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UNIVERSITY OF KENTUCKY

2011

Athletic Association Financial Statements

University of Kentucky
Athletic Association
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
Athletic Association
Lexington, Kentucky

We have audited the accompanying basic financial statements of the University of Kentucky Athletic Association (Association), 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, 2011 and 2010, as listed in the table of contents. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 financial statements referred to above present fairly, in all material respects, the financial position of the Association as of June 30, 2011 and 2010, 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

September 29, 2011

Management's Discussion and Analysis

The University of Kentucky Athletic Association's (the Association) Management's Discussion and Analysis (MD&A) of its financial condition provides an overview of the financial performance of the Association for the years ended June 30, 2011 and 2010. 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 2010-2011 report a solid financial condition at June 30, 2011. Financial operations were in accordance with the revenue expectations and the approved budget plan.
- Total assets decreased $2.0 million or 6.4%. The most significant component of the fluctuation was a $2.2 million decrease in cash and cash equivalents.
- Total liabilities decreased $698,000 or 4.0%. Deferred revenue decreased $504,000 and accounts payable and accrued liabilities decreased $416,000, offset by an increase of $230,000 in long term liabilities.
- Unrestricted net assets decreased $1.2 million or 10.8% caused by operating expenses and grants to the University in excess of operating and nonoperating revenues.
- Operating revenues increased $2.9 million to $66.5 million.
- Operating expenses decreased $1.2 million to $66.4 million.
- Net nonoperating revenues/expenses increased $9.0 million, primarily due to a $11.5 million increase in grants to the University for capital purposes, offset by a $1.7 million increase in grants from the University for noncapital purposes.

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 Association's finances is whether the Association is better off as a result of the year's activities. One key to answering this question is the financial statements of the Association. 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 Association in a format similar to that used by corporations and present a long-term view of the Association's finances. The Association's net assets (the difference between assets and liabilities) are one sign of the Association's financial health. Over time, increases or decreases in net assets indicate the improvement or erosion of the Association's condition, when considered in conjunction with non-financial factors such as the graduation rates of its student athletes and the success of its athletic teams on the field.

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. The utilization of long-lived assets, referred to as capital assets, is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

Another important factor to consider when evaluating financial viability is the Association'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 Athletic Association is a not-for-profit Kentucky corporation, established to promote athletics and physical culture for students at the University of Kentucky (the University) and residents of the Commonwealth of Kentucky. The Association 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 alumni and/or are appointed by the President of the University, and certain officers of the Association are officers of the University.

Condensed Financial Information

Statements of Net Assets

	2011	2010	2009
ASSETS			
Current assets	$ 26,909,396	$ 28,822,817	$ 23,644,731
Capital assets	1,810,659	1,917,862	1,854,524
Other noncurrent assets	289,509	249,342	237,911
Total assets	29,009,564	30,990,021	25,737,166
LIABILITIES			
Current liabilities	15,994,940	16,923,615	15,980,849
Noncurrent liabilities	872,299	641,858	-
Total liabilities	16,867,239	17,565,473	15,980,849
NET ASSETS			
Invested in capital assets, net of related debt	1,810,659	1,917,862	1,854,524
Restricted			
Expendable	337,791	305,927	289,661
Unrestricted	9,993,875	11,200,759	7,612,132
Total net assets	$ 12,142,325	$ 13,424,548	$ 9,756,317

Assets. As of June 30, 2011, the Association's assets totaled $29.0 million. Cash and cash equivalents represented the Association's largest asset, totaling $22.8 million or 78.6% of total assets. Inventories and other assets totaled $3.8 million or 13.1%.

Total assets decreased $2.0 million or 6.4% primarily due to a $2.2 million decrease in cash and cash equivalents resulting from operating expenses and grants to the University exceeding operating and nonoperating revenues.

Liabilities. At June 30, 2011, the Association's liabilities totaled $16.9 million. Deferred revenue, primarily comprised of advance sales of football tickets and reserved parking, totaled $13.8 million and represented 81.7% of total liabilities.

Total liabilities decreased $698,000 during the year ended June 30, 2011. Deferred revenue decreased $504,000 due to lower advance sales of football tickets and reserved parking caused by a delay in offering student tickets for sale and fewer season ticket sales. Long term liabilities increased $230,000 due to an increase in the liability for coach longevity and retention bonuses due to a contract amendment for the men's basketball head coach.

Net Assets. Net assets at June 30, 2011, totaled $12.1 million, or 41.9% of total assets. Invested in capital assets, net of related debt, totaled $1.8 million or 14.9% of total net assets. Restricted net assets totaled $338,000 or 2.8% of total net assets. Unrestricted net assets accounted for $10.0 million or 82.3% of total net assets.

