

**UNIVERSITY OF LOUISVILLE RESEARCH FOUNDATION, INC.**

**A Component Unit of the University of Louisville**

**Accountants' Report and Financial Statements  
June 30, 2008 and 2007**

**UNIVERSITY OF LOUISVILLE RESEARCH FOUNDATION, INC.**

**A Component Unit of the University of Louisville**

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# **UNIVERSITY OF LOUISVILLE RESEARCH FOUNDATION, INC.**

## **A Component Unit of the University of Louisville**

### **Management's Discussion and Analysis (Unaudited)**

#### **Introduction**

The following discussion and analysis provides an overview of the financial position and activities of the University of Louisville Research Foundation, Inc. (Research Foundation) for the years ended June 30, 2008, 2007, and 2006. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

The Research Foundation is a non-profit corporation affiliated with the University of Louisville (University), a state-supported research university located in Kentucky's largest metropolitan area. The Research Foundation was established in 1989 for the purpose of promoting and supporting research projects, investigations, and other activities relating to the educational, scientific, literary, artistic, health care and public service missions of the University.

The University's strategic plan guides the Research Foundation's program. The Research Foundation accepts funding for research, training and service from extramural sources and has progressed steadily towards the goals established by the Kentucky Council on Postsecondary Education. During the fiscal year ended June 30, 2008, total awards were \$120.8 million, and some funding highlights include:

- \$2.2 million to support the National Research Center on Career and Technical Education
- \$1.4 million from the Environmental Protection Agency to support research in the area of the Atherothrombotic Effects of Particulate Matter
- \$1.4 million to support Development of Neural Recovery Rehabilitation and Research Center for Functional Health and Quality of Life Improvements
- \$1.2 million to support Groundwork Education in Mathematics and Science
- \$1.0 million from the NIH to support research on Fabricated Microvascular Networks
- \$0.8 million from the NIH to study the Role of RANTES in Pneumococcal Immunopathogenesis
- \$0.7 million from the NIH to support research of the role of Epithelial Cell TLRs in Disease Susceptibility
- \$0.6 million from the NIH to support research of the Role of PACAP in the Male Fetal Pituitary Breast Cancer

The Research Foundation is expanding its research base by promoting new collaborative research efforts within the University. One such example is the Center for Predictive Medicine for Biodefense and Emerging Infectious Disease (Center for Predictive Medicine). Construction for a building to house this initiative was begun in fiscal year 2007 on the Shelby Campus and the facility is due to open in July 2009. The Center for Predictive Medicine will expand the University's focus in the area of emerging infections.

The University supports these research missions by providing the capital investments needed to complete the research. The Clinical Research and Translational Research Building which will provide additional research space for oncology, infectious disease and other health related research initiatives is due to be completed in 2009.

## Financial Highlights

- The Research Foundation's financial position remains strong at June 30, 2008, with total assets of \$133.0 million and liabilities of \$22.2 million as compared to June 30, 2007 at \$115.9 million of total assets and \$20.8 million of liabilities. Net assets, which represent the residual interest in the Research Foundation's assets after liabilities are deducted, were \$110.8 million and \$95.1 million at June 30, 2008 and 2007, respectively.
- The Research Foundation's total liabilities of \$22.2 million consist primarily of deferred revenue. Deferred revenue represents the unearned portion of grants and sponsored programs and comprises \$13.9 million or 63% of total liabilities.
- Operating revenues amounted to \$355.5 million and \$320.3 million and operating expenditures were \$331.1 million and \$308.6 million resulting in a net operating income of \$24.4 million and \$11.7 million for the years ended June 30, 2008 and 2007, respectively. When adjusted for net nonoperating expenses of \$8.7 million and \$5.2 million, net assets of the Research Foundation increased by \$15.7 million and \$6.5 million for the years ended June 30, 2008, and 2007, respectively.

## Using the Financial Statements

The Research Foundation's financial report includes 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 Government Accounting Standards Board (GASB) principles. The Research Foundation is presented here as a single entity and is also included in the financial statements of the University.

