in future years.
- Total net position increased $1.39 billion or 53.7% primarily due to the acquisition of Royal Blue Health and Insure Blue and net income from current year operations.

- Operating revenues increased $953.0 million or 33.7% primarily due to an increase in net patient revenue of $923.8 million, of this amount $633.6 million is from the King's Daughters health system's operations.
- Operating expenses increased $739.4 million or 31.8%. The largest increases came from personnel costs of $317.1 million, supplies of $238.0 million, purchased services of $80.8 million, other expenses of $52.7 million. Out of the total increase, $519.7 million was due to the additions of RBH and Insure Blue.
- The net nonoperating revenues and expenses increase of $110.5 million is primarily due to the gains on investments going from a loss last year to a gain this year, resulting in an increase of $117.0 million, and a $21.7 million decrease in other nonoperating expenses, and a $1.1 million increase in gifts and non-exchange grants. This increase is offset by a $21.7 million decrease in COVID-19 funding, an interest expense increase of $6.0 million, and a decrease of $1.3 million in capital gifts.
- Total other revenue increased by $673.2 million primarily due to the acquisition of RBH and Insure Blue of $695.6 million. This was offset by increases in transfers to the University of Kentucky for capital purposes of $14.4 million and noncapital purposes of $8.0 million.

Operating Statistics

The following table presents utilization statistics for Chandler and Good Samaritan Hospitals for fiscal years ended 2023 and 2022:

Discharges:	2023	2022
Medicare	14,786	14,149
Medicaid	15,008	13,456
Commercial/Blue Cross	11,742	10,079
Patient/Charity	766	684
Total discharges	42,302	38,368
Average daily census	886	832
Average length of stay	7.65	7.92
Emergency visits	123,415	110,524

Total discharges increased by 3,934 or 10.3% compared to the prior fiscal year. The increase occurred due to increases in Commercial/Blue Cross of 1,663, Medicaid of 1,552, Medicare of 637, and Patient/Charity of 82. Overall, the Diagnosis-Related Group case mix index increased to 2.2558 from 2.2496 and the average length of stay decreased by 0.27 days to 7.65 days. The case mix for Chandler was at 2.4068 while Good Samaritan was at 1.5455. Emergency visits increased by 12,891 or 11.7% over the prior year.

The following table presents utilization statistics for RBH for fiscal year ended June 30, 2023:

	2023
Admissions	14,292
Average daily census	223
Emergency visits	53,733

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, Statement of Revenues, Expenses and Changes in Net Position, Statement of Cash Flows and Notes to the Financial Statements. GASB requires that statements be presented on a System-wide basis.

The System implemented GASB Statement No 96, *Subscription-Based Information Technology Arrangements* in fiscal year 2023. The financial data in the MD&A for fiscal year 2022 was not restated for this implementation.

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, 2023. 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, 2023 and 2022 are as follows:

Condensed Statements of Net Position (in thousands)

	2023	2022
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES		
Current assets	$ 2,675,458	$ 1,765,310
Capital, lease, and subscription assets, net	1,675,071	1,196,813
Other noncurrent assets	906,197	457,412
Deferred outflows of resources	15,973	3,373
Total assets and deferred outflows of resources	5,272,699	3,422,908
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES		
Current liabilities	433,255	273,139
Noncurrent liabilities	844,562	550,668
Deferred inflows of resources	1,005	68
Total liabilities and deferred inflows of resources	1,278,822	823,875
NET POSITION		
Net investment in capital assets	805,636	597,024
Nonexpendable other	2,322	1,862
Restricted expendable	12,700	6,044
Unrestricted	3,173,219	1,994,103
Total net position	$ 3,993,877	$ 2,599,033

Assets. As of June 30, 2023, the System's total assets amounted to approximately $5.26 billion. Cash and cash equivalents of $1.65 billion or 31.3% of total assets represented the System's largest asset. Capital assets, net of depreciation, of $1.55 billion or 29.4% of total assets is the second largest asset, and long-term investments of $802.8 million or 15.3% was the System's third largest asset. Accounts receivable, net, primarily patient-related, of $541.6 million or 10.3% of total assets represents another significant asset of the System.

Total assets increased by $1.84 billion during the year ended June 30, 2023. The increase was primarily due to the acquisition of Royal Blue Health and Insure Blue and the growth within UK HealthCare Chandler and Good Samaritan Hospitals. Cash and cash equivalents increased $491.9 million, long-term investments increased $422.7 million, capital assets, net, increased $416.2 million, estimated third-party payer settlements increased $292.4 million, accounts receivable, net, increased $112.8 million, leases, net increased $32.4 million, inventories and other assets of $31.7 million, subscription assets, net, increased $29.6 million, and other noncurrent assets increased $6.9 million. These increases were offset by a decrease in notes receivable of $457 thousand.

Deferred Outflows of Resources. Deferred outflows of resources totaled $16.0 million, an increase of $12.6 million, out of which $13.5 million is RBH's reported deferred outflow of resources related to its Single Employer Defined Benefit Pension Plan. The remaining 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 fiscal year 2015.

Liabilities. As of June 30, 2023, the System's liabilities totaled $1.28 billion. Long-term debt (current and non-current), which consists of general receipts notes and note payable to the University, comprised the largest liability of $706.3 million or 55.3% of total liabilities. Accounts payable and accrued liabilities totaled

$293.4 million or 23.0% of liabilities. Lease liabilities totaled $102.5 million or 8.0% of liabilities. Long-term liabilities, other accounted for $70.6 million or 5.5% of liabilities and consisted primarily of capital accounts payable and unamortized bond premium. Unearned revenue represented approximately $53.2 million or 4.2% of liabilities. Subscription liabilities of $26.2 million or 2.0% of liabilities, unearned revenue of $15.7 million or 1.2% of liabilities, and net pension liabilities of $9.9 million or 0.8% of liabilities made up the remaining balance.

Total liabilities increased $454.0 million or 55.1%, the main reason is the acquisition of Royal Blue Health and Insure Blue and resulted in increases in long-term debt of $204.4 million. In addition, there are increases in lease liabilities of $37.1 million, accounts payable and accrued expenses of $102.2 million, other long-term liabilities of $42.7 million, subscription liabilities of $26.2 million, unearned revenue of $15.8 million, unearned revenue of $15.7 million, and net pension liabilities of $9.9 million.

Deferred Inflows of Resources. Deferred inflows of resources totaled $1.0 million, of which $930 thousand is related to RBH and represents payments to be received under lease agreements. For the remaining, the System is the residual principal and income beneficiary of an irrevocable trust that is held and controlled by external trustees. For the year ended June 30, 2023, the System did not receive income from this trust.

Net Position. Net position as of June 30, 2023 totaled approximately $3.99 billion, or 76.0% of total assets. Net investment in capital assets totaled $805.6 million or 20.2% of total net position. Restricted net position totaled $15.0 million or 0.4% of total net position. Unrestricted net position accounted for $3.17 billion or 79.5% of total net position. Total net position increased $1.39 billion or 53.7%, out of which $695.6 million is due to the acquisition of RBH and Insure Blue, and the net income from current year operations.

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.

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, 2023. 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 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)

	2023	2022
OPERATING REVENUES		
Net patient service revenues	$ 3,564,984	$ 2,641,160
Sales and services	153,889	138,437
Grant revenue	1,843	—
Management contract revenue	61,648	49,725
Total operating revenues	3,782,364	2,829,322
OPERATING EXPENSES		
Salaries and benefits	1,294,723	977,624
Supplies and purchased services	1,280,422	961,650
Other expenses	293,399	240,654
Depreciation and amortization	140,649	100,411
Management contract expenses	57,271	46,738
Total operating expenses	3,066,464	2,327,077
NET INCOME FROM CONTINUING OPERATIONS	715,900	502,245
NONOPERATING REVENUES (EXPENSES)		
American Rescue Plan	—	21,736
Additions to permanent endowments	460	195
Grants and gifts	6,098	6,366
Investment income (loss)	93,617	(23,421)
Interest on capital asset-related debt	(26,507)	(20,479)
Transfers to the University of Kentucky	(72,572)	(50,188)
Other, net	(17,734)	(38,952)
Special item - acquisition of Royal Blue Health and Insure Blue	695,582	—
Total nonoperating revenues (expenses)	678,944	(104,743)
INCREASE IN NET POSITION	1,394,844	397,502
NET POSITION, beginning of year	2,599,033	2,201,531
NET POSITION, end of year	$ 3,993,877	$ 2,599,033

Operating Revenues

Total operating revenues were approximately $3.78 billion for the year ended June 30, 2023, an increase of $953.0 million or 33.7% over fiscal year 2022. The most significant source of operating revenue for the System was net patient service revenues of $3.56 billion, an increase of $923.8 million or 35.0% in fiscal year 2023 over 2022, out of which $581.5 million was from the operations of RBH.

Inpatient net revenue, including bad debt, increased $159.1 million or 11.3% over prior year. The primary driver of the increase was the acquisition of RBH of $146.1 million, which included directed payments of $40.2 million.

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.

