



UNIVERSITY OF  
**KENTUCKY**<sup>®</sup>

**The Fund for Advancement of Education and Research  
in the University of Kentucky Medical Center  
2009 Financial Statements**

**The Fund for Advancement of  
Education and Research in the  
University of Kentucky Medical Center  
A Component Unit of the University of Kentucky**

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## Independent Accountants' Report on Financial Statements and Supplementary Information

Board of Directors  
The Fund for Advancement of  
Education and Research in the  
University of Kentucky Medical Center  
Lexington, Kentucky

We have audited the accompanying basic financial statements of The Fund for Advancement of Education and Research in the University of Kentucky Medical Center (Fund), a not-for-profit corporation affiliated with and a component unit of the University of Kentucky, as of and for the years ended June 30, 2009 and 2008, as listed in the table of contents. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 audits provide a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Fund as of June 30, 2009 and 2008, and the changes in its financial position and its cash flows for the years 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 supplementary information and express no opinion on it.

*BKD, LLP*

October 1, 2009

# Management Discussion and Analysis

The Fund for Advancement of Education and Research in the University of Kentucky Medical Center's (The Fund) Management Discussion and Analysis (MD&A) of its financial condition provides an overview of the financial performance of The Fund for the years ended June 30, 2009 and 2008. 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

- Total assets decreased \$1.1 million or 6.7%, primarily due to decreases in cash and cash equivalents and accounts receivable.
- Total liabilities increased \$203,000 or 15.5%, primarily due to an increase in accounts payable.
- The decrease in total net assets of \$1.3 million, or 8.6%, was primarily in restricted net assets, due to operating expenses and grants to the University in excess of revenues.
- Operating revenues decreased \$1.4 million or 9% to \$14.2 million, largely due to decreases in dental professional fees of \$1.5 million or 13.9%.
- Operating expenses increased \$1.1 million or 20.4% to \$6.2 million.
- Net assets represented 90.2% 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 Fund's finances is whether The Fund is better off as a result of the year's activities. One key to answering this question is the financial statements of The Fund. 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 Fund in a format similar to that used by corporations, and present a long-term view of The Fund's finances. The Fund's net assets (the difference between assets and liabilities) are one sign of The Fund's financial health. Over time, increases or decreases in net assets indicate the improvement or erosion of The Fund's financial health, when considered in conjunction with non-financial facts.

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. GASB 35 requires gifts and endowment and investment income to be classified as nonoperating revenues.

Another important factor to consider when evaluating financial viability is The Fund'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 Fund is a not-for-profit Kentucky corporation established to promote, advance and support the educational, research, charitable and other purposes of the University of Kentucky Medical Center. The Fund is considered to be an affiliate and component unit of the University of Kentucky (the University) because all Board members are related to the University as faculty, staff or trustees and/or are appointed by the Board of Trustees of the University, and certain officers of The Fund are officers of the University.

### Condensed Financial Information

#### Statements of Net Assets

	2009	2008	2007
<b>ASSETS</b>			
Current assets	\$ 15,160,347	\$ 16,209,161	\$ 14,662,426
Noncurrent assets	173,501	227,501	251,572
Total assets	<u>15,333,848</u>	<u>16,436,662</u>	<u>14,913,998</u>
<b>LIABILITIES</b>			
Current liabilities	1,510,915	1,307,931	1,440,404
Total liabilities	<u>1,510,915</u>	<u>1,307,931</u>	<u>1,440,404</u>
<b>NET ASSETS</b>			
Restricted			
Nonexpendable	30,642	30,642	30,642
Expendable	826,797	1,800,652	1,787,095
Unrestricted	12,965,494	13,297,437	11,655,857
Total net assets	<u>\$ 13,822,933</u>	<u>\$ 15,128,731</u>	<u>\$ 13,473,594</u>

**Assets.** As of June 30, 2009, The Fund's assets totaled \$15.3 million. Cash and cash equivalents, totaling \$12.1 million or 79.1% of total assets, represented The Fund's most significant asset. Accounts receivable (primarily for dental services), net of allowances, totaled \$3.0 million or 19.6% of total assets and was The Fund's second largest asset.

