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UNIVERSITY OF
KENTUCKY[®]

*Gluck Equine Research
Foundation, Inc.*

2008 Financial Statements

University of Kentucky
Gluck Equine Research Foundation, Inc.
A Component Unit of the University of Kentucky

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Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Directors
University of Kentucky
Gluck Equine Research Foundation, Inc.
Lexington, Kentucky

We have audited the accompanying basic financial statements of University of Kentucky Gluck Equine Research Foundation, Inc. (Foundation), a not-for-profit corporation affiliated with and a component unit of the University of Kentucky, as of and for the year ended June 30, 2008, as listed in the table of contents. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Foundation as of and for the year ended June 30, 2007, were audited by other accountants whose report dated November 15, 2007, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2008 financial statements referred to above present fairly, in all material respects, the financial position of the Foundation as of June 30, 2008, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying management's discussion and analysis as listed in the table of contents is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

BKD, LLP

September 29, 2008

Management's Discussion and Analysis

The University of Kentucky Equine Research Foundation's (the Foundation) Management Discussion and Analysis (MD&A) of its financial condition provides an overview of the financial performance of the Foundation for the years ended June 30, 2008 and 2007. Management has prepared this discussion, which provides summary financial information, along with the financial statements and related footnotes. MD&A should be read in conjunction with the accompanying financial statements.

Financial Highlights

- The financial statements for FY 2007-2008 still report a solid financial condition at June 30, 2008 despite a loss on endowment investments due to declining market conditions. Financial operations were in accordance with the revenue expectations and the approved budget plan.
- Total assets decreased approximately \$3.2 million or 24.8%, due to a decrease in endowment investments of approximately \$1.2 million due to a decrease in market value, and a decrease in cash and cash equivalents of approximately \$2 million due to the funding of several endowments established by the Koller Gift and funding of a new building.
- Total net assets decreased approximately \$3.2 million or 24.8%, primarily due to an increase in grants to the University of Kentucky to fund the endowments and building discussed above. Net assets represented 100% of total assets.

Using the Annual Report

This financial report consists of three financial statements: the Statement of Net Assets; the Statement of Revenues, Expenses and Changes in Net Assets; and the Statement of Cash Flows. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*.

One of the most important questions asked about the Foundation's finances is whether the Foundation is better off as a result of the year's activities. One key to answering this question is the financial statements of the Foundation. The Statement of Net Assets; Statement of Revenues, Expenses and Changes in Net Assets; and the Statement of Cash Flows present financial information on the Foundation in a format similar to that used by corporations and present a long-term view of the Foundation's finances. The Foundation's net assets (the difference between assets and liabilities) are one sign of the Foundation's financial health. Over time, increases or decreases in net assets indicate the improvement or erosion of the Foundation's financial health.

The Statement of Net Assets includes all assets and liabilities. It 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.

The Statement of Revenues, Expenses and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. Gifts and endowment and investment income are classified as operating revenues because fundraising is the Foundation's primary operating purpose.

Another important factor to consider when evaluating financial viability is the Foundation's ability to meet financial obligations as they become due. The Statement of Cash Flows presents information related to cash inflows and outflows, summarized by operating, capital, financing and investing activities.

Reporting Entity

The University of Kentucky Gluck Equine Research Foundation, Inc. is a not-for-profit Kentucky corporation formed to establish a continuing partnership between the University of Kentucky and the equine industry of the Commonwealth of Kentucky. The Foundation's objective is to enhance and improve the equine research program at the University of Kentucky (the University) so that it will be one of the finest in the world. The Foundation is considered to be an affiliate and component unit of the University because all Board members are related to the University as faculty, staff or trustees and/or are appointed by the President of the University, and certain of the officers of the Foundation are officers of the University.

Condensed Financial Information

Statements of Net Assets

	<u>2008</u>	<u>2007</u>	<u>2006</u>
ASSETS			
Current assets	\$ 913,598	\$ 2,950,157	\$ 2,808,305
Noncurrent assets	8,766,817	9,936,629	8,902,750
Total assets	<u>9,680,415</u>	<u>12,886,786</u>	<u>11,711,055</u>
LIABILITIES			
Current liabilities	-	-	8,500
Total liabilities	<u>-</u>	<u>-</u>	<u>8,500</u>
NET ASSETS			
Restricted			
Nonexpendable	4,607,071	4,607,071	4,607,071
Expendable	5,073,344	8,279,715	7,095,484
Total net assets	<u>\$ 9,680,415</u>	<u>\$ 12,886,786</u>	<u>\$ 11,702,555</u>

Assets. As of June 30, 2008 the Foundation's total assets amounted to approximately \$9.7 million. Endowment investments represented the Foundation's largest asset, totaling approximately \$8.8 million or 90.7% of total assets. Cash and cash equivalents represented the Foundation's next largest asset, totaling approximately \$914,000 or 9.3% of total assets.