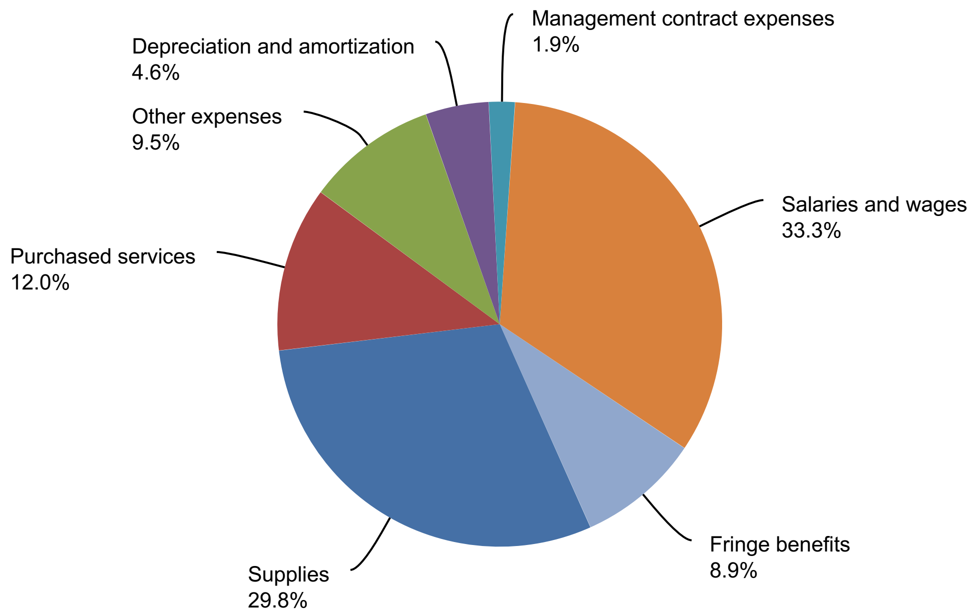
Outpatient net revenue, including bad debt, increased by $864.1 million or 69.9% over prior year. The primary driver was the acquisition of RBH of $518.0 million including $123.6 million in directed payments. Chandler and Good Samaritan contributed $344.3 million to the increase. Surgery Blue had a net patient revenue increase over last year of $1.9 million.

RBH reported grant revenue of $1.8 million.

The System was able to recognize $814.6 million of Directed Payments revenue during the current fiscal year.

Bad debt provision increased by $50.1 million or 68.4% versus the prior year driven by the acquisition of RBH and a 14% increase in gross charges at Chandler and Good Samaritan Hospitals and an increase self-pay gross charges by 17%.

TOTAL OPERATING EXPENSES



Operating Expenses

Total operating expenses, including $140.6 million of depreciation and amortization, were $3.07 billion, an increase of $739.4 million or 31.8% over the prior year.

Salaries and wages increased $247.1 million over the prior fiscal year. The main driver was the acquisition of RBH with its salaries and wages of $232.6 million. The increase in salaries and wages at Chandler and Good Samaritan was driven by an increase of 36 full-time equivalents related to patient services demand. Fringe benefits increased $70.0 million or 34.3% primarily due to the acquisition of RBH of $64.5 million.

Supplies expenses increased $238.0 million or 35.2% primarily due to increases in drugs, antibiotics, variable and hospital supplies driven by the increased utilization and acquisition of RBH. Purchased services increased $80.8 million or 28.3% primarily due to the increase in contract labor expenses, professional, contracts, and other commercial services. Other expenses increased $52.7 million or 21.9% primarily due to increase in repair and maintenance, malpractice expense, equipment service contracts, and security services.

Nonoperating Revenues (Expenses)

Total net nonoperating revenues were $55.9 million in fiscal year 2023 compared to $54.6 million in total nonoperating expenses during the prior fiscal year, an increase of $110.5 million. This is due to the increase in investment income of $117.0 million, a decrease in other nonoperating expenses of $21.7 million, and an increase of $1.1 million in gifts and non-exchange grants. These were offset by a decrease in COVID-19 federal funding of $21.7 million, an increase in interest expense on capital related debt of $6.0 million, and a decrease in capital gifts of $1.3 million.

Total other revenues for fiscal year 2023 were $623.0 million compared to $50.2 million in expenses for fiscal year 2022, which was an increase of $673.2 million. The primary driver was the acquisition of Royal Blue Health and Insure Blue in the amount of $695.6 million. Transfers to the University of Kentucky for capital purposes increased $14.4 million and noncapital purposes increased $8.0 million.

Statement of Cash Flows

The Statement of Cash Flows details how cash has increased or decreased during the year ended June 30, 2023, with comparative financial information for the year ended June 30, 2022. 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)

	2023	2022
CASH PROVIDED (USED) BY:		
Operating activities	$ 682,347	$ 327,585
Noncapital financing activities	(52,490)	(58,469)
Capital and related financing activities	(258,556)	(149,306)
Investing activities	120,630	7,017
Net increase in cash and cash equivalents	491,931	126,827
CASH AND CASH EQUIVALENTS, beginning of year	1,154,052	1,027,225
CASH AND CASH EQUIVALENTS, end of year	$ 1,645,983	$ 1,154,052

The major sources of cash included in operating activities were net patient service revenues of $3.37 billion, sales and services of $147.2 million, and management contract services of $52.2 million. Cash payments for operating activities were $1.56 billion to vendors, $1.27 billion to employees for salaries, wages and fringe benefits, and $56.9 million for management contract services.

Cash used by noncapital financing consists of transfers to the University of Kentucky for noncapital purposes of $56.9 million, and other financing payments of $2.7 million. This was offset by an inflow of cash from gifts of $6.1 million, payments on loans from University departmental units of $475 thousand, and additions to permanent endowments of $460 thousand.

Cash used by capital and related financing activities included purchases of capital assets of $131.6 million, principal and interest payments on long-term obligations of $58.6 million, other capital and related financing payments of $17.1 million, principal and interest payments on lease obligations of $26.0 million, principal and interest payments on subscription obligations of $11.6 million, and transfers to the University for capital purposes of $14.5 million.

Investing activities included proceeds from sales and maturities of investments of $247.7 million, interest and dividends of $55.0 million, and cash acquired with the acquisition of King's Daughters Health System and Insure Blue of $45.0 million. Cash of $227.0 million was used to purchase investments.

Key Ratios

The following table shows key liquidity and capital ratios for fiscal years 2023 and 2022 for Chandler and Good Samaritan Hospitals:

	2023	2022
Days cash on hand	191	188
Days of revenue in accounts receivable	55	59
Debt service coverage (times)	27.9	11.2

Days cash on hand increased to 191 days in fiscal year 2023 from 188 days in fiscal year 2022. 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 $405.4 million.

The days of revenue in accounts receivable measures the average number of days it takes to collect accounts receivable. In fiscal year 2023, days in accounts receivable were 55 compared to 59 days in fiscal year 2022. Net patient service revenues, less provision for doubtful accounts, increased by $923.8 million from fiscal year 2022 to fiscal year 2023, which contributed to the decrease in days 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 2023 is 27.9 versus 11.2 in fiscal year 2022 due to the increase in change in net position in fiscal year 2023 compared to fiscal year 2022.

Capital, Lease and Subscription Assets and Debt Administration

Capital Assets. Capital assets, net of accumulated depreciation, totaled approximately $1.55 billion at June 30, 2023, a net increase of $416.2 million over the prior year. Significant changes in capital assets during fiscal year 2023 included (in millions):

Land, buildings and structures, net additions	$ 334.7
Equipment and vehicles, net additions	107.3
Capitalized software deletions	1.5
Artwork	0.1
Construction in process, net deletions	63.4
Increase in accumulated depreciation, net	(90.8)
Total	$ 416.2

Lease Assets. Lease assets, net of accumulated amortization, totaled approximately $100.0 million at June 30, 2023, a net increase of $32.4 million over June 30, 2022. Significant changes in lease assets during fiscal year 2023 included (in millions):

Lease land, buildings and structures, net additions	$ 43.7
Lease equipment, net additions	16.7
Increase in lease accumulated amortization, net	(28.0)
Total	$ 32.4

Subscription Assets. Subscription assets, net of accumulated amortization, totaled approximately $29.6 million at June 30, 2023, a net increase of $16.5 million over July 1, 2022. Significant changes in subscription assets during fiscal year 2023 included (in millions):

Subscription assets, net additions	$ 24.2
Increase in subscription assets accumulated amortization, net	(7.7)
Total	$ 16.5

GASB Statement No. 96 was adopted during fiscal year 2023 resulting in recognition of subscription assets of $13.1 million for subscription contracts as of July 1, 2022.

Debt. As of June 30, 2023, the System's outstanding debt was $706.3 million. Of this total, $448.4 million was in general receipts project notes outstanding with $22.4 million included in current liabilities and the remainder in long-term liabilities, and $230.3 million was in RBH revenue bonds with $8.4 million included in current liabilities and the remainder in long-term liabilities. On February 28, 2019, approximately $8.4 million of the Surgery Blue promissory note was issued at a variable interest rate between 3.2% and 4.5%. The note was issued for the purpose of funding construction and development of 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. As of June 30, 2023, the promissory note was $6.9 million. As of June 30, 2023, King's Daughters Health System had notes payable of $1.8 million. Capital financed obligations were $18.8 million as of June 30, 2023.

As of June 30, 2023, the System had lease and subscription liabilities of $102.5 million and $26.2 million, respectively.

Economic Factors Impacting Future Periods

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

- For the eighth consecutive year, UK HealthCare is ranked as the No. 1 hospital in Kentucky in the 2023-24 Best Hospitals rankings and ratings from U.S. News & World Report. Annual inpatient discharges from UK's hospitals exceeded 42,300 for fiscal year 2023, about 900 discharges above budget. Ambulatory visits topped 1.3 million in FY23, almost 100,000 visits above budget. Markey Cancer Center, Kentucky's only NCI-designated cancer center, was included in the U.S. News Top 50 national ranking for cancer care for the seventh consecutive year.
- Effective December 1, 2022, the King's Daughters health system located in Ashland, Kentucky, was integrated in the System significantly expanding patient access to UK HealthCare.
- In December 2022, the UK Board of Trustees approved construction of an outpatient cancer and advanced ambulatory building and parking garage on the west side of South Limestone to support Markey's mission to increase access for Kentucky's most complex patients. UK HealthCare's Kentucky Children's Hospital opened a new behavioral health unit for pediatric patients.
- In April 2023, the board approved construction of an additional three floors for ambulatory services within the building, which is projected to open in 2027. The board also endorsed a financial plan that projects $2.4 billion in capital investments across FY23-FY28. Investments include a second patient bed tower on the Chandler campus, new operating suites and new procedures rooms; recruiting and retaining a workforce that aligns with volume growth rates while reducing agency workforce; establishing pipelines to building workforce; and design/plan of four additional ambulatory sites based on UK employee residence, demographic growth and accessibility in underserved areas of Fayette County. In April 2023, the board also endorsed UK HealthCare moving forward with design planning of a medical office building to be located on the approximately 27 acres of property in the Hamburg development along U.S. Interstate I-75.