Total net assets decreased $1.3 million during the year ended June 30, 2011, primarily because of a decrease of $1.2 million in unrestricted net assets caused by operating expenses and grants to the University in excess of operating and nonoperating revenues.

2010 Versus 2009. During the year ended June 30, 2010:

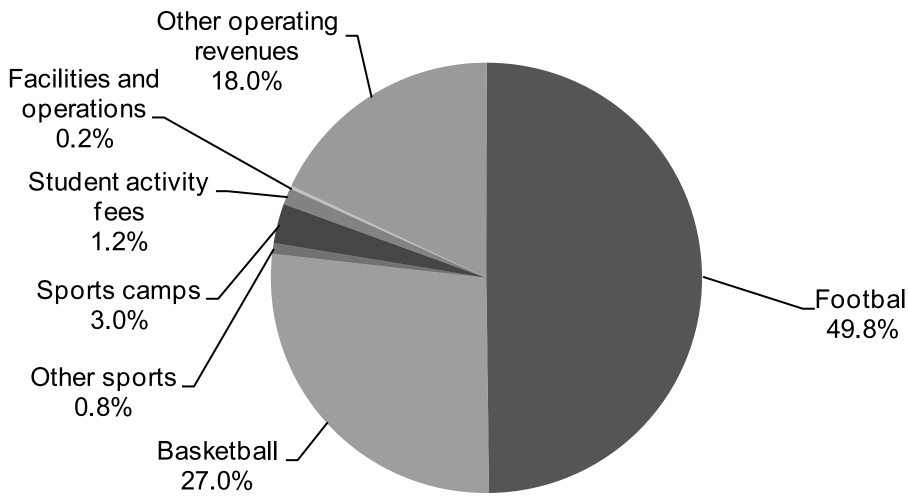
- Total assets increased $5.3 million or 20.4% primarily due to a $5.7 million increase in cash and cash equivalents resulting principally from operating revenues and grants from the University exceeding operating expenses.
- Total liabilities increased $1.6 million. Deferred revenue increased $1.0 million due to higher advance sales of football tickets and reserved parking caused by price increases. Long term liabilities increased $642,000 due to recognition of a liability for coach longevity and retention bonuses.
- Total net assets increased $3.7 million during the year ended June 30, 2010, driven by an increase of $3.6 million in unrestricted net assets caused by operating and nonoperating revenues in excess of operating expenses and transfers to the University.

Statements of Revenues, Expenses and Changes in Net Assets

	2011	2010	2009
OPERATING REVENUES			
Football	$ 33,130,188	$ 30,908,321	$ 25,119,768
Basketball	17,937,889	17,440,345	15,508,292
Other sports	540,130	558,167	383,515
Total sports	51,608,207	48,906,833	41,011,575
Sports camps	1,975,339	1,689,513	1,653,986
Student activity fees	819,124	738,194	686,003
Facilities and operations	182,307	226,128	1,905,765
Other operating revenue, primarily media rights and sponsorships	11,941,605	12,091,660	11,599,589
Total operating revenues	66,526,582	63,652,328	56,856,918
OPERATING EXPENSES			
Football	13,852,365	13,354,165	12,470,120
Basketball	11,516,513	11,166,116	8,182,263
Other sports	15,630,767	14,366,104	13,442,534
Total sports	40,999,645	38,886,385	34,094,917
Sports camps	1,930,336	1,650,044	1,632,972
Facilities and operations	8,155,431	8,253,110	8,468,691
Administrative and general	14,756,844	18,205,416	12,919,237
Depreciation	533,475	555,336	541,996
Total operating expenses	66,375,731	67,550,291	57,657,813
NET INCOME (LOSS) FROM OPERATIONS	150,851	(3,897,963)	(800,895)
NONOPERATING REVENUES (EXPENSES)			
Royalties/license fees	2,133,534	1,487,572	1,809,985
Investment income	71,162	55,265	79,329
Grants from the University of Kentucky for noncapital purposes	11,285,572	9,548,068	6,767,560
Interest on capital asset-related debt	-	-	(626,640)
Net nonoperating revenues and expenses	13,490,268	11,090,905	8,030,234
Net income before other revenues, expenses, gains, or losses	13,641,119	7,192,942	7,229,339
Capital gifts and grants	30,000	-	-
Grants to the University of Kentucky for capital purposes	(15,025,862)	(3,511,737)	(13,270,112)
Other	72,520	(12,974)	(1,648,713)
Total other expenses (net)	(14,923,342)	(3,524,711)	(14,918,825)
Total increase (decrease) in net assets	(1,282,223)	3,668,231	(7,689,486)
Net assets, beginning of year	13,424,548	9,756,317	17,445,803
Net assets, end of year	$ 12,142,325	$ 13,424,548	$ 9,756,317

2011. Total operating revenues were $66.5 million for the year ended June 30, 2011. The most significant sources of operating revenue for the Association were football (49.8%), basketball (27.0%), and other operating revenues, primarily media rights and sponsorships (18.0%). Operating revenues increased $2.9 million primarily due to increases in football revenue of $2.2 million caused by increased ticket and parking passes revenue and additional funds provided by television rights as negotiated by the SEC.

