

**ULH, Inc.**

**Accountants' Report and Financial Statements**

**June 30, 2007 and 2006**

# ULH, Inc.

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## Independent Accountants' Report

Board of Directors  
ULH, Inc.  
Louisville, Kentucky

We have audited the accompanying statements of financial position of ULH, Inc. (Organization) as of June 30, 2007 and 2006, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Organization'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 Organization as of June 30, 2007 and 2006, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

September 21, 2007

**ULH, Inc.**

**Statements of Financial Position**

**June 30, 2007 and 2006**

**(In Thousands)**

	<u>2007</u>	<u>2006</u>
<b>ASSETS</b>		
Cash	\$ 539	\$ 458
Accounts receivable	352	152
Restricted investments	4,759	7,337
Prepaid expenses and other	1,122	1,004
Other assets	2	29
Capital assets, net	46,740	45,769
Total assets	<u>\$ 53,514</u>	<u>\$ 54,749</u>
<b>LIABILITIES AND DEFICIENCY IN NET ASSETS</b>		
Liabilities:		
Accounts payable	\$ 2,672	\$ 2,790
Bonds payable	53,105	53,548
Other liabilities	637	358
Total liabilities	56,414	56,696
Deficiency in net assets	(2,900)	(1,947)
Total liabilities and deficiency in net assets	<u>\$ 53,514</u>	<u>\$ 54,749</u>

See notes to financial statements

**ULH, Inc.**

**Statements of Activities**

**Years Ended June 30, 2007 and 2006**

**(In Thousands)**

	<u>2007</u>	<u>2006</u>
<b>REVENUES</b>		
Residence hall income	\$ 5,742	\$ 4,278
Other	819	428
Total revenues	<u>6,561</u>	<u>4,706</u>
<b>OPERATING EXPENSES</b>		
Residence hall operations (including depreciation)	4,918	3,125
General and administrative	333	385
Total operating expenses	<u>5,251</u>	<u>3,510</u>
<b>Operating income</b>	<u>1,310</u>	<u>1,196</u>
<b>NONOPERATING (EXPENSES)/REVENUES</b>		
Interest expense	(2,440)	(1,801)
Change in fair value of interest rate swap agreements	(27)	500
Other nonoperating expense	-	(13)
Transfers from University of Louisville Foundation, Inc.	204	281
Total nonoperating expenses	<u>(2,263)</u>	<u>(1,033)</u>
<b>Change in net assets</b>	(953)	163
<b>Deficiency in net assets at beginning of year</b>	<u>(1,947)</u>	<u>(2,110)</u>
<b>Deficiency in net assets at end of year</b>	<u>\$ (2,900)</u>	<u>\$ (1,947)</u>

See notes to financial statements

**ULH, Inc.**

**Statements of Cash Flows**

**Years Ended June 30, 2007 and 2006**

**(In Thousands)**

	<b>2007</b>	<b>2006</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Change in net assets	\$ (953)	\$ 163
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization expense	1,916	1,305
Change in fair value of interest rate swap agreements	27	(500)
Loss on disposals of capital assets	3	13
Change in assets and liabilities:		
Accounts receivable	(200)	(63)
Prepaid expenses and other	1	(20)
Accounts payable	(118)	(643)
Other liabilities	279	43
Net cash provided by operating activities	955	298
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchase of investments	(41,941)	(53,162)
Sales of investments	44,519	50,110
Purchase of capital assets	(2,810)	(12,763)
Proceeds from disposals of capital assets	-	2
Net cash used in investing activities	(232)	(15,813)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net proceeds from issuance of bonds payable	-	16,166
Principal payments of bonds payable	(455)	(350)
Payment of bond issue costs	(187)	(226)
Net cash (used in) provided by financing activities	(642)	15,590
Net increase in cash and cash equivalents	81	75
Cash at beginning of year	458	383
Cash at end of year	\$ 539	\$ 458
Supplemental information:		
Cash paid for interest (net of amount capitalized)	\$ 2,467	\$ 2,347

See notes to financial statements

# ULH, Inc.

## Notes to Financial Statements

June 30, 2007 and 2006

1. Organization and Summary of Significant Accounting Policies

a. Organization

ULH, Inc. (ULH) (a Kentucky not-for-profit corporation) is affiliated with the University of Louisville Foundation, Inc. (Foundation) through a common board of directors and certain common management.