Total assets decreased by approximately \$3.2 million during the year ended June 30, 2008. Cash and cash equivalents decreased approximately \$2.0 million due to the funding of several endowments established by the Koller Gift and funding of a new building. Endowment investments decreased approximately \$1.2 million, primarily due to a decrease in market value.

Liabilities. At June 30, 2008, the Foundation had no liabilities.

Net Assets. Net assets at June 30, 2008 totaled \$9.7 million, or 100% of total assets, all of which were restricted net assets. Total net assets decreased by approximately \$3.2 million during the year ended June 30, 2008 in the category of expendable restricted net assets. The decrease was primarily due to an increase in grants to the University.

2007 Versus 2006. Total assets increased by approximately \$1.2 million when comparing fiscal 2007 with fiscal 2006. Endowment investments increased approximately \$1.1 million, primarily due to an increase in the market value.

Statements of Revenues, Expenses and Changes in Net Assets

	<u>2008</u>	<u>2007</u>	<u>2006</u>
OPERATING REVENUES			
Operating revenue (expense)	\$ (459,982)	\$ 1,701,951	\$ 7,703,334
Total operating revenues (expenses)	<u>(459,982)</u>	<u>1,701,951</u>	<u>7,703,334</u>
OPERATING EXPENSES			
Education and general	40,772	9,768	114,638
Grants to the University of Kentucky	2,705,617	507,952	5,640,291
Total operating expenses	<u>2,746,389</u>	<u>517,720</u>	<u>5,754,929</u>
OPERATING INCOME (LOSS)	(3,206,371)	1,184,231	1,948,405
Net assets, beginning of year	12,886,786	11,702,555	9,754,150
Net assets, end of year	<u>\$ 9,680,415</u>	<u>\$12,886,786</u>	<u>\$11,702,555</u>

Operating revenues included gifts of approximately \$222,000 and a loss on investments of approximately \$683,000. Operating revenues decreased \$2.2 million from the previous year because of a loss on endowment investments due to declining market conditions. The endowment pool posted a total loss of 8.2% for fiscal year 2008 versus a total return of 16.8% in the prior year.

Operating expenses totaled approximately \$2.7 million, increasing by approximately \$2.2 million due to an increase in grants to the University to complete the funding of three endowments established by the bequeathal of the Koller gift and to fund construction of a Bio-Isolation facility on Maine Chance Farm.

2007 Versus 2006. Operating revenue decreased by approximately \$6.0 million when comparing fiscal 2007 to fiscal 2006. This decrease was due primarily to a major estate gift of \$6.6 million received in fiscal 2006. Operating expenses decreased by approximately \$5.2 million when comparing fiscal 2007 to fiscal 2006. This decrease was primarily due to the transfer of a portion of the above-mentioned estate gift to the University's endowment fund for the benefit of the Maxwell H. Gluck Equine Research Center.

Statements of Cash Flows

Another way to assess the financial health of an organization is to look at the Statement of Cash Flows. The primary purpose of the Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the Foundation during the period. The Statement of Cash Flows also helps financial statement readers assess:

- the Foundation's ability to generate future net cash flows,
- the Foundation's ability to meet obligations as they become due, and
- the Foundation's need for external financing.

	<u>2008</u>	<u>2007</u>	<u>2006</u>
CASH PROVIDED (USED) BY:			
Operating activities	\$ (2,523,478)	\$ (395,966)	\$ 1,013,679
Investing activities	<u>486,919</u>	<u>537,818</u>	<u>469,949</u>
Net increase (decrease) in cash and cash equivalents	(2,036,559)	141,852	1,483,628
Cash and cash equivalents, beginning of year	<u>2,950,157</u>	<u>2,808,305</u>	<u>1,324,677</u>
Cash and cash equivalents, end of year	<u><u>\$ 913,598</u></u>	<u><u>\$ 2,950,157</u></u>	<u><u>\$ 2,808,305</u></u>

The largest cash receipt from operating activities relates to private gifts of approximately \$222,000. The most significant cash used in this category relates to grants to the University for non-capital purposes of approximately \$2.2 million and capital purposes of approximately \$495,000. The decrease in cash in the operating activities area was primarily a result of the above-mentioned grants to the University.