Total assets decreased \$1.1 million or 6.7% during the year ended June 30, 2009. This decrease was driven by decreases in cash and cash equivalents of \$671,000 and in accounts receivable, net of allowances, of \$378,000.

**Liabilities.** At June 30, 2009, The Fund's liabilities totaled \$1.5 million. Accounts payable and accrued liabilities of \$773,000 represented 51.5% of total liabilities. Amounts due to the University for faculty salary supplements of \$738,000 comprised the remainder of The Fund's liabilities.

Total liabilities increased \$203,000 or 15.5% during the year ended June 30, 2009. This increase was primarily in accounts payable due to timing of payments to vendors.

**Net Assets.** Net assets at June 30, 2009, totaled \$13.8 million, or 90.2% of total assets. Restricted net assets totaled \$857,000 or 6.2% of total net assets and unrestricted net assets accounted for \$13.0 million or 93.8% of total net assets.

Total net assets decreased \$1.3 million or 8.6% during the year ended June 30, 2009 primarily as a result of a decrease in restricted net assets, due to operating expenses and grants to the University in excess of revenues.

**2008 Versus 2007.** During the year ended June 30, 2008:

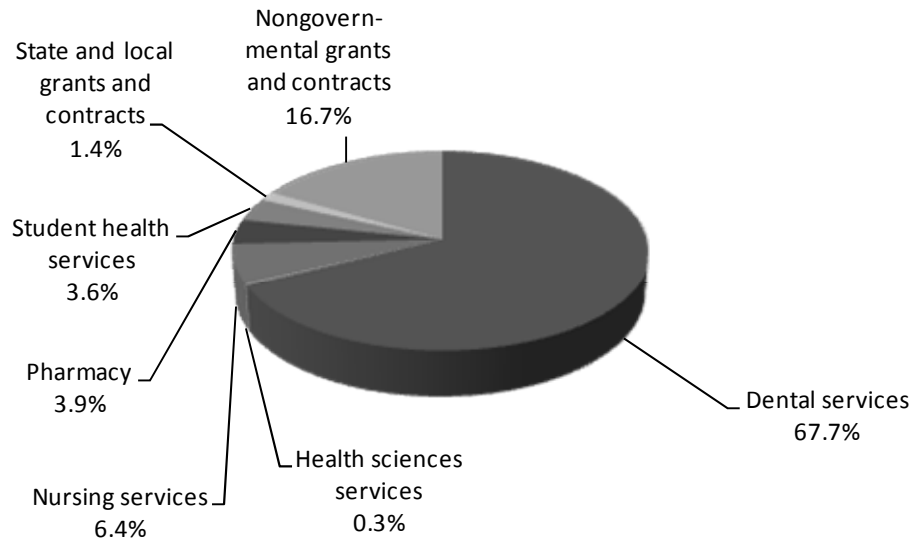
- Total assets increased \$1.5 million or 10.2%. This increase was driven by increases in cash and cash equivalents of \$1.3 million and in accounts receivable, net of allowances, of \$264,000.
- Total liabilities decreased \$132,000 or 9.2%, due primarily to a decrease in accounts payable and accrued liabilities of \$129,000.
- Total net assets increased \$1.7 million or 12.3%, primarily due to an increase in unrestricted net assets of \$1.6 million caused by operating revenues in excess of expenses.