ULH's purpose is to (a) lease and/or acquire and operate university housing projects and issue revenue bonds for university housing, and (b) receive and dispose of or retain gifts of real estate independent of the Foundation.

b. Investments

Investments consist of U.S. Treasury money market and time deposits and are stated at estimated market value.

Market value of restricted investments was approximately \$4.8 million and \$7.3 million at June 30, 2007 and 2006, respectively. These investments are restricted by bond indenture for payment of debt service, and repairs and replacement.

c. Derivatives

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, ULH entered into interest rate swap agreements for its floating rate debt.

Management has not designated the interest rate swap agreements as hedging instruments under the provisions of Statement of Financial Accounting Standards No. 133. As a result, the agreements are recorded at fair value (included in other assets) with subsequent changes in fair value included in earnings in the accompanying statements of activities.

d. Capital assets

Capital assets are stated at cost or estimated market value at date of receipt from donors. The provision for depreciation is calculated using the straight-line method based on the estimated useful lives of the assets.

ULH capitalizes interest costs as a component of construction in progress, based on interest costs of borrowing specifically for the project, net of interest earned on investments acquired with the proceeds of the borrowing. Total interest capitalized was (in thousands):

	<u>2007</u>	<u>2006</u>
Total interest expense incurred on borrowings for project	\$ -	\$ 520
Interest income from investment of proceeds of borrowings for project	-	(277)
Net interest cost capitalized	<u>\$ -</u>	<u>\$ 243</u>

e. Tax status

ULH has received a favorable determination letter from the Internal Revenue Service exempting it from federal income taxes under §501(c)(3) of the Internal Revenue Code and a similar provision of state law.

f. Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

g. Functional allocation of expenses

The costs of supporting the residence hall operations have been summarized on a functional basis in the statements of activities. Certain costs have been allocated among the residence hall operations and general and administrative categories based on actual expenses and other methods.

2. Capital assets, net

Capital assets, as of June 30, 2007 and 2006 are as follows (in thousands):

	<u>2007</u>	<u>2006</u>
Residence halls:		
Buildings	\$ 50,318	\$ 35,633
Furniture and fixtures	3,265	2,566
Construction in process	16	12,595
Accumulated depreciation	<u>(6,859)</u>	<u>(5,025)</u>
Total - net	<u>\$ 46,740</u>	<u>\$ 45,769</u>

Pursuant to a lease agreement, ULH agreed to pay the University of Louisville annual ground rental equal to available excess cash flow, as defined in the agreement. For the years ended June 30, 2007 and 2006, ULH recognized ground rental expense of approximately \$389,000 and \$225,000, respectively.

### 3. Bonds Payable

Bonds payable consist of the following at June 30, 2007 and 2006 (in thousands):