Cash provided by investing activities included \$17.2 million from the sale of investments, net of \$17.1 million used in the purchase of investments, and approximately \$330,000 from interest and dividends.

2007 Versus 2006. Cash flows fluctuated significantly in the area of operating activities when comparing 2007 versus 2006 as a result of the estate gift and the subsequent related transfer to the University.

Capital Asset and Debt Administration

Capital Assets. Capital assets purchased by the Foundation are granted to the University of Kentucky at the time of acquisition.

Debt. The Foundation had no debt at or during the year ended June 30, 2008.

Factors Impacting Future Periods

There are no known facts and circumstances that will affect future financial results.

UNIVERSITY OF KENTUCKY GLUCK EQUINE RESEARCH FOUNDATION, INC.
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF NET ASSETS
JUNE 30, 2008 AND 2007

	<u>2008</u>	<u>2007</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 913,598	\$ 2,950,157
Total current assets	<u>913,598</u>	<u>2,950,157</u>
Noncurrent Assets		
Endowment investments	8,766,817	9,936,629
Total noncurrent assets	<u>8,766,817</u>	<u>9,936,629</u>
Total assets	<u>9,680,415</u>	<u>12,886,786</u>
 LIABILITIES		
Current Liabilities		
Total current liabilities	<u>-</u>	<u>-</u>
Total liabilities	<u>-</u>	<u>-</u>
 NET ASSETS		
Restricted		
Nonexpendable	4,607,071	4,607,071
Expendable	<u>5,073,344</u>	<u>8,279,715</u>
Total restricted	<u>9,680,415</u>	<u>12,886,786</u>
Total net assets	<u>\$ 9,680,415</u>	<u>\$ 12,886,786</u>

See notes to financial statements.

**UNIVERSITY OF KENTUCKY GLUCK EQUINE RESEARCH FOUNDATION, INC.
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2008 AND 2007**

	<u>2008</u>	<u>2007</u>
OPERATING REVENUES		
Gifts	\$ 222,436	\$ 130,254
Investment income (loss)	(682,893)	1,571,697
Sales related to fundraising activities	475	-
Total operating revenues (expenses)	<u>(459,982)</u>	<u>1,701,951</u>
OPERATING EXPENSES		
Educational and general:		
Research	-	1,264
Institutional support	40,772	8,504
Total educational and general	<u>40,772</u>	<u>9,768</u>
Grants to (from) the University of Kentucky for non-capital purposes	2,210,917	507,952
Grants to (from) the University of Kentucky for capital purposes	494,700	-
Total operating expenses	<u>2,746,389</u>	<u>517,720</u>
Net income (loss) from operations	<u>(3,206,371)</u>	<u>1,184,231</u>
NET ASSETS, beginning of year	<u>12,886,786</u>	<u>11,702,555</u>
NET ASSETS, end of year	<u><u>\$ 9,680,415</u></u>	<u><u>\$ 12,886,786</u></u>

See notes to financial statements.

**UNIVERSITY OF KENTUCKY GLUCK EQUINE RESEARCH FOUNDATION, INC.
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2008 AND 2007**

	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Private gifts	\$ 222,436	\$ 130,254
Payments to vendors and contractors	(14,231)	(18,268)
Salaries, wages and benefits	(26,541)	-
Grants (to) from the University of Kentucky for non-capital purposes	(2,210,917)	(507,952)
Grants (to) from the University of Kentucky for capital purposes	(494,700)	-
Other receipts (payments)	475	-
Net cash provided (used) by operating activities	<u>(2,523,478)</u>	<u>(395,966)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	17,207,969	19,892,737
Interest and dividends on investments	330,221	381,998
Purchase of investments	<u>(17,051,271)</u>	<u>(19,736,917)</u>
Net cash provided (used) by investing activities	<u>486,919</u>	<u>537,818</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<u>(2,036,559)</u>	<u>141,852</u>
CASH AND CASH EQUIVALENTS, beginning of year	<u>2,950,157</u>	<u>2,808,305</u>
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 913,598</u>	<u>\$ 2,950,157</u>
Reconciliation of net income (loss) from operations to net cash provided (used) by operating activities:		
Net income (loss) from operations	\$(3,206,371)	\$ 1,184,231
Adjustments to reconcile net income (loss) from operations to net cash provided (used) by operating activities:		
Investment (income) loss	682,893	(1,571,697)
Change in assets and liabilities:		
Accounts payable and accrued liabilities	<u>-</u>	<u>(8,500)</u>
Net cash provided (used) by operating activities	<u><u>\$(2,523,478)</u></u>	<u><u>\$ (395,966)</u></u>