TOTAL OPERATING REVENUES

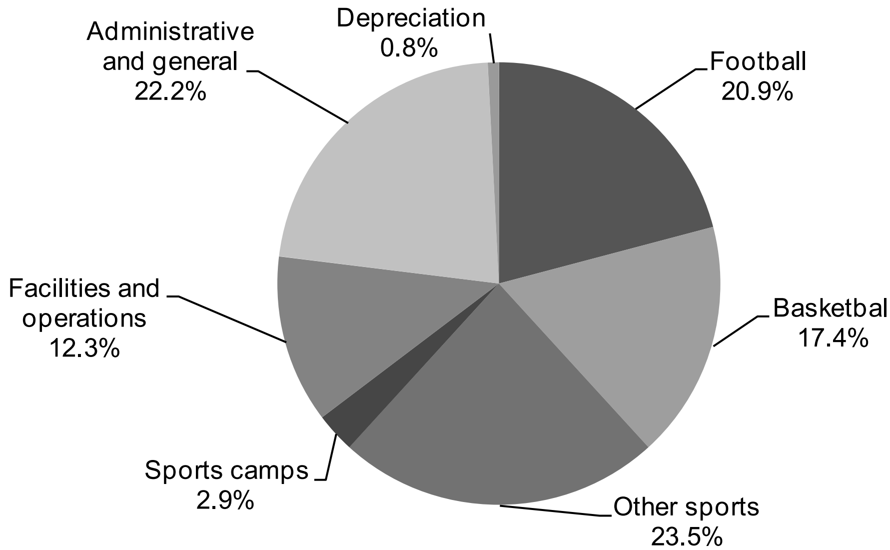


Operating expenses, including $533,000 of depreciation, totaled $66.4 million. Of this amount, $41.0 million or 61.7% was used in direct support of sports programs and $14.8 million or 22.3% supported the Association's administrative operations.

Operating expenses decreased $1.2 million or 1.7% primarily caused by decreases in administrative and general expenses of $3.4 million or 18.9%, offset by an increase in sports related expenses of $2.1 million or 5.4%. Administrative and general expenses decreased primarily due to the settlement last year of a lawsuit with the former men's basketball head coach. Sports related expenses increased mainly due to increased coaches' salaries caused by contractual increases.

The Association's expenses for operating sports programs include scholarship expenses of $9.5 million. These scholarships are funded by a transfer from the University of Kentucky K Fund (the K Fund).

TOTAL OPERATING EXPENSES



2010 Versus 2009. During the year ended June 30, 2010:

- Total operating revenues were $63.7 million. The most significant sources of operating revenue for the Association were football (48.6%), basketball (27.4%), and other operating revenues, primarily media rights and sponsorships (18.9%). Operating revenues increased $6.8 million primarily due to increases in football revenue of $5.8 million and basketball revenue of $1.9 million caused mainly by TV/broadcasting income from the SEC resulting from a new contract for television broadcasting rights. The increases were offset by a decrease in facilities and operations revenues of $1.7 million caused by the receipt of a legal settlement in the prior year.

- Operating expenses increased $9.9 million or 17.2% primarily caused by increases in administrative and general expenses of $5.3 million or 40.9% and sports related expenses of $4.8 million or 14.1%. Administrative and general expenses increased primarily due to the settlement of a lawsuit with the former men's basketball head coach. Sports related expenses increased mainly due to increased coaches' salaries caused by head coach and other staffing changes in basketball and football.

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

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

	2011	2010	2009
CASH PROVIDED (USED) BY :			
Operating activities	$ (224,158)	$ (1,273,955)	$ 627,727
Noncapital financing activities	13,419,106	11,035,640	8,586,611
Capital and related financing activities	(15,377,315)	(4,140,409)	(9,369,619)
Investing activities	30,994	43,834	3,326,879
Net increase in cash and cash equivalents	(2,151,373)	5,665,110	3,171,598
Cash and cash equivalents, beginning of year	24,929,560	19,264,450	16,092,852
Cash and cash equivalents, end of year	$22,778,187	$24,929,560	$19,264,450

2011. The major source of funds included in operating activities is revenue from sports of $50.8 million for the year ended June 30, 2011. The largest cash payments for operating activities were made to suppliers and for reimbursements of salaries and wages of approximately $36.8 million and $29.1 million, respectively. Cash used by operating activities decreased $1.0 million due to a decrease of $2.2 million in payments to suppliers, increases of other receipts of $622,000 and sports revenues of $414,000, offset by an increase of $2.2 million in reimbursements of salaries and wages.