**Statements of Revenues, Expenses and Changes in Net Assets**

	2009	2008	2007
<b>OPERATING REVENUES</b>			
Professional service fees, net of allowances			
Dental services	\$ 9,589,649	\$ 11,135,044	\$ 10,066,416
Health sciences services	37,138	42,104	40,942
Nursing services	904,085	718,083	640,059
Pharmacy	556,023	583,771	655,202
Student health services	515,638	465,863	437,484
Total professional service fees	<u>11,602,533</u>	<u>12,944,865</u>	<u>11,840,103</u>
State and local grants and contracts	205,058	36,445	9,577
Nongovernmental grants and contracts	2,366,205	2,597,144	2,289,294
Other operating revenue	7,838	7,540	106,558
Total operating revenues	<u>14,181,634</u>	<u>15,585,994</u>	<u>14,245,532</u>
<b>OPERATING EXPENSES</b>			
Educational and general	<u>6,231,616</u>	<u>5,177,156</u>	<u>5,505,493</u>
Total operating expenses	<u>6,231,616</u>	<u>5,177,156</u>	<u>5,505,493</u>
<b>NET INCOME FROM OPERATIONS</b>	<u>7,950,018</u>	<u>10,408,838</u>	<u>8,740,039</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>			
Gifts and grants	231,373	506,694	1,007,640
Investment income	70,678	465,996	610,501
Grants to the University of Kentucky	<u>(9,557,867)</u>	<u>(9,726,391)</u>	<u>(8,710,953)</u>
Total nonoperating revenues (expenses)	<u>(9,255,816)</u>	<u>(8,753,701)</u>	<u>(7,092,812)</u>
Total increase in net assets	(1,305,798)	1,655,137	1,647,227
<b>Net assets, beginning of year</b>	<u>15,128,731</u>	<u>13,473,594</u>	<u>11,826,367</u>
<b>Net assets, end of year</b>	<u>\$ 13,822,933</u>	<u>\$ 15,128,731</u>	<u>\$ 13,473,594</u>

**2009.** Total operating revenues were \$14.2 million for the year ended June 30, 2009. The most significant source of operating revenues for The Fund was professional service fees, primarily dental, of \$11.6 million or 81.7% of the total. Operating revenues decreased \$1.4 million or 9%, due principally to a decrease in dental professional service fees of \$1.5 million resulting from a decline in patient services.

## TOTAL OPERATING REVENUES



Operating expenses totaled \$6.2 million. This entire amount was used for educational and general expenses related to functions such as academic support, instruction, research, institutional support and public services. Operating expenses increased \$1.1 million or 20.4% due primarily to the payment by The Fund of dental clinics expenses that were charged to the University in the prior fiscal year.

**2008 Versus 2007.** During the year ended June 30, 2008:

- Total operating revenues were \$15.6 million. The most significant source of operating revenues for The Fund was professional service fees of \$12.9 million or 82.7% of total operating revenues. Operating revenues increased \$1.3 million or 9.4% due primarily to increases in dental service revenues as a result of improved billing software, increases in patient volume and dental service fee increases.
- Operating expenses totaled \$5.2 million. This entire amount was used for educational and general expenses related to functions such as academic support, instruction, hospitals and clinics, institutional support and public service. Operating expenses decreased \$328,000 or 5.9% due primarily to decreases in expenses in the hospitals and clinics category related to fundraising activities.

### 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 Fund during the period. The Statement of Cash Flows also helps financial statement readers assess The Fund's:

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

	2009	2008	2007
<b>CASH PROVIDED (USED) BY:</b>			
Operating activities	\$ 8,560,866	\$ 10,017,269	\$ 8,720,963
Noncapital financing activities	(8,914,712)	(8,168,028)	(7,278,941)
Capital and related financing activities	(438,611)	(1,062,494)	(346,622)
Investing activities	121,836	495,613	582,444
	<u>(670,621)</u>	<u>1,282,360</u>	<u>1,677,844</u>
<b>Cash and cash equivalents, beginning of year</b>	12,815,158	11,532,798	9,854,954
<b>Cash and cash equivalents, end of year</b>	<u>\$ 12,144,537</u>	<u>\$ 12,815,158</u>	<u>\$ 11,532,798</u>

**2009.** The major source of funds included in operating activities was professional service fees of \$12.1 million. The largest cash payments for operating activities were made to suppliers of \$5.1 million.