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The University of Kentucky Gluck Equine Research Foundation, Inc. (the Foundation) is a not-for-profit Kentucky corporation formed to establish a continuing partnership between the University of Kentucky (the University) and the equine industry of the Commonwealth of Kentucky (the Commonwealth). The Foundation's objective is to enhance and improve the equine research program at the University so that it will be one of the finest in the world. The Foundation is considered to be an affiliate and component unit of the University because all Board members are related to the University as faculty, staff or trustees and/or are appointed by the President of the University, and certain of the officers of the Foundation are officers of the University.

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 assets categories:

- Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- Restricted:
Nonexpendable – Net assets subject to externally imposed stipulations that they be maintained permanently by the Foundation. Such assets include the principal of the Foundation's permanent endowment funds.

Expendable – Net assets whose use by the Foundation is subject to externally imposed stipulations that can be fulfilled by actions of the Foundation pursuant to those stipulations or that expire by the passage of time.
- Unrestricted: Net assets whose use by the Foundation is not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Directors 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 Foundation's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Pursuant to GASB Statement No. 20, the Foundation has elected to apply the provisions for all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989 and do not conflict with or contradict GASB pronouncements.

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.

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

Cash and cash equivalents of the Foundation's endowment fund are included in noncurrent endowment investments.

Pooled Endowment Funds. The Foundation's endowment investments are administered as part of the University's pooled endowment funds. The University employs the total return concept of investment management for setting investment objectives and determining investment performance. This concept recognizes dividends and interest, plus or minus realized and unrealized gains or losses, in determining the total return earned during any particular period. 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.

The Uniform Management of Institutional Funds Act (UMIFA), as adopted by the Commonwealth of Kentucky, permits the University to appropriate an amount of the realized and unrealized endowment appreciation to support current programs. Accordingly, spendable return from the endowment is determined using the total return philosophy. This philosophy recognizes a prudent amount of realized and unrealized gains as spendable return in addition to traditional yield. Distribution of investment earnings for expenditure by participating funds is supported first by traditional yield earned and, if necessary, a transfer from the endowment of any prior years' accumulated earnings (unexpended traditional yield) or net realized or unrealized gains.

The University's endowment spending rule provides for annual distributions of 4.5 percent of the three-year moving average market value of fund units. For the years ended June 30, 2008 and 2007, approximately \$110,000 and \$109,000, respectively, was transferred from endowment realized and unrealized gains to support current programs in accordance with the University's endowment spending rule. Appreciation on endowments available to support future spending rule distributions amounted to approximately \$4.5 million at June 30, 2008. Additionally, the University assesses eligible endowment accounts with a management fee of 0.5 percent of total asset value to support fundraising and endowment administration.

Investments. Investments in marketable securities are carried at fair value, as determined by the major securities markets. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the Statement of Revenues, Expenses and Changes in Net Assets.

Income Taxes. The Foundation has been granted exemption from federal income taxation pursuant to the provisions of Internal Revenue Code section 501(c)(3).

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

Operating Activities. The Foundation defines operating activities, as reported on the Statement of Revenues, Expenses and Changes in Net Assets, 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. Gifts and endowment and investment income are also classified as operating revenues because fundraising activities represent the Foundation's primary operating purpose.

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

2. DEPOSITS AND INVESTMENTS

The fair value of deposits and investments, by type, at June 30, 2008 and 2007 is as follows:

	<u>2008</u>	<u>2007</u>
Cash on deposit with the University of Kentucky	\$ 913,598	\$ 2,950,157
Investment in University of Kentucky pooled endowment fund	<u>8,766,817</u>	<u>9,936,629</u>
Total	<u>\$ 9,680,415</u>	<u>\$ 12,886,786</u>

At June 30, 2008, the University's pooled endowment fund consists of pooled equity funds (66.0%), private equity funds (1.7%), pooled real estate funds (9.0%), government agency fixed income funds (5.8%), corporate fixed income funds (5.9%), pooled fixed income funds (10.8%) and cash equivalents (0.8%).

Deposit and investment policies. The Foundation follows the deposit and investment policies established by the University of Kentucky's Board of Trustees. Such policies are developed to establish and maintain sound financial management practices for the investment and management of the Foundation's funds.