GASB Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, requires the Research Foundation to present a classified Statement of Net Assets and Statement of Revenues, Expenses and Changes in Net Assets. Significant presentations under GASB Statement No. 35 with respect to the Research Foundation financial statements are as follows:

- Revenues and expenses are categorized as either operating or nonoperating. Certain revenues, including state appropriations, gifts, and investment income (loss) are considered nonoperating, as defined by GASB Statement No. 35. The Research Foundation's nonoperating revenues consist mainly of \$5.1 million and \$5.8 million in gift revenue for the years ended June 30, 2008 and 2007, respectively. These revenues relate to non-exchange transactions in which the Research Foundation is the beneficiary.
- Unexpended cash advances received for grants and sponsored programs are recorded as deferred revenue rather than as income when received. Such deferred revenues totaled \$13.9 million and \$13.0 million for the fiscal years ended June 30, 2008 and 2007, respectively.
- Capital assets are depreciated and reported net of accumulated depreciation. The Research Foundation's capital assets as of June 30, 2008 and 2007 consist primarily of equipment and library materials with a net asset value of \$60.5 million and \$40.6 million, respectively.

## Statements of Net Assets

The statements of net assets present the financial position of the Research Foundation at the end of the fiscal year and include all assets and liabilities. Net assets represent the difference between total assets and total liabilities and provide a snapshot of the current financial condition of the Research Foundation at the end of a fiscal year. The change in net assets indicates whether the overall financial condition has improved or worsened during the year. Assets and liabilities are generally measured using current values. Capital assets are stated at historical cost less accumulated depreciation. A condensed version of the Research Foundation's assets, liabilities and net assets at June 30, 2008, 2007, and 2006 is summarized below:

### Condensed Statements of Net Assets June 30, 2008, 2007, and 2006 (In Thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2008 - 2007</u> Change	<u>2007 - 2006</u> Change
<b>ASSETS</b>					
Current assets	\$ 67,744	\$70,351	\$76,188	\$ (2,607)	\$ (5,837)
Capital assets	60,505	40,629	36,333	19,876	4,296
Other noncurrent assets	4,848	4,955	753	(107)	4,202
Total assets	<u>133,097</u>	<u>115,935</u>	<u>113,274</u>	<u>17,162</u>	<u>2,661</u>
<b>LIABILITIES</b>					
Current liabilities	21,212	20,801	24,593	411	(3,792)
Noncurrent liabilities	1,033	-	-	1,033	-
Total liabilities	<u>22,245</u>	<u>20,801</u>	<u>24,593</u>	<u>1,444</u>	<u>(3,792)</u>
<b>NET ASSETS</b>					
Invested in capital assets, net of related debt	60,505	40,548	36,074	19,957	4,474
Restricted-Expendable	829	4,426	3,348	(3,597)	1,078
Unrestricted	49,518	50,160	49,259	(642)	901
Total net assets	<u>\$110,852</u>	<u>\$95,134</u>	<u>\$88,681</u>	<u>\$ 15,718</u>	<u>\$ 6,453</u>

## Assets

A review of the Research Foundation's statement of net assets at June 30, 2008 indicates that the Research Foundation is highly liquid with no long-term debt. Of the \$67.7 million in current assets, \$40.1 million, or 59%, consists of cash and cash equivalents. Of the remaining \$27.6 million, \$27.0 million, or 40%, of total current assets represents accounts receivable that are to be collected within the next year. As detailed in the Statement of Cash Flows, the cash decreased during the year by \$3.3 million.

Noncurrent assets consist of \$60.5 million of capital assets, \$0.3 million of noncurrent accounts receivable, and \$4.5 million of investments held with the University of Louisville Foundation, Inc (Foundation). The increase in depreciable equipment reflects the Research Foundation's emphasis on providing researchers the equipment and supplies necessary to further their progress.