During the year ended June 30, 2011, cash receipts in the noncapital financing activities group were generated mainly by grants from the K Fund of $9.5 million for athletic scholarships and $5.8 million for student athlete support services, offset by transfers of $4.0 million to the University, primarily in support of non-athletic scholarships. In addition, royalties and license fees provided cash of $2.1 million.

Cash used by capital and related financing activities is primarily expended on grants to the University to fund the construction and acquisition of capital assets, including principal and interest payments on debt. In addition, cash is also used for the direct purchase of capital assets.

During the year ended June 30, 2011, cash provided by investing activities reflects proceeds from sales and maturities of investments of $249,000 and interest and dividend income on investments of $31,000, net of cash used to purchase investments of $249,000.

2010 Versus 2009. Cash increased $5.7 million primarily due to cash provided by $11.0 million noncapital financing activities and $44,000 investing activities, offset by cash used by operating activities of $1.3 million and capital and related financing activities of $4.1 million.

Capital Asset and Debt Administration

Capital Assets. Capital assets, net of accumulated depreciation, of $1.8 million at June 30, 2011, were comparable to the prior year end. Significant changes to capital assets during FY 2010-2011 included:

Capital asset additions	$	462,000
Capital asset disposals, net	$	(36,000)
Current year depreciation expense	$	(533,000)

Debt. As of June 30, 2011, the Association has no debt.

Factors Impacting Future Periods

The Association is funded primarily by sales of tickets to athletic events and support from contributors. During fiscal year 2011, ticket revenues and donations have increased. Should ticket revenues or donations ever decrease, it could impact the Association's future financial results.

UNIVERSITY OF KENTUCKY ATHLETIC ASSOCIATION
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF NET ASSETS
JUNE 30, 2011 AND 2010

	2011	2010
ASSETS		
Current Assets		
Cash and cash equivalents	$22,778,187	$24,929,560
Accounts receivable	305,943	316,888
Inventories and other assets	3,825,266	3,576,369
Total current assets	26,909,396	28,822,817
Noncurrent Assets		
Endowment investments	289,509	249,342
Capital assets, net	1,810,659	1,917,862
Total noncurrent assets	2,100,168	2,167,204
Total assets	29,009,564	30,990,021
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	2,091,931	2,508,048
Deferred revenue	13,797,058	14,300,954
Due to the University of Kentucky	105,951	114,613
Total current liabilities	15,994,940	16,923,615
Noncurrent Liabilities		
Long term liabilities	872,299	641,858
Total noncurrent liabilities	872,299	641,858
Total liabilities	16,867,239	17,565,473
NET ASSETS		
Invested in capital assets, net of related debt	1,810,659	1,917,862
Restricted expendable	337,791	305,927
Unrestricted	9,993,875	11,200,759
Total net assets	$12,142,325	$13,424,548

See notes to financial statements.

UNIVERSITY OF KENTUCKY ATHLETIC ASSOCIATION
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

	2011	2010
OPERATING REVENUES		
Sports:		
Football	$33,130,188	$30,908,321
Basketball	17,937,889	17,440,345
Other sports	540,130	558,167
Total sports	51,608,207	48,906,833
Sport camps	1,975,339	1,689,513
Student activity fees	819,124	738,194
Facilities and operations	182,307	226,128
Other operating revenues, primarily media rights and sponsorships	11,941,605	12,091,660
Total operating revenues	66,526,582	63,652,328
OPERATING EXPENSES		
Sports:		
Football	13,852,365	13,354,165
Basketball	11,516,513	11,166,116
Other sports	15,630,767	14,366,104
Total sports	40,999,645	38,886,385
Sport camps	1,930,336	1,650,044
Facilities and operations	8,155,431	8,253,110
Administrative and general	14,756,844	18,205,416
Depreciation	533,475	555,336
Total operating expenses	66,375,731	67,550,291
Net income (loss) from operations	150,851	(3,897,963)
NONOPERATING REVENUES (EXPENSES)		
Royalties/license fees	2,133,534	1,487,572
Investment income	71,162	55,265
Grants (to) from the University of Kentucky for noncapital purposes	11,285,572	9,548,068
Net nonoperating revenues (expenses)	13,490,268	11,090,905
Net income (loss) before other revenues, expenses, gains, or losses	13,641,119	7,192,942
Capital grants and gifts	30,000	-
Grants (to) from the University of Kentucky for capital purposes	(15,025,862)	(3,511,737)
Other	72,520	(12,974)
Total other revenues (expenses)	(14,923,342)	(3,524,711)
Increase (decrease) in net assets	(1,282,223)	3,668,231
NET ASSETS, beginning of year	13,424,548	9,756,317
NET ASSETS, end of year	$12,142,325	$13,424,548

See notes to financial statements.