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

- Cash on deposit with the University of Kentucky, which the University invests in deposits and repurchase agreements with local banks and the Commonwealth of Kentucky, and
- Endowment investments in the University's pooled endowment fund.

Cash on deposit with the University is managed based on the University's Overnight and Short-Term Investment Policy approved by the Investment Committee of the University's Board of Trustees.

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

Deposit and investment risks. The Foundation's deposits and investments are exposed to various risks, including credit, interest rate and foreign currency risk, as discussed in more detail below:

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligation, causing the Foundation 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 on deposit with the University of Kentucky is governed by policy that minimizes risk in several ways. Deposits are governed by state law which requires full collateralization. Credit risk on repurchase agreements with local banks is mitigated by requiring the issuing financial institution's pledge of specific U.S. treasury or agency securities, held in the name of the University by the Federal Reserve Bank. Credit risk on repurchase agreements with the Commonwealth of Kentucky is mitigated by the Commonwealth's requirement that providers of overnight repurchase agreements collateralize these investments at 102% of face value with U.S. treasury or agency securities, pledged in the name of the Commonwealth.
- Endowment investments held by the University's fixed income managers are generally limited to holdings of high quality fixed income securities. These managers may invest a portion of the portfolio in other below-investment grade bonds, non-U.S. dollar denominated bonds, and emerging market bonds, provided the overall credit quality of the fixed income portfolios is not lower than A-.

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

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

- Cash on deposit with the University is invested in deposits and repurchase agreements with local banks, which are held in the University's name, and deposits and repurchase agreements with the Commonwealth of Kentucky, which are held in the Commonwealth's name. The University maintains records evidencing the Foundation'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 Foundation's ownership interest (units) in the University's pooled endowment fund.

Concentrations of Credit Risk. The Foundation'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 on deposit with the University is not limited as to the maximum amount that may be invested in one issuer. However, all such investments in excess of Federal Depository Insurance are required to be fully collateralized by U.S. treasury and/or U.S. agency securities or other similar investments as provided by KRS 41.240.
- The University's endowment investment managers are limited to a maximum investment in any one issuer of no more than 5% of total investments.

At June 30, 2008, the Foundation had no underlying investments in any one issuer which represent more than 5% of total investments.

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

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

- Cash on deposit with the University has limited exposure to interest rate risk due to the short term nature of the investment. The University requires that all deposits and repurchase agreements be available for use on the next business day.
- Endowment investments held by the University's fixed income managers are limited to a duration that is within +/-25% of the duration of the Lehman Aggregate Bond Index.

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

The Foundation's exposure to foreign currency risk derives from certain limited endowment investments of the University's pooled endowment fund, including pooled fixed income funds, a pooled global equity fund, and a pooled non-U.S. equity fund. The University's endowment investment policy allows fixed-income managers to invest a portion of their funds in non-U.S. securities and equity fund managers of co-mingled portfolios to invest in accordance with the guidelines established in the individual fund's prospectus.

3. INVESTMENT INCOME

Components of investment income for the years ended June 30, 2008 and 2007 are as follows:

	<u>2008</u>	<u>2007</u>
Interest and dividends earned on endowment investments	\$ 257,998	\$ 230,535
Realized and unrealized gains and losses on endowment investments	(1,013,114)	1,189,699
Interest on cash and non-endowment investments	<u>72,223</u>	<u>151,463</u>
Total	<u>\$ (682,893)</u>	<u>\$ 1,571,697</u>

4. RISK MANAGEMENT

The Foundation is exposed to various risks of loss related to torts and errors and omissions. These risks are covered by extension of coverage by the University's participation in an insurance risk retention group and self-insurance. Claims against directors and officers for wrongful acts (errors and omissions) are insured through a risk retention group. There have been no significant reductions in insurance coverage from 2007 to 2008. Settlements have not exceeded insurance coverage during the past three years.

5. TRANSACTIONS WITH THE UNIVERSITY OF KENTUCKY

Grants to the University of Kentucky are for the purposes of equine research and in support of the Gluck Equine Research Center.

6. RECLASSIFICATIONS

Certain reclassifications to fiscal 2007 comparative amounts have been made to conform to the 2008 classifications. Certain transactions previously reported on the Statement of Net Assets as restricted nonexpendable have been reclassified as restricted expendable. Such reclassifications had no effect on the change in net assets.

BOARD OF DIRECTORS

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