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENT OF NET POSITION (in thousands)
JUNE 30, 2023

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES		
Current Assets		
Cash and cash equivalents	$	1,554,289
Accounts receivable, net (less allowance for doubtful accounts of $113,276)		541,578
Inventories and other assets		92,900
Investments		1,020
Estimated third-party payer settlements		482,603
Notes receivable		3,068
Total current assets		2,675,458
Noncurrent Assets		
Restricted cash and cash equivalents		91,694
Long-term investments		802,848
Capital assets, net		1,545,405
Lease assets, net		100,027
Subscription assets, net		29,639
Notes receivable		866
Other assets		10,789
Total noncurrent assets		2,581,268
Total assets		5,256,726
Deferred Outflows of Resources		15,973
Total assets and deferred outflows of resources		5,272,699
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES		
Current Liabilities		
Accounts payable and accrued liabilities		293,442
Unearned revenue		53,167
Estimated third-party payer settlements		15,739
Long-term debt - current portion		35,349
Lease liabilities - current portion		25,336
Subscription liabilities - current portion		10,222
Total current liabilities		433,255
Noncurrent Liabilities		
Long-term liabilities - other		70,564
Long-term liabilities - debt		670,936
Lease liabilities		77,163
Subscription liabilities		15,972
Net pension liabilities		9,927
Total noncurrent liabilities		844,562
Total liabilities		1,277,817
Deferred Inflows of Resources		1,005
Total liabilities and deferred inflows of resources		1,278,822
NET POSITION		
Net investment in capital assets		805,636
Restricted		
Nonexpendable-other		2,322
Expendable		
Debt Service		59
Capital projects		2,262
Other		10,379
Total restricted expendable		12,700
Total restricted		15,022
Unrestricted		3,173,219
Total net position	$	3,993,877

See notes to the financial statements

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION (in thousands)
FOR THE YEAR ENDED JUNE 30, 2023

OPERATING REVENUES	
Net patient service revenues, less provision for doubtful accounts of $123,297	$ 3,564,984
Sales and services	153,889
Grant revenue	1,843
Management contract revenue	61,648
Total operating revenues	3,782,364
OPERATING EXPENSES	
Salaries and wages	1,020,605
Fringe benefits	274,118
Supplies	914,053
Purchased services	366,369
Other expenses	293,399
Depreciation and amortization	140,649
Management contract expenses	57,271
Total operating expenses	3,066,464
Net income from continuing operations	715,900
NONOPERATING REVENUES (EXPENSES)	
Additions to permanent endowments	460
Gifts and non-exchange grants	5,752
Capital gifts	346
Investment income	93,617
Interest on capital asset-related debt	(26,507)
Loss on disposal of capital assets	(42)
Other, net	(17,692)
Net nonoperating revenue	55,934
Net income before other revenues, expenses, gains or losses, and special item	771,834
Transfers to the University of Kentucky for noncapital purposes	(56,856)
Transfers to the University of Kentucky for capital purposes	(15,716)
Special item - acquisition of Royal Blue Health and Insure Blue	695,582
Total other revenue	623,010
INCREASE IN NET POSITION	1,394,844
NET POSITION, beginning of year	2,599,033
NET POSITION, end of year	$ 3,993,877

See notes to the financial statements

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENT OF CASH FLOWS (in thousands)
FOR THE YEAR ENDED JUNE 30, 2023

CASH FLOWS FROM OPERATING ACTIVITIES	
Net patient service revenues	$ 3,369,994
Sales and services	147,198
Grant revenue	1,899
Management contract services	52,217
Payments to vendors and contractors	(1,561,610)
Salaries, wages and fringe benefits	(1,267,760)
Payments on management contract services	(56,922)
Payments on short-term leases	(1,119)
Other receipts	(1,550)
Net cash provided by operating activities	682,347
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Gifts	6,093
Additions to permanent endowments	460
Payments on loans from University of Kentucky departmental units	475
Transfers to the University of Kentucky for noncapital purposes	(56,856)
Other financing payments	(2,662)
Net cash used by noncapital financing activities	(52,490)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Capital grants and gifts	11
Purchases of capital assets	(131,619)
Principal payments - long-term obligations	(36,007)
Interest payments - long-term obligations	(22,584)
Principal payments received on leases receivable	155
Interest payments received on leases receivable	21
Principal payments - lease payable	(23,643)
Interest payments - lease payable	(2,392)
Principal payments - subscriptions payable	(11,116)
Interest payments - subscriptions payable	(466)
Proceeds from long-term obligations	712
Other capital and related financing payments	(17,140)
Transfers to the University of Kentucky for capital purposes	(14,488)
Net cash used by capital and related financing activities	(258,556)
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from sales and maturities of investments	247,661
Interest and dividends on investments	54,953
Purchase of investments	(226,959)
Cash acquired from acquisition of Royal Blue Health and Insure Blue	44,975
Net cash provided by investing activities	120,630
NET INCREASE IN CASH AND CASH EQUIVALENTS	491,931
CASH AND CASH EQUIVALENTS, beginning of year	1,154,052
CASH AND CASH EQUIVALENTS, end of year	$ 1,645,983

See notes to the financial statements

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENT OF CASH FLOWS (in thousands)
FOR THE YEAR ENDED JUNE 30, 2023

Reconciliation of net income from continuing operations to net cash provided by operating activities:		
Net income from continuing operations	$	715,900
Adjustments to reconcile net income from continuing operations to net cash provided by operating activities:		
Depreciation and amortization		140,649
Write off of principal note receivable		932
Provision for doubtful accounts		123,297
Change in assets and liabilities:		
Accounts receivable		(162,699)
Inventories and other		(4,274)
Estimated third-party payer settlements receivable and payable		(175,365)
Deferred outflows of resources		(12,493)
Other assets		(4,107)
Accounts payable and accrued liabilities		26,714
Unearned revenue		15,584
Long-term liabilities		1,901
Net pension liability		16,467
Deferred inflows of resources		(159)
Net cash provided by operating activities	$	682,347
NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:		
Transfer of capital assets from the University	$	(1,228)
Capital lease additions by Lexington Surgery Center	$	143
Capital asset change in accounts payable and long-term liabilities - other	$	(4,941)
Amortized bond premium	$	3,069
Amortized difference between reacquisition price and net carrying amount of refunded debt	$	908
Investment unrealized gain	$	37,240
Lease obligation incurred for lease assets	$	38,536
Subscription obligations incurred for subscription assets	$	10,186
In conjunction with the acquisition of Royal Blue Health and Insure Blue noncash assets, deferred outflows or resources and liabilities assumed were as follows:		
Patient and other accounts receivable	$	98,310
Other current assets	$	145,964
Other long-term investments	$	405,776
Capital assets	$	395,876
Other assets	$	38,263
Deferred outflows of resources	$	1,015
Current liabilities	$	(108,533)
Long-term debt	$	(239,875)
Other long-term liabilities	$	(85,100)
Deferred inflows of resources	$	(1,089)

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENT OF FIDUCIARY NET POSITION (in thousands)
JUNE 30, 2023

ASSETS	
Cash and cash equivalents	$ 1,147
Accrued interest receivable	112
Investments	52,502
Total assets	53,761
LIABILITIES	
Accounts payable and accrued liabilities	—
Total liabilities	—
NET POSITION	
Net position restricted for postemployment benefits	$ 53,761

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENT OF CHANGES IN FIDUCIARY NET POSITION (in thousands)
FOR THE YEAR ENDED JUNE 30, 2023

Revenues	
Investment loss:	
Interest and dividend income	$ 203
Net decrease in fair value of investments	(1,248)
Net investment loss	(1,045)
Contributions:	
University of Kentucky	—
Beneficiaries	—
Total contributions	—
Total loss	(1,045)
Expenses	
Administrative expenses	6
Payments to retirees and beneficiaries	359
Total expenses	365
Acquisition of Royal Blue Health	55,171
INCREASE IN NET POSITION	53,761
NET POSITION restricted for postemployment benefits, beginning of year	—
NET POSITION restricted for postemployment benefits, end of year	$ 53,761

See notes to the financial statements

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., a wholly owned for-profit subsidiary, which has no balances or transactions as of and for the year ended June 30, 2023; Beyond Blue Corporation, a wholly owned non-profit subsidiary, and its non-profit subsidiary Royal Blue Health, LLC (RBH or King's Daughters health system), and Insure Blue, formerly Integrated Health Insurance, Ltd; Surgery Blue, LLC, a wholly owned for-profit subsidiary and its for-profit subsidiary, Surgery Center of Lexington, LLC (SCL) (51% ownership). SCL 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, 2022 are included in the System's financial statements as of June 30, 2023.

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

The King's Daughters Medical Center Retirement Plan (Pension Plan) is a single-employee defined benefit plan included in the System's financial statements as a pension trust fiduciary fund. The board of Royal Blue Health, LLC performs the governing duties of the pension plan, as the Pension Plan does not have a separate board. The fiduciary fund statement are presented as of December 31, 2022, the Pension Plan's fiscal year-end.

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:

- <u>Net investment in capital assets:</u> Capital and lease assets, net of accumulated depreciation and amortization and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- <u>Restricted:</u>
  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.