## **Liabilities**

The Research Foundation's current liabilities consist mainly of \$13.9 million of unexpended cash advances for sponsored research activities. This deferred revenue increased by \$0.9 million from the fiscal year ended June 30, 2007, due mainly to the receipt of increased funding related to the sponsored research projects. The Research Foundation is required to set up a deferred liability when awards are paid in advance, as they are responsible for paying back any unused funds to the sponsor. Trade accounts payable accounts for the remaining \$7.3 million of current liabilities due at June 30, 2008. Other long-term liabilities of \$1.0 million and \$0.6 million of accounts payable and accrued liabilities relate to the Research Foundation's allocated portion of other post-employment benefits. This is the first year for which a liability for other post-employment benefits is required to be recognized.

## **Net Assets**

Net assets represent the residual interest in the Research Foundation's assets after liabilities are deducted. The Research Foundation's net assets at June 30, 2008 and 2007 were \$110.8 million and \$95.1 million, respectively. They are summarized into the three major categories in accordance with GASB Statement No. 35 reporting requirements as follows:

### **Invested in capital assets, net of related debt - \$60.5 million**

The Research Foundation's \$60.5 million in net capital assets represent construction in progress, equipment and depreciable library materials, net of accumulated depreciation. There is no debt attributable to the acquisition, construction or improvement of those assets. The \$20.0 million increase over prior year reflects \$27.2 million of capital asset additions, offset by recognition of depreciation expense.

### **Restricted expendable net assets - \$0.8 million**

Restricted expendable net assets represent funds primarily from fixed payment contracts that are subject to externally imposed restrictions governing their use. Net assets result from the excess of contract revenues over expenses incurred through June 30, 2008. The net assets remain restricted until the contract is completed.

Restricted expendable net assets decreased \$3.6 million or 82%. As contracts are completed and grant awards are fully utilized, it is expected that there will not be excess net assets.

### **Unrestricted net assets - \$49.5 million**

Unrestricted net assets result primarily from net operating income derived from clinical services and fixed contract revenues in excess of actual expenses. Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the Research Foundation's unrestricted net assets have been designated for various academic and research programs and initiatives.

Unrestricted net assets decreased \$0.6 million, or less than 1%, from unrestricted net assets at June 30, 2007. The decrease is a result of additional expenditures in the clinical operations, including a \$5.2 million increase in payments to the University Physicians Association (UPA) as compared to the fiscal year ended June 30, 2007.

## **Fiscal Year 2007**

The Research Foundation's financial position as of the fiscal year ended June 30, 2007 shows an increase in assets and a decrease in liabilities with an overall increase in net assets. Assets increased during the fiscal year ended June 30, 2007 by \$2.7 million, or 3%, as compared to the fiscal year ended June 30, 2006. This increase was due mainly to the \$4.3 million increase in capital assets as well as a \$4.3 million

increase in investments held by the Foundation, offset by the \$8.3 million decrease in cash and cash equivalents and a \$1.1 million decrease in amounts due from the University. The decrease in liabilities mainly resulted from the decrease in deferred revenues which decreased \$3.7 million from the fiscal year ended June 30, 2006.

Net assets increased \$6.5 million or 7% over net assets at June 30, 2006 due mainly to the \$4.5 million increase in investments in capital assets. This increase reflects the \$11.5 million investment in new capital assets, offset by the recognition of depreciation expense.

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

The statements of revenues, expenses and changes in net assets present the Research Foundation's results of operations. A condensed version of the Research Foundation's revenues, expenses and changes in net assets for the years ended June 30, 2008, 2007, and 2006 is as follows:

**Condensed Statements of Revenues, Expenses and Changes in Net Assets**  
**Years ended June 30, 2008, 2007, and 2006**  
(In Thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2008 - 2007</u> Change	<u>2007 - 2006</u> Change
<b>OPERATING REVENUES</b>					
Clinical services	\$ 160,490	\$ 144,267	\$ 128,298	\$ 16,223	\$ 15,969
Grants and contracts	173,073	154,811	146,763	18,262	8,048
Facilities and administrative cost recoveries	21,204	20,575	18,623	629	1,952
Other operating revenues	<u>701</u>	<u>622</u>	<u>356</u>	<u>79</u>	<u>266</u>
Total operating revenues	<u>355,468</u>	<u>320,275</u>	<u>294,040</u>	<u>35,193</u>	<u>26,235</u>
<b>OPERATING EXPENSES</b>					
Depreciation	7,168	6,855	4,841	313	2,014
Other operating expenses	<u>323,896</u>	<u>301,767</u>	<u>271,977</u>	<u>22,129</u>	<u>29,790</u>
Total operating expenses	<u>331,064</u>	<u>308,622</u>	<u>276,818</u>	<u>22,442</u>	<u>31,804</u>
Operating income	<u>24,404</u>	<u>11,653</u>	<u>17,222</u>	<u>12,751</u>	<u>(5,569)</u>
Gifts	5,145	5,773	6,102	(628)	(329)
Transfers	(14,229)	(11,296)	(11,206)	(2,933)	(90)
Other nonoperating revenues	<u>398</u>	<u>323</u>	<u>56</u>	<u>75</u>	<u>267</u>
Increase in net assets	<u>15,718</u>	<u>6,453</u>	<u>12,174</u>	<u>9,265</u>	<u>(5,721)</u>
Net assets, beginning of year	95,134	88,681	76,507	6,453	12,174
Net assets, end of year	<u>\$ 110,852</u>	<u>\$ 95,134</u>	<u>\$ 88,681</u>	<u>\$ 15,718</u>	<u>\$ 6,453</u>

### Operating Revenues

The Research Foundation recognized \$355.5 million in operating revenues for the year ended June 30, 2008. This represents an 11% increase in revenues from the \$320.3 million reported for the year ended June 30, 2007.

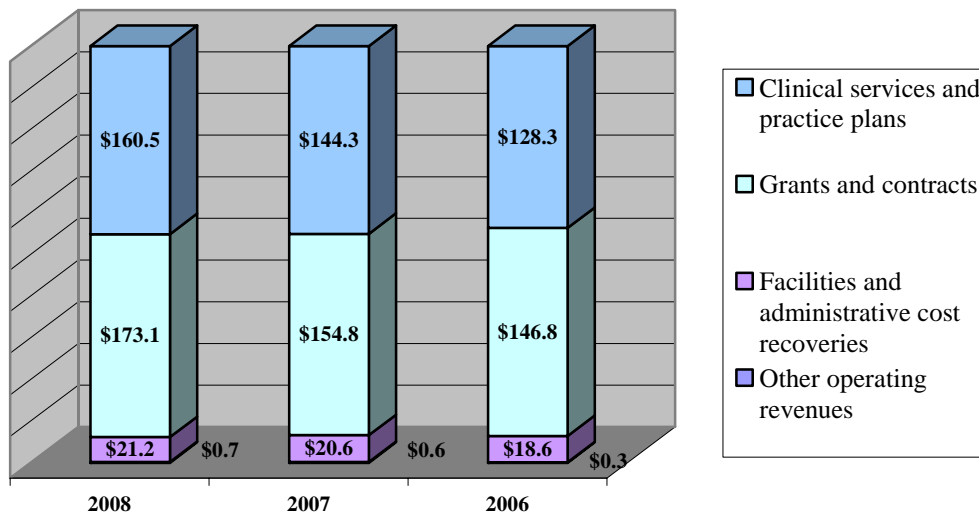
Revenues from clinical services were \$160.5 million for the year. This is an increase of approximately \$16.2 million, or 11%, compared to \$144.3 million in similar revenues reported for the year ended June 30, 2007. The increase in revenues is partially related to the \$5.4 million increase in income received from intergovernmental transfer transaction with the state Medicaid office. For the years ended June 30, 2008 and 2007, revenues earned for clinical services are reported net of \$26.6 million and \$28.0 million, respectively, in contractual allowances related to federal, state and private insurance providers.