UNIVERSITY OF KENTUCKY ATHLETIC ASSOCIATION
A COMPONENT UNIT OF THE UNIVERSITY OF KENTUCKY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Revenues from sports	$ 50,844,300	$ 50,430,175
Payments to vendors and contractors	(36,757,411)	(38,960,585)
Salaries, wages and benefits reimbursements to the University of Kentucky	(29,114,856)	(26,925,500)
Other receipts (payments)	14,803,809	14,181,955
Net cash provided (used) by operating activities	(224,158)	(1,273,955)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Royalties/license fees	2,133,534	1,487,572
Grants (to) from the University of Kentucky	11,285,572	9,548,068
Net cash provided (used) by noncapital financing activities	13,419,106	11,035,640
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Grants (to) from the University of Kentucky for capital purposes	(15,034,524)	(3,524,448)
Purchases of capital assets	(342,791)	(615,961)
Net cash provided (used) by capital and related financing activities	(15,377,315)	(4,140,409)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	249,365	357,866
Interest and dividends on investments	30,995	31,562
Purchase of investments	(249,366)	(345,594)
Net cash provided (used) by investing activities	30,994	43,834
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2,151,373)	5,665,110
CASH AND CASH EQUIVALENTS, beginning of year	24,929,560	19,264,450
CASH AND CASH EQUIVALENTS, end of year	$ 22,778,187	$ 24,929,560
Reconciliation of net income (loss) from operations to net cash provided (used) by operating activities:		
Net income (loss) from operations	$ 150,851	$ (3,897,963)
Adjustments to reconcile net income (loss) from operations to net cash provided (used) by operating activities:		
Depreciation expense	533,475	555,336
Change in assets and liabilities:		
Accounts receivable, net	10,945	(20,856)
Inventories and other assets	(248,897)	507,880
Accounts payable and accrued liabilities	(397,077)	(72,124)
Deferred revenue	(503,896)	1,011,914
Long term liabilities	230,441	641,858
Net cash provided (used) by operating activities	$ (224,158)	$ (1,273,955)
NONCASH TRANSACTIONS		
Transfer of capital equipment (to) from the University of Kentucky	$ (26,540)	$ (158,634)
Trade in and disposal of capital equipment	$ (25,437)	$ 12,974
Capital asset additions in accounts payable	$ 1,541	$ 20,581

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity
The University of Kentucky Athletic Association (the Association) is a not-for-profit Kentucky corporation, established to promote athletics and physical culture for students at the University of Kentucky (the University) and residents of the Commonwealth of Kentucky (the Commonwealth). The Association 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 alumni and/or are appointed by the President of the University, and certain officers of the Association 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 Association.

  Expendable – Net assets whose use by the Association is subject to externally imposed stipulations that can be fulfilled by actions of the Association pursuant to those stipulations or that expire by the passage of time.

- Unrestricted: Net assets whose use by the Association 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 Association's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

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

Cash and Cash Equivalents. The Association 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 Association's endowment funds are included in noncurrent endowment investments.

Accounts Receivable. This classification consists of amounts due from sponsors for advertising rights and reimbursement of expenses made pursuant to contract agreements. Accounts receivable are recorded net of estimated uncollectible amounts based upon a review of outstanding receivables, historical collection information and existing economic conditions. No allowance was deemed necessary for 2011 or 2010.

Inventories. Inventories are stated principally at the lower of average cost or market. Inventories primarily consist of sports equipment and supplies.

Pooled Endowment Funds. The Association's endowment investments are administered as part of the University's pooled endowment funds. All contributing endowments participate in the income and appreciation of the pool on a per unit basis commensurate with their contribution to the pool. New endowments purchase units in the pool at the current unit value which is calculated each month based on the fair value of the pool investments divided by the number of pool units outstanding. The market value method of accounting for pooled endowment funds is employed to ensure proper distribution of market price changes, realized gains (losses) on sales, accrued income earned, and distribution of investment earnings for expenditure by participating funds.

In accordance with the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"), as adopted by the Commonwealth of Kentucky 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. Prior to the passage of UPMIFA, the University was subject to the Uniform Management of Institutional Funds Act ("UMIFA"), as adopted by the Commonwealth of Kentucky, which also allowed for total return management.