- <u>Unrestricted:</u> 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 University's 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, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*. 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. All endowments are managed in a consolidated investment pool which consists of 2,564 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.

Other investments include U.S. Treasury obligations, equity securities, mutual funds, collective investment funds and real estate funds which are carried at fair value, as determined by the major securities markets. Investments in collective investment funds and real estate funds are stated at net asset value. See note 2 for more information on the fair value determination. Changes in unrealized gains (losses) on the carrying value of investments are reported as a component of investment income (loss) in the Statement of Revenues, Expenses and Changes in Net Position.

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%, 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. For the year ended June 30, 2023, the University's annual endowment management fee was 0.90%.

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 the year ended June 30, 2023, management elected to retain the spending distribution in the quasi-endowment and the amount available for spending in accordance with the University’s endowment spending policy was $15.1 million.

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.

Equipment with a unit cost of $5 thousand and having an estimated useful life of greater than one year is capitalized. Institutional software costing more than $400 thousand 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.

Lease Assets. Lease assets are recorded at the initial measurement of the lease liability, plus payments made at or before the commencement of the lease term, less any lease incentive received from the lessor at or before the commencement of the lease term, plus initial direct costs that are ancillary to place the asset into service. Lease assets are amortized on a straight-line basis over the shorter of the lease term or the useful life of the underlying asset. Lease assets are reported under various assets categories.

Subscription Assets. Subscription assets are initially recorded at the initial measurement of the subscription liability, plus subscription payments made at or before the commencement of the subscription-based information technology arrangement (SBITA) term, less any SBITA vendor incentives received from the SBITA vendor at or before the commencement of the SBITA term, plus capitalizable initial implementation costs. Subscription assets are amortized on a straight-line basis over the shorter of the SBITA term or the useful life of the underlying IT asset.

Capital, Lease and Subscription Assets Impairment. The System evaluates capital, lease and subscription assets for impairment whenever events or circumstances indicate a significant, unexpected decline in the service utility of a capital, lease or subscription asset has occurred. If a capital, lease or subscription asset is tested for impairment and the magnitude of the decline in service utility is significant and unexpected, the accumulated depreciation or accumulated amortization 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 capital, lease, or subscription asset impairment was recognized during the year ended June 30, 2023.

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 were $16.0 million as of June 30, 2023, out of which $13.5 million is RBH's reported deferred outflow of resources related to its Pension Plan. The remaining represents 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 Commonwealth Department for Public Health and administered by the System. The funds are to support the operations of the KADAP Income Reinvestment Program.

Compensated Absences. The amount of vacation leave earned but not taken by employees at June 30, 2023 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.

Interest Rate Swap Agreements. RBH's asset/liability strategy is to have a mixture of fixed- and variable-rate debt to take advantage of market fluctuations. As part of this strategy, RBH entered into the 2016 interest rate swap agreement (2016 agreement) for its 2016 B Bonds. The intention of the swap is to reduce exposure to interest rate fluctuations. The University evaluated the 2016 agreement for effectiveness as of June 30, 2023 under the synthetic instrument method and determined it to be an ineffective hedge, thus it is reported as an investment derivative instrument. RBH has also entered into the 2006 interest rate swap agreement (2006 agreement) that was determined to be an ineffective hedge as the related bonds (hedgeable item) have been retired, thus it is reported as an investment derivative instrument. The agreements with the counterparties are scheduled to end on February 1, 2036, and September 1, 2036, respectively.

As of June 30, 2023, the 2016 agreement had a fair value of $4.4 million and the 2006 agreement has a fair value of $707 thousand calculated using the par value method, i.e., the fixed and variable rates, respectively, on the swaps were compared with the current fixed rates that could be achieved in the marketplace should the swaps be unwound. The fair value of the agreements of $5.1 million was recognized in long-term liabilities - other in the statement of net position and was classified within level 2 of the valuation hierarchy. The change in fair value of the interest rate agreements was $1.3 million for the year ended June 30, 2023 and was recorded in investment income in the statement of revenues, expenses and changes in net position.

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 were $1.0 million as of June 30, 2023, of which $930 thousand is related to RBH and represents payments to be received under lease agreements. The remaining represents 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 non-acute 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 31% and 42%, respectively, of the System's net patient service revenues before the provision for doubtful accounts for the year ended June 30, 2023. 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 the COVID-19 pandemic and unemployment, more Kentuckians applied and received presumptive Medicaid. 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 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. The program is based upon data two years in arrears. The payments are based upon two components: access and quality. For fiscal year 2023, access is 90% of the program and quality is 10%. 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 2023 for July through September 2022. A receivable for these dollars has been applied to the third party liability account for fiscal year 2023. Directed Payments of $814.6 million was recognized in net patient service revenue in fiscal year 2023. The Department of Medicaid Services will be refunding the 5% withhold in the near future thus relieving this receivable.

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.

<u>Management Contract Revenue.</u> The System entered into a contract with the Kentucky Cabinet for Health and Family Services 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 $41.9 million, and $2.2 million, for ESH and CKRC, respectively. The System also receives an eight percent management fee. For fiscal year 2023, the contract included $14.0 million for increased census and COVID costs. 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. The contract was renewed for the period of July 1, 2023 to June 30, 2024.

<u>Charity Care.</u> 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 $82.0 million in fiscal year 2023. The costs of charity care provided under the System's charity

care policy were $24.4 million for the year ended June 30, 2023. The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges.

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 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.

Adoption of GASB Statement No. 96. In May 2020, GASB issued Statement No. 96, *Accounting for Subscription-based Information Technology Arrangements*, which improved the usefulness of financial statements by requiring recognition of information technology subscription-based arrangement assets and liabilities. The System's financial statements now include subscription information technology assets, subscription liabilities and additional components associated with recording subscription assets and subscription liabilities. The adoption of this statement resulted in recording $13.1 million in subscription assets and liabilities as of July 1, 2022.

Recent Accounting Pronouncements. As of June 30, 2023, the GASB has issued the following applicable statements to the System but are not yet implemented.

- GASB Statement No. 101, *Compensated Absences*, issued June 2022. The provisions of this statement are effective for fiscal years beginning after December 15, 2023 (fiscal year 2025). It provides guidance for measuring liability for leave that has not been used, generally using an employee's pay rate as of the date of the financial statements. A liability for leave that has been used but not yet paid or settled should be measured at the amount of the cash payment or noncash settlement to be made. Certain salary-related payments that are directly and incrementally associated with payments for leave also should be included in the measurement of the liabilities. With respect to financial statements prepared using the current financial resources measurement focus, it requires that expenditures be recognized for the amount that normally would be liquidated with expendable available financial resources. The System has yet to determine the impact GASB Statement No. 101 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, 2023 are as follows (in thousands):

Statement of Net Position classification:	
Cash and cash equivalents	$ 1,554,289
Restricted cash and cash equivalents	91,694
Total cash and cash equivalents	1,645,983
Long-term investments	802,848
Total deposits and investments	$ 2,448,831

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 (NAV) per share (or its equivalent), practical expedient, amortized costs, or historical costs and therefore have not been classified in the fair value hierarchy. These investments have been included in the table below to permit reconciliation of the fair value hierarchy to the amounts presented in the Statement of Net Position.

The System has the following valuation measurements, by type, at June 30, 2023 (in thousands):

		Fair Value Measurement Using					
	Total value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total measured at fair value	Net asset value (NAV)	Amortized or historical cost
Cash and cash equivalents	$ 1,645,983	$ —	$ —	$ —	$ —	$ —	$ 1,645,983
Cash surrender value of life insurance policies	41	—	—	—	—	—	41
Diversifying strategies	44,230	44,230	—	—	44,230	—	—
Endowed deposits and investments	406,335	—	—	406,335	406,335	—	—
Global equity - international	52,947	—	943	—	943	52,004	—
Global equity - U.S.	81,884	—	3,878	—	3,878	78,006	—
Global fixed income - public fixed income	171,385	56,021	22,380	—	78,401	92,984	—
Real assets - private	14,318	—	—	—	—	14,318	—
Real assets - public	31,708	—	—	—	—	31,708	—
Total deposits and investments	$ 2,448,831	$ 100,251	$ 27,201	$ 406,335	$ 533,787	$ 269,020	$ 1,646,024

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 the 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, 2023.

The composition of the University's pooled endowment fund based upon fair value at June 30, 2023 is as follows:

	2023
Cash and cash equivalents	0.3 %
Diversifying strategies	12.8 %
Global equity - international	16.6 %
Global equity - private	20.6 %
Global equity - U.S.	23.9 %
Global fixed income - public fixed income	7.9 %
Global fixed income - private credit	3.8 %
Real assets - private	12.4 %
Real assets - public	1.7 %
Total	100.0 %

Investments valued using NAV per share (or its equivalent) as of June 30, 2023 are as follows (in thousands):

		Redemption Frequency/Notice Period						
	Net asset value (NAV)	Daily, weekly/ 1-7 days	Semi-monthly, monthly/ 15-30 days	Quarterly/ 45-90 days	Semi-annually/ 60-180 days	Annually/ 360 days	End of term/ 5-10 years	Unfunded commitments
Global equity - international	$ 52,004	$ 52,004	$ —	$ —	$ —	$ —	$ —	$ —
Global equity - U.S.	78,006	78,006	—	—	—	—	—	—
Global fixed income - public fixed income	92,985	92,985	—	—	—	—	—	—
Real assets - private	14,318	—	—	14,318	—	—	—	—
Real assets - public	31,708	31,708	—	—	—	—	—	—
Total measured at net asset value	$ 269,021	$ 254,703	$ —	$ 14,318	$ —	$ —	$ —	$ —

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 three 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.

- Cash on deposit with local banks and investments in direct obligations of an other obligations guaranteed as to principal by the U.S. Treasury, U.S. agencies and instrumentalities, bank repurchase agreements, corporate bonds, equity securities, money market mutual funds, mutual funds and collective investment funds.
- Endowment investments in the University's pooled endowment fund.