Cash used in the noncapital financing activities group consisted of \$9.2 million in grants to the University of Kentucky offset by receipt of private gifts and grants of \$236,000.

Cash used by capital and related financing activities was related to grants of capital assets to the University.

Cash provided by investing activities included \$296,000 from the sale of investments and interest and dividend income of \$122,000, net of \$296,000 expended on the purchase of investments.

**2008 Versus 2007.** From June 30, 2007 to June 30, 2008 cash increased \$1.3 million primarily due to increased operating revenue from professional service fees.

### **Capital Asset and Debt Administration**

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

**Debt.** The Fund had no debt at or during the year ended June 30, 2009.

### **Factors Impacting Future Periods**

Due to the current economic conditions Dentistry has experienced a decline in patient services; this trend is expected to continue in FY 2010. Dental service fees will not be increased in FY 2010. It is projected that the general decline in patient services and the freeze on fees will be offset by outreach efforts in Western Kentucky that are expected to generate \$800,000 in additional revenues.



THE FUND FOR ADVANCEMENT OF EDUCATION AND RESEARCH  
 IN THE UNIVERSITY OF KENTUCKY MEDICAL CENTER  
 A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY  
 STATEMENTS OF NET ASSETS  
 JUNE 30, 2009 AND 2008

	<u>2009</u>	<u>2008</u>
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 12,144,537	\$ 12,815,158
Accounts receivable, net	3,015,810	3,394,003
Total current assets	<u>15,160,347</u>	<u>16,209,161</u>
<b>Noncurrent Assets</b>		
Endowment investments	170,798	221,956
Accounts receivable, net	2,703	5,545
Total noncurrent assets	<u>173,501</u>	<u>227,501</u>
Total assets	<u>15,333,848</u>	<u>16,436,662</u>
<b>LIABILITIES</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued liabilities	773,066	538,709
Due to the University of Kentucky	737,849	769,222
Total current liabilities	<u>1,510,915</u>	<u>1,307,931</u>
Total liabilities	<u>1,510,915</u>	<u>1,307,931</u>
<b>NET ASSETS</b>		
<b>Restricted</b>		
Nonexpendable	30,642	30,642
Expendable	826,797	1,800,652
Total restricted	<u>857,439</u>	<u>1,831,294</u>
<b>Unrestricted</b>	<u>12,965,494</u>	<u>13,297,437</u>
Total net assets	<u>\$ 13,822,933</u>	<u>\$ 15,128,731</u>

See notes to financial statements.

**THE FUND FOR ADVANCEMENT OF EDUCATION AND RESEARCH  
 IN THE UNIVERSITY OF KENTUCKY MEDICAL CENTER  
 A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY  
 STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS  
 FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
<b>OPERATING REVENUE</b>		
Professional service fees, net of allowances:		
Dental services	\$ 9,589,649	\$ 11,135,044
Health sciences services	37,138	42,104
Nursing services	904,085	718,083
Pharmacy	556,023	583,771
Student health services	515,638	465,863
Total professional service fees	<u>11,602,533</u>	<u>12,944,865</u>
State and local grants and contracts	205,058	36,445
Nongovernmental grants and contracts	2,366,205	2,597,144
Other operating revenues	7,838	7,540
Total operating revenues	<u>14,181,634</u>	<u>15,585,994</u>
<b>OPERATING EXPENSES</b>		
Educational and general:		
Instruction	574,203	575,280
Research	433,826	397,822
Public service	972,690	537,690
Libraries	3,498	3,503
Academic support	3,430,333	3,008,718
Student services	68,397	73,737
Institutional support	317,128	305,082
Student financial aid	322,682	193,325
Hospital and clinics	108,859	81,999
Total operating expenses	<u>6,231,616</u>	<u>5,177,156</u>
Net income (loss) from operations	<u>7,950,018</u>	<u>10,408,838</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Gifts and grants	231,373	506,694
Investment income	70,678	465,996
Grants to the University of Kentucky for non-capital purposes	(9,119,256)	(8,663,897)
Net nonoperating revenues (expenses)	<u>(8,817,205)</u>	<u>(7,691,207)</u>
Net income (loss) before other revenues, expenses, gains, or losses	<u>(867,187)</u>	<u>2,717,631</u>
Grants to the University of Kentucky for capital purposes	(438,611)	(1,062,494)
Total other revenues (expenses)	<u>(438,611)</u>	<u>(1,062,494)</u>
Increase (decrease) in net assets	(1,305,798)	1,655,137
<b>NET ASSETS, beginning of year</b>	<u>15,128,731</u>	<u>13,473,594</u>
<b>NET ASSETS, end of year</b>	<u>\$ 13,822,933</u>	<u>\$ 15,128,731</u>