The University utilizes a spending policy designed to smooth spending distributions and protect endowed programs from market volatility by calculating distributions based on a percentage of the average market value of the endowment over a specified period of time. The University has made expenditure decisions in accordance with prevailing UPMIFA or UMIFA statutes and donor gift agreements. UPMIFA allows institutions to appropriate for expenditure so much of an endowment fund as the institution deems is prudent based on a review of various factors set forth in the Act, subject to terms set forth in a gift agreement. UMIFA allowed institutions to appropriate for expenditure a prudent amount of realized and unrealized gains over the historic dollar value of an endowment fund, also subject to terms set forth in a gift agreement.

For the year ended June 30, 2011 the University's endowment spending rule provided for annual distributions of 4.375 percent of the sixty month moving average market value of fund units. For the year ended June 30, 2010, the University's endowment spending rule provided for annual distributions of 4.5 percent of the thirty-six month moving average market value of fund units. Approximately $7,100 and $7,600 respectively, was transferred from endowment realized and unrealized gains to support current programs in accordance with the University's endowment spending rule. Additionally, for the year ended June 30, 2011, the University assessed eligible endowment accounts with a management fee of 0.375 percent of total asset value. For the year ended June 30, 2010, the University assessed eligible endowment accounts with a management fee of 0.5 percent of total asset value.

The Investment Committee of the University's Board of Trustees has approved a spending rate distribution of 4.25 percent of a sixty month moving average market value of fund units for the year ended June 30, 2012. Additionally, the Investment Committee has approved a management fee of 0.25 percent for the year ended June 30, 2012.

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.

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 $2,000 or more ($1,000 for computers) and having an estimated useful life of greater than one year 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 and 5 – 20 years for equipment and vehicles.

Deferred Revenue. Deferred revenue consists of amounts received in advance of an event, primarily football ticket and football reserved parking sales relating to the upcoming season. Revenue is recognized in the period in which the event occurs.

Compensated Absences. The amount of vacation leave earned but not taken by University employees at June 30 is recorded as a liability owed to the University by the Association. Compensated absence liabilities are computed using the pay rates in effect at the statement of net assets date plus an additional amount for compensation-related payments such as social security and Medicare taxes, computed using rates in effect at that date.

Income Taxes. The Association is exempt from federal income tax under the Internal Revenue Code, as a 501(c)(3) organization.

Restricted Asset Spending Policy. The Association'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 Association 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. Nearly all of the Association's expenses are from exchange transactions. Certain revenues relied upon for operations, such as gifts and investment income, are recorded as nonoperating 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 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 accrued expenses and other liability accounts.

2. DEPOSITS AND INVESTMENTS

The fair value of deposits and investments, by type, at June 30, 2011 and 2010 is as follows:

	2011	2010
Cash on deposit with the University of Kentucky	$ 22,778,187	$ 24,929,560
Investment in University of Kentucky pooled endowment fund (quasi endowment)	289,509	249,342
Total	$ 23,067,696	$ 25,178,902

	2011	2010
Statement of Net Assets classification		
Cash and cash equivalents	$ 22,778,187	$ 24,929,560
Endowment investments	289,509	249,342
Total	$ 23,067,696	$ 25,178,902

At June 30, 2011, the University's pooled endowment fund consisted of common and preferred stock (5.3%), pooled equity funds (37.0%), pooled private equity funds (4.7%), pooled absolute return funds (19.1%), pooled real return funds (10.4%), pooled real estate funds (5.5%), U.S. treasury fixed income (0.8%), government agency fixed income funds (1.8%), corporate fixed income funds (2.2%), pooled fixed income funds (13.1%) and cash and cash equivalents (0.1%). At June 30, 2010, the University's pooled endowment fund consisted of pooled equity funds (48.2%), pooled private equity funds (3.6%), pooled absolute return funds (10.0%), pooled real return funds (7.1%), pooled real estate funds (6.9%), U.S. treasury fixed income (4.4%), government agency fixed income funds (2.0%), corporate fixed income funds (4.4%), pooled fixed income funds (12.1%) and cash and cash equivalents (1.3%).

Deposit and investment policies. The Association 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 Association's funds.

For purposes of investment management, the Association'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 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 Association's deposits and investments are exposed to various risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could affect the investment amounts in the statement of net assets.

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligation, causing the Association 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 for balances exceeding amounts covered by the Federal Deposit Insurance Corporation. On November 9, 2010, the FDIC Board of Directors issued a final rule to implement Section 343 of the Dodd-Frank Wall Street Reform and Consumer Protection Act that provides temporary unlimited deposit insurance coverage for noninterest-bearing transaction accounts at all FDIC-insured depository institutions (the "Dodd-Frank Provision"). The separate coverage for noninterest-bearing transaction accounts became effective on December 31, 2010 and terminates on December 31, 2012. The Association's deposits are non-interest bearing and are fully insured by FDIC coverage. Credit risk on repurchase agreements 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 managers are permitted to use derivative instruments to limit credit risk. Additionally, 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 Association 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 held in the University's name. Deposits and repurchase agreements with the Commonwealth of Kentucky are held in the Commonwealth's name. The University maintains records evidencing the Association'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 Association's ownership interest (units) in the University's pooled endowment fund.