Cash and cash equivalents on deposit with the University are managed within guidelines established by the University's Operating Fund Investment Policy, as approved by the Investment Committee of the University's Board of Trustees and maintained by the Operating Fund Investment Committee.

Endowment investments are managed within 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 changes could affect the investment amounts in the Statement 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.
- Investments in corporate bonds is limited to the top two ratings issued by nationally recognized statistical rating organizations.
- 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 the 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 are invested in deposits and money market funds which 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.

As of June 30, 2023, there were $7.5 million of cash and cash equivalents held by component units of the System by various financial institutions that were exposed to custodial credit risk. These balances were uninsured and uncollateralized.

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 agency securities or other similar investments as provided by Kentucky Revised Statutes 41.240.
- The University's endowment core-plus fixed income manager is 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, 2023, the System had no underlying investments in any one issuer which represented more than five percent of total investments, other than U.S. Treasury and agency obligations.

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.
- Cash and cash equivalents on deposit with local banks and investments in money market mutual funds have limited exposure to interest rate risk due to the short-term nature of the deposits and investments.
- Endowment managers are permitted to use derivative instruments to limit interest rate risk. Additionally, the University's actively managed core-plus fixed income portfolio manager is limited to a duration that is within two years of the duration of the Barclays U.S. Aggregate Bond Index. Unconstrained fixed income strategies have been implemented to further mitigate interest rate risk.

As of June 30, 2023, the System had fixed income securities managed based on duration. The securities duration was 4.5 years as of June 30, 2023.

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, 2023 are as follows (in thousands):

	Gross Receivable	Allowance	Net Receivable
Medicare, Medicaid and other third parties	$ 583,895	$ (44,223)	$ 539,672
Private pay	69,965	(68,207)	1,758
Pledges receivable	994	(846)	148
Total	$ 654,854	$ (113,276)	$ 541,578

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 year ended June 30, 2023, 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 17.6% of patient accounts receivable as of June 30, 2023. A summary of the changes in the allowance for uncollectible patient accounts receivable is as follows:

Balance, beginning of year	$ 65,646
Provision for doubtful accounts	123,297
Receivables charged off, net of recoveries	(75,667)
Balance, end of year	$ 113,276

4. CAPITAL, LEASE, AND SUBSCRIPTION ASSETS, NET

Capital assets as of June 30, 2023 and capital asset activity for the year ended June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Deletions	Balance June 30, 2023
Land	$ 43,458	$ 33,385	$ —	$ 76,843
Non-depreciable land improvements	18,809	—	—	18,809
Depreciable land improvements	9,339	4,913	—	14,252
Buildings	1,123,224	294,734	359	1,417,599
Fixed equipment	58,061	1,334	—	59,395
Infrastructure	31,864	760	—	32,624
Equipment	380,799	124,913	17,457	488,255
Vehicles	1,975	441	599	1,817
Capitalized software	207,453	1,467	—	208,920
Artwork	3,208	50	—	3,258
Construction in process	17,054	70,419	7,043	80,430
Certificate of need	11,609	116	—	11,725
	1,906,853	532,532	25,458	2,413,927
Accumulated Depreciation:				
Depreciable land improvements	7,216	480	—	7,696
Buildings	357,417	40,004	359	397,062
Fixed equipment	34,678	3,852	—	38,530
Infrastructure	14,768	1,286	—	16,054
Equipment	260,999	44,536	13,605	291,930
Vehicles	1,173	233	188	1,218
Capitalized software	101,429	14,603	—	116,032
	777,680	104,994	14,152	868,522
Capital assets, net	$ 1,129,173	$ 427,538	$ 11,306	$ 1,545,405

Reductions to equipment and depreciation included equipment disposed by the Surgery Center of Lexington, LLC, of $1.1 million for both cost and depreciation in fiscal year 2023.

At June 30, 2023, the System has commitments in construction projects in progress totaling approximately $1.06 billion in scope. The estimated cost to complete these projects was approximately $1.01 billion, not including RBH. Such construction is principally financed by the System's cash reserves and proceeds from the System general receipts bonds. Additionally, RBH had capital expenditure commitments of approximately $21.6 million related to construction contracts.

During fiscal year 2023, the System utilized capital financing to acquire various items of land and buildings. The net book value for capitalized land and buildings is $64.6 million at June 30, 2023. The net book value for capitalized leased land, buildings and equipment for the Surgery Center of Lexington, LLC is recorded as $12.0 million for the year ended June 30, 2023.

On December 1, 2022 the System obtained $395.9 million of capital assets, net from the acquisition of RBH.

Lease assets as of June 30, 2023 and lease asset activity for the year ended June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Deletions	Balance June 30, 2023
Land	$ —	$ 469	$ —	$ 469
Buildings	56,388	43,233	—	99,621
Equipment	24,514	16,669	—	41,183
	80,902	60,371	—	141,273
Accumulated amortization:				
Land	—	65	—	65
Buildings	10,883	14,328	—	25,211
Equipment	2,379	13,591	—	15,970
	13,262	27,984	—	41,246
Lease assets, net	$ 67,640	$ 32,387	$ —	$ 100,027

The additions from the acquisition of RBH were $21.8 million.

Subscription assets as of June 30, 2023 and subscription asset activity for the year ended June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Deletions	Balance June 30, 2023
Subscription assets	$ 13,110	$ 24,200	$ —	$ 37,310
Accumulated amortization	—	7,671	—	7,671
Subscription assets, net	$ 13,110	$ 16,529	$ —	$ 29,639

The System adopted GASB Statement No. 96 and recorded subscription assets of $13.1 million as of July 1, 2022, and the additions from the acquisition of RBH were $14.0 million.

5. NOTES RECEIVABLE

Notes receivable at June 30, 2023 are as follows (in thousands):

Non-interest bearing, unsecured receivable from UK College of Pharmacy	$	2,022
Non-interest bearing, unsecured receivable from UK College of Nursing		1,912
Total	$	3,934
Current portion	$	3,068
Noncurrent portion		866
Total	$	3,934

6. OTHER ASSETS

Other assets at June 30, 2023 are as follows (in thousands):

Amounts on deposit with trustee	$	99
Goodwill		2,127
Noncurrent receivable		3,693
Noncurrent portion of prepaid expenses		4,708
Pledges receivable noncurrent, net		162
Total	$	10,789

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, 2023 are summarized as follows (in thousands):

Payable to vendors and contractors	$	149,712
Due to the University of Kentucky		7,280
Accrued expenses, including vacation leave		136,450
Total	$	293,442

8. LONG-TERM DEBT

Long-term debt as of June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Reductions	Balance June 30, 2023	Current Portion	Noncurrent Portion
Bonds, notes and capital debt						
General receipts bonds	$ 469,673	$ —	$ 21,240	$ 448,433	$ 22,380	$ 426,053
Revenue bonds	—	145,245	5,715	139,530	5,545	133,985
Note payable	7,738	2,702	1,748	8,692	2,051	6,641
Due to the University of Kentucky	3,394	—	3,394	—	—	—
Capital financed obligations	21,104	112	2,371	18,845	2,474	16,371
Total	501,909	148,059	34,468	615,500	32,450	583,050
Bonds from direct borrowings and direct placements						
Revenue bonds	—	92,767	1,982	90,785	2,899	87,886
Total	—	92,767	1,982	90,785	2,899	87,886
Total bonds, notes and capital debt	$ 501,909	$ 240,826	$ 36,450	$ 706,285	$ 35,349	$ 670,936

Principal maturities and interest on long-term debt for the next five years and in subsequent five-year periods as of June 30, 2023 are as follows (in thousands):

			Bonds from direct borrowings and direct placements		
	Principal	Interest	Principal	Interest	Total
2024	$ 32,450	$ 25,779	$ 2,899	$ 3,363	$ 64,491
2025	32,690	24,257	3,109	3,237	63,293
2026	34,078	22,765	3,229	3,109	63,181
2027	36,252	22,258	3,338	2,976	64,824
2028	37,926	20,499	3,461	2,842	64,728
2029-2033	126,939	85,540	29,349	10,826	252,654
2034-2038	169,743	51,202	16,205	5,423	242,573
2039-2043	115,692	15,273	9,055	3,766	143,786
2044-2048	29,730	1,895	10,510	2,309	44,444
2049-2052	—	—	9,630	638	10,268
Total	$ 615,500	$ 269,468	$ 90,785	$ 38,489	$ 1,014,242

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 $1.5 million during fiscal year 2023, is included in gifts and non-exchange grants in the Statement 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 33% in fiscal year 2023.

On December 1, 2022, the University acquired RBH via member substitution and the University assumed a total debt obligation of $240.7 million at the time of acquisition. RBH had Revenue Bonds Series 2016 A and B, Revenue Bonds Series 2019 and Revenue Bonds Series 2022. These bonds are secured by a security interest in the gross receipts of RBH and a first lien Mortgage and Security interest in mortgaged property. Payments of bond principal on the Revenue Bonds Series 2019 are also secured by an insurance policy issued by a commercial insurer. These bonds has an original amount of $269.5 million dated September 23, 2016 through September 22, 2022, which bear interest at 3.0% to 5.0%. The bonds are payable in annual installments through February 1, 2052. All bonds are callable on February 1, 2030, except for the series 2016 A which is callable on February 1, 2026.

The RBH Revenue Bonds Series 2016 B and 2022 are from direct borrowing, which are secured by a security interest in the gross receipts of the RBH and a first lien mortgage and security interest in mortgage property. Under the term of the Master Trust Indenture, there are limits on the incurrence of additional borrowing and requirements of certain measures of financial performance to be maintained as long as the bonds are outstanding for the Revenue Bonds Series 2022.