See notes to financial statements.

**THE FUND FOR ADVANCEMENT OF EDUCATION AND RESEARCH  
 IN THE UNIVERSITY OF KENTUCKY MEDICAL CENTER  
 A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY  
 STATEMENTS OF CASH FLOWS  
 FOR THE YEARS ENDED JUNE 30, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Professional service fees	\$ 12,089,820	\$ 12,801,844
Payments to vendors and contractors	(5,148,151)	(4,553,617)
Student financial aid	(322,682)	(193,325)
Salary, wage and benefit reimbursements to the University of Kentucky	(619,848)	(595,228)
Grants and contracts	2,553,889	2,550,055
Other receipts (payments)	7,838	7,540
Net cash provided (used) by operating activities	<u>8,560,866</u>	<u>10,017,269</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
Private gifts and grants received for other than capital purposes	235,917	499,634
Grants (to) from the University of Kentucky	(9,150,629)	(8,667,662)
Net cash provided (used) by noncapital financing activities	<u>(8,914,712)</u>	<u>(8,168,028)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Grants (to) from the University of Kentucky for capital purposes	(438,611)	(1,062,494)
Net cash provided (used) by capital and related financing activities	<u>(438,611)</u>	<u>(1,062,494)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sales and maturities of investments	296,492	435,666
Interest and dividends on investments	121,836	491,646
Purchase of investments	(296,492)	(431,699)
Net cash provided (used) by investing activities	<u>121,836</u>	<u>495,613</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<u>(670,621)</u>	<u>1,282,360</u>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<u>12,815,158</u>	<u>11,532,798</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<u>\$ 12,144,537</u>	<u>\$ 12,815,158</u>
<b>Reconciliation of net income (loss) from operations to net cash provided (used) by operating activities:</b>		
Net income (loss) from operations	\$ 7,950,018	\$ 10,408,838
Adjustments to reconcile net income (loss) from operations to net cash provided (used) by operating activities:		
Change in assets and liabilities:		
Accounts receivable, net	376,491	(262,861)
Accounts payable and accrued liabilities	<u>234,357</u>	<u>(128,708)</u>
<b>Net cash provided (used) by operating activities</b>	<u>\$ 8,560,866</u>	<u>\$ 10,017,269</u>

See notes to financial statements.

## NOTES TO FINANCIAL STATEMENTS

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

#### Reporting Entity

The Fund for Advancement of Education and Research in the University of Kentucky Medical Center (The Fund) is a not-for-profit Kentucky corporation established to promote, advance and support the educational, research, charitable and other purposes of the University of Kentucky Medical Center (Medical Center). The Fund is considered to be an affiliate and component unit of the University of Kentucky (the University) because all Board members are related to the University as faculty, staff or trustees and/or are appointed by the Board of Trustees of the University, and certain officers of The Fund are officers of the University.

The Fund's mission is carried out through various means, including the operation of clinical practice plans and fundraising for several of the University's medical center programs.