	<u>Description</u>	<u>Year of Maturity</u>	<u>2007</u>	<u>2006</u>
Series 2001A (non taxable)	Principal payments of \$115 to \$2,935 are due annually beginning 9/1/02 through maturity, and interest is due monthly at variable rates up to 12% (3.75% and 3.99% as of June 30, 2007 and 2006, respectively)	2029	\$ 23,160	\$ 23,485
Series 2002A (non taxable)	Principal payments of \$25 to \$985 are due annually beginning 7/1/05 through maturity, and interest is due monthly at variable rates up to 12% (3.75% and 3.99% as of June 30, 2007 and 2006, respectively)	2032	14,060	14,110
Series 2002B (non taxable)	Principal payments of \$70 to \$100 are due annually beginning 7/1/04 through maturity, and interest is due monthly at variable rates up to 12% (5.47% and 5.96% as of June 30, 2007 and 2006, respectively)	2007	100	180
Series 2005A (non taxable)	Principal payments of \$270 to \$1,060 are due annually beginning 6/1/16 through maturity, and interest is due monthly at fixed rates from 4% to 5%.	Ranging from 2016 to 2035	13,910	13,910
Series 2005B (taxable)	Principal payments of \$55 to \$390 are due annually beginning 6/1/07 through maturity, and interest is due monthly at a fixed rate of 4.91%.	2016	2,115	2,115
Total bonds payable			<u>53,345</u>	<u>53,800</u>
Less unamortized premium and discount			(240)	(252)
Bonds payable, net			<u>\$ 53,105</u>	<u>\$ 53,548</u>

The bonds are secured by letters of credit and the guaranty of the Foundation. Amounts payable under the guaranty are limited as follows (in thousands):

<b>Residence Hall</b>	<b>Aggregate limit</b>	<b>Annual limit</b>
Bettie Johnson Hall	\$ 30,000	Lesser of \$1.5 million, or annual debt service.
Kurz Hall	\$ 14,460	\$ 1,037
Community Park	\$ 31,308	\$ 1,121

Principal payments on the above obligations will be due in the next five years and thereafter as follows (in thousands):

For the Year Ended June 30,	<b>Principal Due</b>
2008	\$ 720
2009	765
2010	905
2011	1,055
2012	1,165
Thereafter	48,735
Total	\$ 53,345

4. Derivative financial instruments (in thousands)

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, ULH entered into interest rate swap agreements for a portion of its floating rate debt. Under the agreements, ULH pays or receives the net interest amount monthly, with the monthly settlements included in interest expense. The agreements are recorded at their fair value with subsequent changes in fair value included in change in fair value of swap agreements in nonoperating (expenses) revenues.

ULH has a swap agreement whereby ULH pays a fixed interest rate of 3.60% on notional amounts of \$14,060 and \$14,110 as of June 30, 2007 and 2006, respectively, in exchange for receiving payments based on a floating interest rate tied to the Municipal Bond Association Index. The floating rate is reset on a weekly basis. The market value of this agreement was approximately \$2 and \$40 at June 30, 2007 and 2006, respectively, and is included in other assets on the statements of financial position. This agreement terminates on July 2, 2007.

ULH also had two swap agreements whereby ULH paid a fixed interest rate of 3.88% and 3.66%, equally divided on notional amounts of \$23,485 as of June 30, 2006 in exchange for receiving payments based on a floating interest rate tied to the Municipal Bond Association Index. The floating rate is reset on a weekly basis. The market values of these agreements were approximately (\$11) at June 30, 2006 and are included in other assets on the statements of financial position. These agreements were terminated on September 1, 2006.

5. Disclosures about fair value of financial instruments

ULH records financial instruments at their fair value, which approximates carrying value (except bonds payable, as discussed below). The following methods were used to estimate the fair value of financial instruments.

Fair value is the estimated amount at which financial assets or liabilities could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Because no market exists for certain of these financial instruments and because management does not intend to sell these financial instruments, ULH does not know whether the fair values shown represent values at which the respective financial instruments could be sold individually or in the aggregate.

Restricted investments:

Fair value is based on quoted market prices.

Accounts receivable:

The carrying amount is a reasonable estimate of fair value.

Bonds payable:

Fair value is estimated by a third party based on the borrowing rates currently available to ULH for debt with similar terms and maturities. The following table presents estimated fair values and carrying values of ULH's bonds payable at June 30, 2007 and 2006 (in thousands):

	<u>2007</u>	<u>2006</u>
Carrying value	\$ 53,105	\$ 53,548
Fair value	\$ 52,870	\$ 53,220

Interest rate swap agreement:

The fair value is estimated by a third party.