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 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 one percent. The total effective rate was 2.34% for interest payments in fiscal year 2023. The balance of internal loan was paid off in December 2022.

On February 28, 2019, $8.4 million of the Surgery Blue promissory note was issued at a variable interest rate between 3.2% and 4.5%. This note was 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.

RBH has a line of credit with a bank in the amount of $15 million. The borrowing on the line bore interest at the Adjusted Term Secured Overnight Finance Rate rate per annum (2.96% at June 30, 2023). RBH did not have borrowing under the line as of June 30, 2023. The line of credit has maturity date of March 25, 2025.

9. LEASE LIABILITIES

Lease liabilities as of June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Reductions	Balance June 30, 2023	Current Portion	Noncurrent Portion
Land	$ —	$ 470	$ 62	$ 408	$ 107	$ 301
Buildings	45,791	43,389	13,060	76,120	15,046	61,074
Equipment	19,572	16,606	10,207	25,971	10,183	15,788
	$ 65,363	$ 60,465	$ 23,329	$ 102,499	$ 25,336	$ 77,163

The System leases buildings and equipment, the terms of which expire in various years through 2033. The lease liabilities were reported at present value using the University's incremental borrowing rate unless otherwise noted in the contract term.

Principal and interest on lease obligations for the next five fiscal years and in subsequent five-year fiscal periods as of June 30, 2023, are as follows (in thousands):

	Principal	Interest	Total
2024	$ 25,336	$ 2,805	$ 28,141
2025	21,811	2,056	23,867
2026	19,867	1,417	21,284
2027	14,042	882	14,924
2028-2033	21,443	864	22,307
Total	$ 102,499	$ 8,024	$ 110,523

10. SUBSCRIPTION LIABILITIES

Subscription liabilities as of June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Reductions	Balance June 30, 2023	Current Portion	Noncurrent Portion
Subscription liabilities	$ 13,110	$ 24,200	$ 11,116	$ 26,194	$ 10,222	$ 15,972
	$ 13,110	$ 24,200	$ 11,116	$ 26,194	$ 10,222	$ 15,972

The System has various subscription-based technology arrangements (SBITAs), the terms of which expire in various years through 2028. The System adopted GASB Statement No. 96 and recorded subscription liabilities of $13.1 million as of July 1, 2022. The subscription liabilities were reported at present value using the University's incremental borrowing rate unless otherwise noted in the contract term.

Principal and interest on subscription-based technology arrangements for the next five fiscal years and in subsequent five-year fiscal periods as of June 30, 2023, are as follows (in thousands):

	Principal	Interest	Total
2024	$ 10,222	$ 618	$ 10,840
2025	7,830	382	8,212
2026	4,821	182	5,003
2027	3,293	68	3,361
2028	28	—	28
Total	$ 26,194	$ 1,250	$ 27,444

11. PENSION PLANS

On December 1, 2022, the University acquired RBH through member substitution and assumed the obligation of the King's Daughters Medical Center retirement plan (Pension Plan or Plan).

RBH contributes to the King’s Daughter Medical Center retirement plan a single-employer plan covering substantially all employees employed January 1, 2011 and prior. The Pension Plan is administered by the governing board of RBH. Benefit provisions are contained in the plan document and were established and can be amended by action of RBH's governing body. The Plan issues publicly available financial statements and required disclosures through December 31, 2022 which can be obtained at www.efast.dol.gov/5500search/.

The Pension Plan provides retirement and death benefits to plan members and their beneficiaries. Normal retirement benefits for participants 65 years or older are calculated as a monthly benefit equal to the greater of 0.75 percent of the first $650 of their average monthly earnings plus 1-1/4 percent of the excess of their average monthly earnings over $650, all multiplied by years of credited service, to a maximum of 35 years plus 1-1/4 percent of average monthly earnings times credited service in excess of 35 years. Earnings used in the benefit formula cannot exceed $230 thousand indexed as provided by law or a dollar amount multiplied by years of credited service. Early retirement benefits for participants 55 or older and 10 years of service as the normal retirement benefit reduced by 1/300th for each month by the which the commencement date of benefits precedes normal retirement date. Late retirement benefits for participants that are employed beyond age 70 ½ are calculated as the greater of earnings and credited service as of the actual retirement date or the normal retirement benefit increased actuarially to their late retirement date. Death benefits are equal to 50% of the participant’s accrued benefits. If a participant has attained age 55 and completed 10 years of service, the death benefit payable to their spouse is equal to one half of the benefit payable if the participant had elected to retire the day they died and chosen the joint and one-half to spouse form of payment. If a participant dies prior to attaining age 55 but after completing five years of service, his spouse (if any) is entitled to a benefit commencing at the time the participant could have retired, if still living, and equal to 50% of the qualified joint and 50% survivor benefit payable at retirement.

Effective January 1, 2011, a plan amendment was approved to freeze the benefit accruals in the plan. New employees since the amendment date have not been eligible to participate.

For Plan reporting purposes, GASB Statement No. 67, Financial Reporting for Pension Plans, measures net pension liability as of December 31, 2022 for fiscal year 2023. For employer reporting purposes, GASB Statement No. 68, Accounting and Financial Reporting for Pensions, measures net pension liability as of December 31, 2022 for fiscal year 2023. The following note disclosure is presented in order to comply with GASB Statement No. 67 and GASB Statement No. 68.

The net pension liability was measured as of December 31, 2022 for the period from December 1, 2022 through June 30, 2023. The total pension liability used to calculate the net pension liability was determined using an actuarial valuation as of January 1, 2021 and rolled forward to December 31, 2022 using the following actuarial assumptions as of December 31, 2022:

Inflation	N/A
Salary increases	N/A
Investment rate of return	5.25% net of pension plan investment expense

Mortality rates were based on the Pri-2012 employee and retiree tables, no collar. For surviving beneficiaries of deceased participants: Pri-2012 contingent survivor mortality table. All tables include generational projection based on SOA Scale Mortality Projection-2021.

The actuarial assumptions used in the June 30, 2023 valuation was based on the results of an actuarial experience study for the period January 1, 2022 through December 31, 2022.

The members covered by the Plan at December 31, 2022 are as follows:

Inactive members or beneficiaries currently receiving benefits	669
Inactive members entitled to but not yet receiving benefits	279
Active plan members	290
Total plan members	1,238

The Plan legally invests in direct obligations and other obligations guaranteed as to principal by the U.S. Treasury, U.S. agencies and instrumentalizes, bank repurchase agreements, corporate bonds, equity securities, money market mutual funds, mutual funds and collective investment funds.

The fair value of deposits and investments, by Statement of Fiduciary Net Position classification, at June 30, 2023 is as follows (in thousands):

Statement of Fiduciary Net Position classification		
Cash and cash equivalents	$	1,147
Investments		52,502
Total deposits and investments	$	53,649

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. See footnote 2 for a description of the framework used to measure fair value.

The University categorizes its fair value measurements within the fair value hierarchy. Certain investments are measured at amortized costs or historical costs and therefore have not been classified in the fair value hierarchy. These investments have been included in the table below to permit reconciliation of the fair value hierarchy to the amounts presented in the Statement of Fiduciary Net Position.

The Pension Plan has the following valuation measurements, by type, at June 30, 2023 (in thousands):

		Fair Value Measurement Using			
	Total value	Quoted prices in active markets for identical assets (Level 1)	Total measured at fair value	Net asset value (NAV)	Amortized or historical cost
Cash and cash equivalents	$ 1,147	$ —	$ —	$ —	$ 1,147
Diversifying strategies	2,268	—	—	2,268	—
Global equity - international	6,569	—	—	6,569	—
Global equity - U.S.	9,854	—	—	9,854	—
Global fixed income - public fixed income	30,143	30,143	30,143	—	—
Real assets - private	1,960	—	—	1,960	—
Real assets - public	1,708	—	—	1,708	—
Total deposits and investments	$ 53,649	$ 30,143	$ 30,143	$ 22,359	$ 1,147

The pension trust investments are exposed to various risks. Due to the level of risk associated with certain investments securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could affect the investment amounts in the Statement of Fiduciary Net Position.

The trustee of the pension trust diversifies the investments to minimize the risk of losses due to credit risk, interest rate risk, currency and other risks, as appropriate, based on market conditions. At June 30, 2023, the pension trust had no underlying investments in any one issuer which represented more than five percent of total investments, other than U.S. Treasury and agency obligations, as a way to limit concentration of credit risks. See note 2 for a description of credit, interest rate, foreign currency and concentration of credit risks.

For the year ended June 30, 2023, the annual money-weighted rate of return on the Plan investments, net of Plan investment expense, was (19.17)%. The money-weighted rate of return expresses investment performance, net of investment expenses, adjusted for the changing amounts actually invested.

The long-term expected rate of return on pension plan investments was determined using a building-block approach considering the Plan's long-term inflation assumption of 2.5%, the Plan's target asset allocation, long-term real rate of return for each asset class and net of assumed investment expenses.

The target allocation and real rate of return for both the University and Plan for each major asset class are summarized in the following table:

	Target Allocation	Long-Term Expected Real Rate of Return (Geometric)
Asset Class		
Fixed income	55%	3.0%
Global equity	32%	5.9%
Hedged equity	5%	2.4%
Inflation sensitive assets	8%	2.1%
Total	100%	

The discount rate is based on the expected rate of return on pension plan investments (net of investment expenses) of 5.25% and a municipal bond rate of 3.72%. Considering the Plan's contribution history in the most recent five-years, as well as our professional judgment that at a non-ERISA Plan, the Plan will formulate a contribution policy to target full funding, the pension plan's fiduciary net position and future contributions are projected to be sufficient to finance the future benefit payments of the current plan members for all projection years. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of the projected benefit payments to determine the total pension liability.