Concentrations of Credit Risk. Association 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 deposited or invested in one issuer. However, all such deposits 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 five (5) 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, 2011, the Association had no underlying investments in any one issuer which represent more than five (5) 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 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 managers are permitted to use derivative instruments to limit interest rate risk. Additionally, endowment investments held by the University's fixed income managers are limited to a duration that is within +/-25% of the duration of the Barclays Aggregate Bond Index.

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 Association'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. The University's investments in the various pooled funds are denominated in U.S. dollars, with the exception of two private equity funds denominated in Euros. Endowment managers are permitted to use derivative instruments to limit foreign currency risk.

3. CAPITAL ASSETS, NET

Capital assets as of June 30, 2011 are summarized as follows:

	2011			
	Beginning Balance	Additions	Deletions	Ending Balance
Equipment	$ 5,220,913	$ 462,052	$ 311,784	$ 5,371,181
Vehicles	582,627	-	-	582,627
	5,803,540	462,052	311,784	5,953,808
Accumulated Depreciation				
Equipment	3,438,684	480,401	276,004	3,643,081
Vehicles	446,994	53,074	-	500,068
	3,885,678	533,475	276,004	4,143,149
Net capital assets	$ 1,917,862	$ (71,423)	$ 35,780	$ 1,810,659

Capital assets as of June 30, 2010 are summarized as follows:

	2010			
	Beginning Balance	Additions	Deletions	Ending Balance
Equipment	$ 4,795,606	$ 614,980	$ 189,673	$ 5,220,913
Vehicles	561,459	21,168	-	582,627
	5,357,065	636,148	189,673	5,803,540
Accumulated Depreciation				
Equipment	3,137,399	473,484	172,199	3,438,684
Vehicles	365,142	81,852	-	446,994
	3,502,541	555,336	172,199	3,885,678
Net capital assets	$ 1,854,524	$ 80,812	$ 17,474	$ 1,917,862

4. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2011 and 2010, are as follows:

	2011	2010
Payable to vendors and contractors	$ 1,524,278	$ 1,991,700
Due to the University of Kentucky for accrued payroll and vacation	567,653	516,348
Total	$ 2,091,931	$ 2,508,048

5. LONG TERM LIABILITIES

Long-term liabilities as of June 30, 2011 and 2010, are summarized as follows:

	2011					
	Beginning Balance	Additions	Deletions	Ending Balance	Current Portion	Noncurrent Portion
Deferred compensation	$ 641,858	$ 463,977	$ 233,536	$ 872,299	$ -	$ 872,299

The reduction in deferred compensation for the fiscal year ending June 30, 2011 was the result of a contract amendment for the head men's basketball coach.

	2010					
	Beginning Balance	Additions	Deletions	Ending Balance	Current Portion	Noncurrent Portion
Deferred compensation	$ -	$ 641,858	$ -	$ 641,858	$ -	$ 641,858

6. CONTINGENT LIABILITIES

The Association is responsible for annual debt service payments related to certain athletic facilities as follows:

- Commonwealth Football Stadium was expanded and renovated in 1999. Funding for this project was provided by the University, through a lease financing arrangement with the Commonwealth of Kentucky. Although the debt for this project is not reflected on the Association's financial statements, the Association is responsible for the annual lease payment on Commonwealth Stadium of approximately $2,200,000.
- A project was completed in fiscal year 2007 to renovate and expand Memorial Coliseum. To provide part of the required funding for this project, the University issued $7.2 million of its General Receipts Bonds in fiscal 2006. Although the debt for this project is not reflected on the Association's financial statements, the Association is responsible for the annual debt service payment on these bonds, which is approximately $523,000.

7. INVESTMENT INCOME

Components of investment income for the years ended June 30, 2011 and 2010 are as follows:

	2011	2010
Interest and dividends earned on endowment investments	$ 4,694	$ 5,815
Realized and unrealized gains and losses on endowment investments	40,167	23,703
Interest on cash and non-endowment investments	26,301	25,747
Total	$ 71,162	$ 55,265

8. TRANSACTIONS WITH THE UNIVERSITY OF KENTUCKY

All salaries, wages and benefits reimbursements represent charges for University employees. Payments for the capital lease for Commonwealth Stadium and the debt service for Memorial Coliseum are grants to the University of Kentucky. For each of the years ended June 30, 2011 and 2010, payments of capital leases for Commonwealth Stadium were $2,219,000 and $2,216,000, respectively. Payments for debt service for Memorial Coliseum for the years ended June 30, 2011 and 2010 were $523,000 and $528,000, respectively.