#### 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 Fund. Such assets include the principal of The Fund's permanent endowment funds.
  - Expendable* – Net assets whose use by The Fund is subject to externally imposed stipulations that can be fulfilled by actions of The Fund pursuant to those stipulations or that expire by the passage of time.
- Unrestricted: Net assets whose use by The Fund 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 required by GASB Statement No. 35 is intended to provide a comprehensive, entity-wide perspective of The Fund's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Pursuant to GASB Statement No. 20, The Fund 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. The Fund reports as a Business Type Activity (BTA) as defined by GASB Statement No. 35. BTAs are those activities that are financed in whole or part by fees charged to external parties for goods and services.

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

Accounts Receivable. This classification consists of patient accounts receivable and pledges that are verifiable, measurable and expected to be collected. Accounts receivable are recorded net of estimated uncollectible amounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Pooled Endowment Funds. The Fund'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 each of the years ended June 30, 2009 and 2008 approximately \$4,500 and \$2,800, 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 \$111,000 at June 30, 2009. The University assesses eligible endowment accounts with a management fee of 0.5 percent of total asset value.

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.

Professional Service Fees. Professional service fees are reported at net realizable amounts from patients, third-party payors and others for services rendered. Services covered by Medicare are reimbursed in accordance with the applicable published fee schedules from the Centers for Medicare and Medicaid Services while services rendered to Medicaid program beneficiaries are reimbursed according to a predetermined fee schedule provided by the Cabinet for Health and Family Services Department of Medicaid Services.

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

Nongovernmental Grants and Contracts. The University and Kentucky Medical Services Foundation, Inc. (KMSF) (an entity with which the University's faculty in its College of Medicine has "Practice Agreements and Assignments") have an agreement whereby The Fund receives two percent of clinical income collected by KMSF to be used for academic enrichment of the College of Medicine. This revenue is classified as an operating activity in nongovernmental grants and contracts due to its contractual nature.

Grants to the University of Kentucky. Grants to the University are primarily for general program support and supplemental compensation of Medical Center health professionals. Other grants consist of capital assets purchased by The Fund that are granted to the University at the time of acquisition and endowment management fees.

Income Taxes. The Fund 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 Fund'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 Fund 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 services and goods received. Nearly all of The Fund's revenues are from exchange transactions. Certain significant expenditures, such as grants to the University, are recorded as non-operating expenses, 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 use estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The accompanying financial statements include estimates for items such as bad debt allowances.

## 2. DEPOSITS AND INVESTMENTS

The fair value of deposits and investments, by type, at June 30, 2009 and 2008 is as follows:

	2009	2008
Cash on deposit with the University of Kentucky	\$ 12,144,537	\$ 12,815,158
Investment in University of Kentucky pooled endowment fund	170,798	221,956
Total	<u>\$ 12,315,335</u>	<u>\$ 13,037,114</u>

At June 30, 2009, the University's pooled endowment fund consists of pooled equity funds (61.2%), pooled private equity funds (2.7%), pooled absolute return funds (2.2%), pooled real return funds (3.2%), pooled real estate funds (8.3%), U.S. Treasury fixed income (1.8%), government agency fixed income funds (0.2%), corporate fixed income funds (7.9%), pooled fixed income funds (9.9%) and cash equivalents (2.6%).

**Deposit and investment policies.** The Fund 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 Fund's balances.

For purposes of investment management, The Fund'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 Fund'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 Fund 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 (the Commonwealth) is mitigated by the Commonwealth's requirement that providers of overnight repurchase agreements collateralize these investments at 102% of face value with U.S. treasury or agency securities, pledged in the name of the Commonwealth.
- 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 Fund 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 Fund'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 Fund's ownership interest (units) in the University's pooled endowment fund.

**Concentrations of Credit Risk.** The Fund'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 fixed income managers are limited to a maximum investment in any one issuer of no more than 5% of total investments.