RBH's governing body has the authority to establish and amend the contribution requirements and definition of active employees. The governing body establishes rates based on an actuarially determined rate recommended by an independent actuary. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. RBH is required to contribute the actuarially determined rate. The employees may not make contributions to the Plan. For the period from December 1, 2022, through June 30, 2023, the System's contribution was $0.

Changes in the total pension liability, plan fiduciary net position and the net pension liability for the University and Plan at June 30, 2023 are as follows (in thousands):

	Increase (decrease)		
	Total Pension liability (asset)	Plan fiduciary net position	Net Pension liability (asset)
Balance, beginning of period 12/1/2022 (based on 12/31/2021 measurement date)	$ 64,721	$ 71,262	$ (6,541)
Change recognized for the fiscal year:			
Interest	3,285	—	3,285
Contributions from the employer	—	1,015	(1,015)
Net investment income	—	(13,255)	13,255
Benefit payments	(4,318)	(4,318)	—
Administrative expense	—	(943)	943
Net changes	(1,033)	(17,501)	16,468
Balance recognized at 6/30/2023 (based on 12/31/2022 measurement date)	$ 63,688	$ 53,761	$ 9,927

The net pension liability of the Plan has been calculated using a discount rate of 5.25%. The following presents the net pension liability, as well as what the University's net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower (4.25%) or one-percentage-point higher (6.25%) than the current discount rate (in thousands):

	1% Decrease (4.25%)	Current Rate (5.25%)	1% Increase (6.25%)
Total pension liability	$ 70,196	$ 63,688	$ 58,194
Plan fiduciary net position	(53,761)	(53,761)	(53,761)
Net pension liability	$ 16,435	$ 9,927	$ 4,433

For the period from December 1, 2022, through June 30, 2023, the University recorded pension expense of $4.0 million. At June 30, 2023, the University reported deferred outflows of resources related to pensions of $13.5 million for the net difference between projected and actual earnings on pension plan investments.

Deferred outflows of resources as of June 30, 2023, related to pensions will be recognized in pension expense as follows:

2024	$	3,377
2025		3,377
2026		3,377
2027		3,377
	$	13,508

12. LONG-TERM LIABILITIES - OTHER

Other long-term liabilities as of June 30, 2023 are summarized as follows (in thousands):

	Balance June 30, 2022	Additions	Reductions	Balance June 30, 2023
Refundable deposits	$ (3)	$ 13	$ —	$ 10
Workers compensation	207	—	34	173
Construction retainage	562	963	562	963
Unamortized bond premium	18,780	—	3,069	15,711
Capital payable	8,350	49,171	3,814	53,707
Total	$ 27,896	$ 50,147	$ 7,479	$ 70,564

13. 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, 2023 are as follows (in thousands):

Working capital requirements	$	1,976,624
Future capital expenditures		1,196,595
Total	$	3,173,219

14. INVESTMENT INCOME

Components of investment income for the year ended June 30, 2023 are as follows (in thousands):

Interest and dividends earned on endowment investments	$	5,168
Realized and unrealized gains on endowment investments		26,006
Interest and dividends on cash and non-endowment investments		61,619
Realized and unrealized gains on non-endowment investments		824
Total	$	93,617

15. 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 from 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 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 $649.9 million as of June 30, 2023. Principal and interest paid for the year ended June 30, 2023 was $39.3 million.

16. 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.

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 was approximately $58.0 million for the year ended June 30, 2023. Employees contributed $29.0 million during fiscal year 2023. The payroll for employees covered by the retirement plans was $579.8 million for fiscal year 2023.

The King’s Daughters Medical Center Center’s Base Contribution Plan and Matching Contribution Plan were established to cover substantially all RBH’s employees employed subsequent to December 31, 1992, (except for collectively bargained employees at that time) who qualifies as to age and length of service and those employees who were participates in the defined benefit plan and qualify as to length of service, but as of January 1, 2011 elected to become a limited participant in the defined benefit plan and an active participant in the defined contribution plans. Effective January 1, 2011, employees subject to collective bargaining may participate in the Base and Matching Plans. The contributions are three percent of the participants’ compensation for the Base Plan and 50% of eligible participants contributes up to three percent of the employee's contribution for the Matching Plan, unless such contributions are suspended or terminated. RBH’s contributions were approximately $9.8 million to the Plans for the Period from December 1, 2022, through the fiscal year ended June 30, 2023.

17. HEALTH INSURANCE BENEFITS FOR RETIREES

The University administers a single-employer defined-benefit healthcare plan including medical and prescription drug benefits. The plan provides lifetime healthcare insurance benefits for eligible retirees and their surviving spouses. 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% of the "true retiree" cost of the post-65 medical plan. However, retirees must pay the greater of $88 per month for fiscal year 2023 or 10% of total plan costs.

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 Other Postemployment Benefit trust based on a funding policy supported by an actuarial study in accordance with the parameters of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*.

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 as of June 30, 2023.

18. 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 Commonwealth's 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 $10 thousand and $5.0 million per occurrence. Losses in excess of $5.0 million are insured by commercial carriers up to $1.00 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 $250 thousand for any one person or $400 thousand for all persons damaged by a single act of negligence. Claims against educators' errors and omissions and wrongful acts are insured through a reciprocal risk retention group. There have been no significant reductions in insurance coverage from fiscal year 2022 to 2023. 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. 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 4.5%. The malpractice liability at June 30, 2023 is based on the requirements of GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, 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, 2023. 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, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. 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, 2023.

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 as of June 30, 2023.

19. 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 $26.7 million in fiscal year 2023 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 2023, the System received payments of approximately $34.0 million from the University for the capitation health plan. Noncapital transfers between the System and the University were $56.9 million for fiscal year 2023. In addition, capital transfers from the University were $15.7 million for fiscal year 2023.

20. 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 year ended June 30, 2023, the System received income from this trust of approximately $0. The market value of the irrevocable external trust assets as of June 30, 2023 was approximately $75 thousand.

21. MEMBER SUBSTITUTION

In April 2021, the University entered into a significant joint venture through the Affiliation, Member Substitution and Formation Agreement dated January 29, 2021, by and among King’s Daughters Health System, Inc. (KDHS), Beyond Blue Corporation, a component unit of the University (“the UK Member”), and Royal Blue Health LLC (RBH). Effective December 1, 2022, King’s Daughters Health System, Inc. transferred its membership interest in RBH to Beyond Blue Corporation, whereby Beyond Blue Corporation became the sole member of RBH, and the Operating Agreement of RBH was also amended and restated such that the University appoints the governing board of RBH, and upon dissolution of RBH, the net assets revert to Beyond Blue Corporation. The primary reason for the combination is to increase the availability and quality of healthcare services while providing high-quality, efficient, and cost-effective healthcare services for the benefit of the communities in which the King’s Daughters health system operates. The consideration provided in connection with the combination was the assumption of $387.2 million in liabilities of RBH. Beyond Blue Corporation acquired $1.08 million in assets and $695.5 million of net position from the acquisition of RBH.

22. COMBINED CONDENSED STATEMENTS

The System and its blended component units' statements are summarized as follows for the year ended June 30, 2023:

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED CONDENSED STATEMENT OF NET POSITION (in thousands)
AS OF JUNE 30, 2023

	University of Kentucky Healthcare	Surgery Blue, LLC	Beyond Blue Corporation	Eliminations	Total
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES					
Current Assets					
Cash and cash equivalents	$ 1,443,069	$ 2,676	$ 108,544	$ —	$ 1,554,289
Accounts receivable,net (less allowance for doubtful accounts of $113,276)	463,654	1,592	76,332	—	541,578
Inventories and other assets	63,048	102	29,750	—	92,900
Investments	—	—	1,020	—	1,020
Estimated third-party payor settlements	303,474	—	179,129	—	482,603
Notes receivable	3,068	—	—	—	3,068
Total current assets	2,276,313	4,370	394,775	—	2,675,458
Noncurrent Assets					
Restricted cash and cash equivalents	87,826	—	3,868	—	91,694
Equity in health care corporations	1,278	—	—	(1,278)	—
Long-term investments	408,224	—	396,473	(1,849)	802,848
Capital assets, net	1,123,705	11,960	409,740	—	1,545,405
Lease assets, net	80,077	—	19,950	—	100,027
Subscription assets, net	18,004	—	11,635	—	29,639
Notes receivable	866	—	—	—	866
Other assets	4,969	2,127	3,693	—	10,789
Total noncurrent assets	1,724,949	14,087	845,359	(3,127)	2,581,268
Total assets	4,001,262	18,457	1,240,134	(3,127)	5,256,726
Deferred Outflows of Resources	2,465	—	13,508	—	15,973
Total assets and deferred outflows of resources	4,003,727	18,457	1,253,642	(3,127)	5,272,699
LIABILITIES AND DEFERRED INFLOWS OF RESOURCES					
Current Liabilities					
Accounts payable and accrued liabilities	199,135	1,671	92,636	—	293,442
Unearned revenue	52,979	—	188	—	53,167
Estimated third-party payor settlements	—	—	15,739	—	15,739
Long-term debt - current portion	24,524	1,176	9,649	—	35,349
Lease liabilities - current portion	20,179	—	5,157	—	25,336
Subscription liabilities - current portion	5,865	—	4,357	—	10,222
Total current liabilities	302,682	2,847	127,726	—	433,255
Noncurrent Liabilities					
Long-term liabilities - other	28,990	101	41,473	—	70,564
Long-term liabilities - debt	436,954	11,541	222,441	—	670,936
Lease liabilities	62,580	—	14,583	—	77,163
Subscription liabilities	10,098	—	5,874	—	15,972
Net pension liabilities	—	—	9,927	—	9,927
Total noncurrent liabilities	538,622	11,642	294,298	—	844,562
Total liabilities	841,304	14,489	422,024	—	1,277,817
Deferred Inflows of Resources	75	—	930	—	1,005
Total liabilities and deferred inflows of resources	841,379	14,489	422,954	—	1,278,822
NET POSITION					
Net investment in capital assets	622,847	—	182,789	—	805,636
Restricted					
Nonexpendable other	2,322	—	—	—	2,322
Expendable	12,294	—	406	—	12,700
Total restricted	14,616	—	406	—	15,022
Unrestricted	2,524,885	3,968	647,493	(3,127)	3,173,219
Total net position	$ 3,162,348	$ 3,968	$ 830,688	$ (3,127)	$ 3,993,877