9. THE UNIVERSITY OF KENTUCKY K FUND

The University of Kentucky K Fund is a restricted fund within the University that can be used at the discretion of the Board of Trustees of the University for specified purposes related only to intercollegiate athletic activities of the University. The K Fund's expenses for the year ended June 30, 2011 included grants to the Association of $15,260,000 and to the University's unexpended plant funds of $2,000,000. The K Fund's expenses for the year ended June 30, 2010 included grants to the Association of $13,525,000 and to the University's unexpended plant funds of $400,000. The Association's financial statements for both of these years reflect the grants received from the K Fund as part of the grants from the University for noncapital purposes.

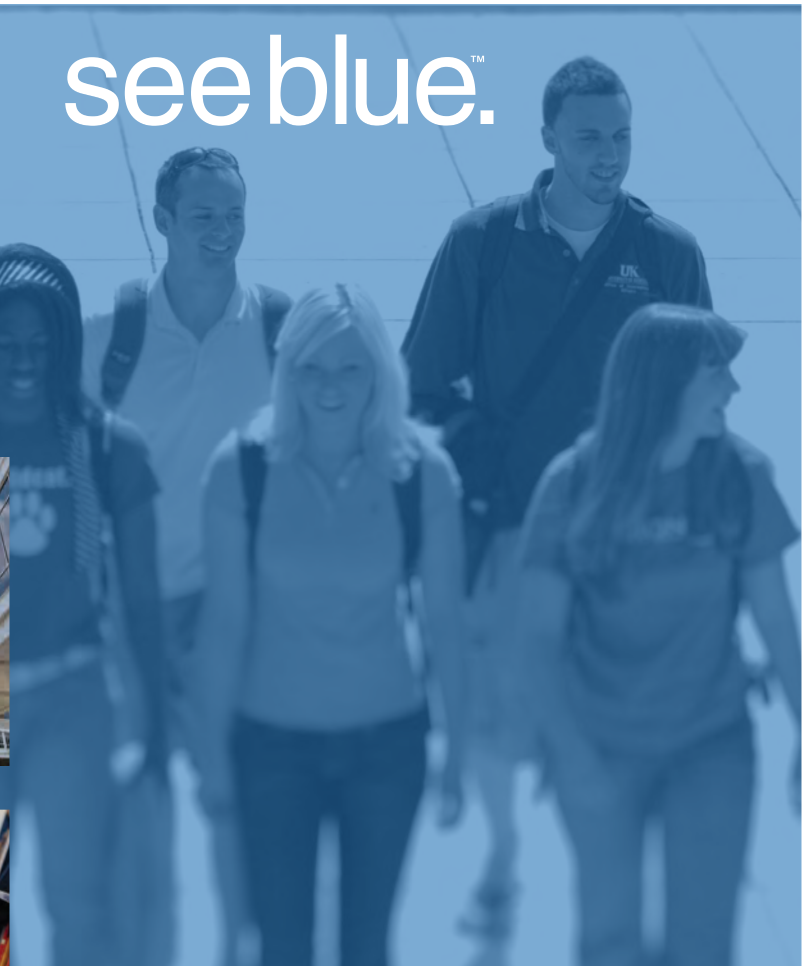
10. RISK MANAGEMENT

The Association is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omission; and natural disasters. These risks are covered by the State Fire and Tornado Insurance Fund (the Fund), commercial insurance, extension of coverage by the University's participation in an insurance risk retention group, and self-insurance.

The Fund covers losses to property from fire, wind, earthquake, flood and other named perils between $250,000 and $500,000 per occurrence. Losses in excess of $500,000 are insured by commercial carriers up to $1.00 billion per occurrence, buildings at replacement cost and contents on an actual cash value basis. Claims against directors, officers and employees for wrongful acts (errors and omission) are insured through a risk retention group. There have been no significant reductions in insurance coverage from 2010 to 2011. Settlements have not exceeded insurance coverage during the past three years.

11. CURRENT ECONOMIC CONDITIONS

The current protracted economic decline continues to present not-for-profit organizations with difficult circumstances and challenges, which in some cases have resulted in large declines in the fair value of investments, contributions, purchases of tickets to athletic events, and sport camp memberships. These conditions have made it difficult for many donors to continue to contribute to not-for-profit organizations and have caused many individuals to become more conservative in their spending. A significant decline in donation revenue, purchases of tickets to athletic events and sport camp memberships could have an adverse impact on the Association's future operating results. The financial statements have been prepared using values and information currently available to the Association. Due to the volatility of capital markets subsequent to year end, changes in investment values have been significant and may continue to affect investment amounts in the statement of net assets in the near term.



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