At June 30, 2009, The Fund 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 Fund'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. ACCOUNTS RECEIVABLE

Accounts receivable as of June 30, 2009 and 2008 are as follows:

	2009		
	Gross Receivable	Allowance	Net Receivable
Dental patient accounts	\$ 3,716,187	\$(1,176,517)	\$ 2,539,670
University health service patient accounts	158,498	-	158,498
Pledges receivable, discounted	4,187	-	4,187
Other receivables, primarily KMSF	316,159	-	316,159
Total	<u>\$ 4,195,031</u>	<u>\$(1,176,517)</u>	<u>\$ 3,018,513</u>
Current portion			\$ 3,015,810
Noncurrent portion			<u>2,703</u>
Total			<u>\$ 3,018,513</u>
	2008		
	Gross Receivable	Allowance	Net Receivable
Dental patient accounts	\$ 4,304,724	\$(1,227,453)	\$ 3,077,271
University health service patient accounts	95,748	-	95,748
Pledges receivable, discounted	8,729	-	8,729
Other receivables, primarily KMSF	217,800	-	217,800
Total	<u>\$ 4,627,001</u>	<u>\$(1,227,453)</u>	<u>\$ 3,399,548</u>
Current portion			\$ 3,394,003
Noncurrent			<u>5,545</u>
Total			<u>\$ 3,399,548</u>



#### 4. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
Payable to vendors and contractors - operating	\$ 354,680	\$ 210,402
Credit balances on patient accounts	417,147	321,286
Due to the University of Kentucky accrued payroll	1,239	7,021
Total	<u>\$ 773,066</u>	<u>\$ 538,709</u>

#### 5. DESIGNATIONS OF UNRESTRICTED NET ASSETS

The Fund's management and/or Board of Directors designates unrestricted net assets for specific purposes, as follows:

	<u>2009</u>	<u>2008</u>
Working capital needs	\$ 3,018,513	\$ 3,399,548
Budget appropriations for operating purposes for the upcoming fiscal year	2,992,900	3,588,800
Available for future operating purposes	6,954,081	6,309,089
Total	<u>\$ 12,965,494</u>	<u>\$ 13,297,437</u>

#### 6. INVESTMENT INCOME

Components of investment income for the years ended June 30, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
Interest and dividends earned on endowment investments	\$ 5,454	\$ 6,532
Realized and unrealized gains and losses on endowment investments	(51,158)	(25,650)
Interest on cash and non-endowment investments	116,382	485,114
Total	<u>\$ 70,678</u>	<u>\$ 465,996</u>

#### 7. PLEDGES AND DEFERRED GIFTS

Operating pledges totaling approximately \$6,200 are expected to be collected over the next five years. In accordance with GASB Statement No. 33, "Accounting and Financial Reporting for Nonexchange Transactions," The Fund is required to record operating pledges as revenue when all eligibility requirements have been met. Accordingly, at June 30, 2009, The Fund recorded the discounted value of operating pledges receivable using a rate of 5 percent, net of allowance for uncollectible pledges, of approximately \$1,400.

#### 8. RISK MANAGEMENT

The Fund 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 2008 to 2009. Settlements have not exceeded insurance coverage during the past three years.

## **9. TRANSACTIONS WITH THE UNIVERSITY OF KENTUCKY**

All salary, wage and benefit reimbursements to the University represent charges for University employees.

## **10. CURRENT ECONOMIC CONDITIONS**

The current economic conditions present not-for-profit organizations with unprecedented circumstances and challenges, which have lead to large declines in fair value of investments and donations. The rising unemployment rate have made it difficult for certain of The Fund's patients to pay for services rendered. As employers make adjustments to health insurance plans or more patients become unemployed, services provided to self-pay and other payers may significantly impact net revenues from professional service fees, which could have adverse impact on The Fund's future operating results. The financial statements have been prepared using values and information currently available to The Fund.

## BOARD OF DIRECTORS

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Kumble Subbaswamy  
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## OFFICERS

Kumble Subbaswamy, Chair  
Sharon Turner, Secretary



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