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION (in thousands)
FOR THE YEAR ENDED JUNE 30, 2023

	University of Kentucky Healthcare	Surgery Blue, LLC	Beyond Blue Corporation	Eliminations	Total
OPERATING REVENUES					
Net patient service revenues, less provision for doubtful accounts of $123,297	$ 2,981,119	$ 19,134	$ 581,506	$ (16,775)	$ 3,564,984
Sales and services	96,884	29	56,976	—	153,889
Grant Revenue	—	—	1,843	—	1,843
Management contract revenue	61,648	—	—	—	61,648
Total operating revenues	3,139,651	19,163	640,325	(16,775)	3,782,364
OPERATING EXPENSES					
Salaries and wages	784,010	3,910	232,685	—	1,020,605
Fringe benefits	208,646	917	64,555	—	274,118
Supplies	796,475	7,619	109,959	—	914,053
Purchased services	317,693	417	48,259	—	366,369
Other expenses	250,169	2,263	40,967	—	293,399
Depreciation and amortization	113,129	1,354	26,166	—	140,649
Management contract expenses	57,271	—	—	—	57,271
Total operating expenses	2,527,393	16,480	522,591	—	3,066,464
Net income (loss) from continuing operations	612,258	2,683	117,734	(16,775)	715,900
NONOPERATING REVENUES (EXPENSES)					
Additions to permanent endowments	460	—	—	—	460
Gifts and non-exchange grants	5,723	—	29	—	5,752
Capital gifts	335	—	11	—	346
Investment income	78,066	43	15,273	235	93,617
Interest on capital asset-related debt	(19,715)	(588)	(6,204)	—	(26,507)
Gain (loss) on disposal of capital assets	(47)	—	5	—	(42)
Other, net	(31,805)	(2,600)	(62)	16,775	(17,692)
Net nonoperating revenues (expenses), net	33,017	(3,145)	9,052	17,010	55,934
Net income (loss) before other revenues, expenses, gains or losses, and special item	645,275	(462)	126,786	235	771,834
Transfers to the University of Kentucky for noncapital purposes	(56,659)	—	(197)	—	(56,856)
Transfers from the University of Kentucky for capital purposes	(15,716)	—	—	—	(15,716)
Special item - acquisition of Royal Blue Health and Insure Blue	—	—	695,582	—	695,582
Total other revenues (expenses)	(72,375)	—	695,385	—	623,010
INCREASE (DECREASE) IN NET POSITION	572,900	(462)	822,171	235	1,394,844
NET POSITION, beginning of year	2,589,448	4,430	8,517	(3,362)	2,599,033
NET POSITION, end of year	$ 3,162,348	$ 3,968	$ 830,688	$ (3,127)	$ 3,993,877

UNIVERSITY OF KENTUCKY HEALTHCARE
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
COMBINED CONDENSED STATEMENT OF CASH FLOWS (in thousands)
FOR THE YEAR ENDED JUNE 30, 2023

	University of Kentucky Healthcare	Surgery Blue, LLC	Beyond Blue Corporation	Eliminations	Total
CASH FLOWS FROM OPERATING ACTIVITIES					
Net patient service revenues	$ 2,833,011	$ 19,538	$ 517,445	$ —	$ 3,369,994
Sales and services	96,884	29	50,285	—	147,198
Grant revenue	—	—	1,899	—	1,899
Management contract services	52,217	—	—	—	52,217
Payments to vendors and contractors	(1,357,682)	(10,384)	(193,544)	—	(1,561,610)
Salaries, wages and fringe benefits	(979,264)	(4,326)	(284,170)	—	(1,267,760)
Payments on management contract services	(56,922)	—	—	—	(56,922)
Payments on short-term leases	(1,119)	—	—	—	(1,119)
Other receipts (payments)	(1,564)	14	—	—	(1,550)
Net cash provided by operating activities	585,561	4,871	91,915	—	682,347
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES					
Gifts	6,064	—	29	—	6,093
Additions to permanent endowments	460	—	—	—	460
Loan to University of Kentucky departmental units	475	—	—	—	475
Transfers to the University of Kentucky for noncapital purposes	(54,059)	(2,600)	(197)	—	(56,856)
Other financing payments	(2,600)	—	(62)	—	(2,662)
Net cash used by noncapital financing activities	(49,660)	(2,600)	(230)	—	(52,490)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Capital grants and gifts	—	—	11	—	11
Purchases of capital assets	(98,618)	(123)	(32,878)	—	(131,619)
Principal payments - long-term obligations	(26,688)	(822)	(8,497)	—	(36,007)
Interest payments - long-term obligations	(16,831)	(588)	(5,165)	—	(22,584)
Principal payments received on leases receivable	—	—	155	—	155
Interest payments received on leases receivable	—	—	21	—	21
Principal payments - lease payable	(19,614)	(316)	(3,713)	—	(23,643)
Interest payments - lease payable	(2,086)	—	(306)	—	(2,392)
Principal payments - subscriptions payable	(7,036)	—	(4,080)	—	(11,116)
Interest payments - subscriptions payable	(391)	—	(75)	—	(466)
Proceeds from long-term obligations	—	—	712	—	712
Other capital and related financing payments	(17,145)	—	5	—	(17,140)
Transfers from the University of Kentucky for capital purposes	(14,488)	—	—	—	(14,488)
Net cash used by capital and related financing activities	(202,897)	(1,849)	(53,810)	—	(258,556)
CASH FLOWS FROM INVESTING ACTIVITIES					
Proceeds from sales and maturities of investments	173,161	—	74,500	—	247,661
Interest and dividends on investments	51,764	43	3,146	—	54,953
Purchase of investments	(172,914)	—	(54,045)	—	(226,959)
Cash acquired from acquisition of Royal Blue Health and Insure Blue	—	—	44,975	—	44,975
Net cash provided by investing activities	52,011	43	68,576	—	120,630
NET INCREASE IN CASH AND CASH EQUIVALENTS	385,015	465	106,451	—	491,931
CASH AND CASH EQUIVALENTS, beginning of year	1,145,880	2,211	5,961	—	1,154,052
CASH AND CASH EQUIVALENTS, end of year	$ 1,530,895	$ 2,676	$ 112,412	$ —	$ 1,645,983

UK HEALTHCARE HOSPITAL SYSTEM
AN ORGANIZATIONAL UNIT OF THE UNIVERSITY OF KENTUCKY
REQUIRED SUPPLEMENTARY INFORMATION

1. UK HEALTHCARE HOSPITAL SYSTEM NET PENSION LIABILITY AND RELATED RATIOS

SCHEDULE OF CHANGES IN THE NET PENSION LIABILITY (in thousands) AND RELATED RATIOS

	2023
Total pension liability	
Interest cost	$ 3,285
Benefit payments	(4,318)
Net change in total pension liability	(1,033)
Total pension liability, beginning	—
Acquisition of Royal Blue Health	64,721
Total pension liability, ending	63,688
Plan fiduciary net position	
Contributions - employer	1,015
Net investment income	(13,255)
Benefit payments, including refunds of employee contributions	(4,318)
Administrative expense	(943)
Net change in plan fiduciary net position	(17,501)
Plan fiduciary net position, beginning	—
Acquisition of Royal Blue Health	71,262
Plan fiduciary net position, ending	53,761
Net pension liability, ending	$ 9,927
Plan fiduciary net position as a percentage of total pension liability	84.4%
Covered-employee payroll	N/A
Net pension liability as a percentage of covered-employee payroll	0%

Notes to schedule:

The Schedule of Changes in the Net Pension Liability and Related Ratios is presented as of the measurement date of the December 31 prior to the end of the fiscal year listed above. Ten years of data for the Pension Plan is required and will be added as information becomes available.

Change of assumptions and benefit terms:

2023: The mortality table was updated to reflect the most recent publicly available, with mortality improvement projected generationally using scale Mortality Projection-2021.

SCHEDULE OF PENSION INVESTMENT RETURNS

Year	Annual money-weighted rate of return, net of investment expenses
2023	(19.17%)

SCHEDULE OF PENSION CONTRIBUTIONS (in thousands)

	2023
Actuarially determined contribution	$ —
Contribution in relation to actuarially determined contribution	—
Contribution deficiency (excess)	$ —
Covered employee payroll	N/A
Contribution as a percentage of covered employee payroll	0%

Notes to schedule:

Actuarially determined contributions rates are calculated as of December 1, prior to the end of the fiscal year in which contributions are reported. Ten years of data for the Pension Plan is required and will be added as information becomes available.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	The actuarial cost method used was entry age normal level percentage of pay.
Amortization method	The amortization method was level dollar, closed (pursuant to ERISA minimum required contribution).
Remaining Amortization period	The remaining amortization period was 15 years for new gains/losses.
Asset valuation method	Three year smoothed market date.
Inflation	2.5%
Salary increases	N/A
Investment rate of return	The investment rate of return was 5.25%.
Retirement age	Age-specific rates starting at age 55 with 100% retirement at age 70.
Mortality	Pri-2012 employee and retiree tables, no collar. For surviving beneficiaries of deceased participants: Pri-2012 contingent survivor mortality table. All tables include generational projection based on SOA Scale Mortality Projection-2021.

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

UNIVERSITY FINANCIAL SERVICES

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https://www.uky.edu/ufs/financial-statements

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