Revenues from grants and contracts were \$173.1 million for the year ended June 30, 2008 as compared to \$154.8 million in revenues reported in the previous year. The increase is attributable to additional federal grants of \$16.0 million and a \$2.6 million increase in state and local grants for the year ended June 30, 2008. These increases reflect the Research Foundation’s commitment to reach the research goals in the Challenge for Excellence.

Revenues from facilities and administrative cost recoveries were \$21.2 million and \$20.6 million for the years ended June 30, 2008 and 2007, respectively. This represents the collection of a contractually agreed upon percentage applied to the grant reimbursements in lieu of calculating fees for indirect costs, such as general and administrative expenses, use of buildings and labs or utilities. As grant revenues increase, these cost recoveries increase accordingly. The Research Foundation, in turn, compensates the University for a portion of the cost recoveries in support of those expenditures. For the years ended June 30, 2008 and 2007, approximately \$11.9 million and \$10.4 million, respectively, were transferred to the University for this purpose.

The following is a graphic illustration of the Research Foundation’s operating revenues by major source for the years ended June 30, 2008, 2007, and 2006 (in millions).

**Operating Revenues  
Years Ended June 30, 2008, 2007, and 2006**

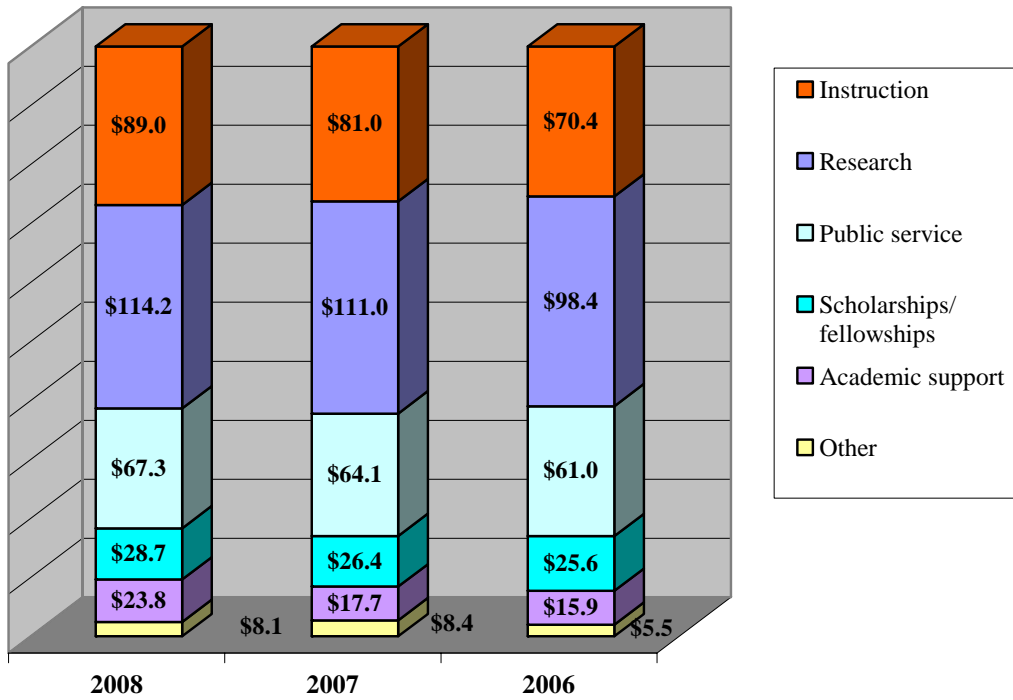


**Operating Expenses by Functional and Natural Class**

Total operating expenses were \$331.1 million and \$308.6 million for the fiscal years ended June 30, 2008 and 2007, respectively. The increase of \$22.5 million, or 7%, is directly related to the \$8.0 million increase in instruction expense along with the \$6.1 million increase in expenses related to academic support. Increases of \$5.7 million in clinical program instruction expense, account for the majority of the total increase. This is mostly related to increased cost associated with the teaching staff. In addition, there was a \$6.1 million increase in clinical expenses as it relates to academic support. The increase is mostly related to the \$5.2 million increase in payments to the University Physicians Association (UPA).

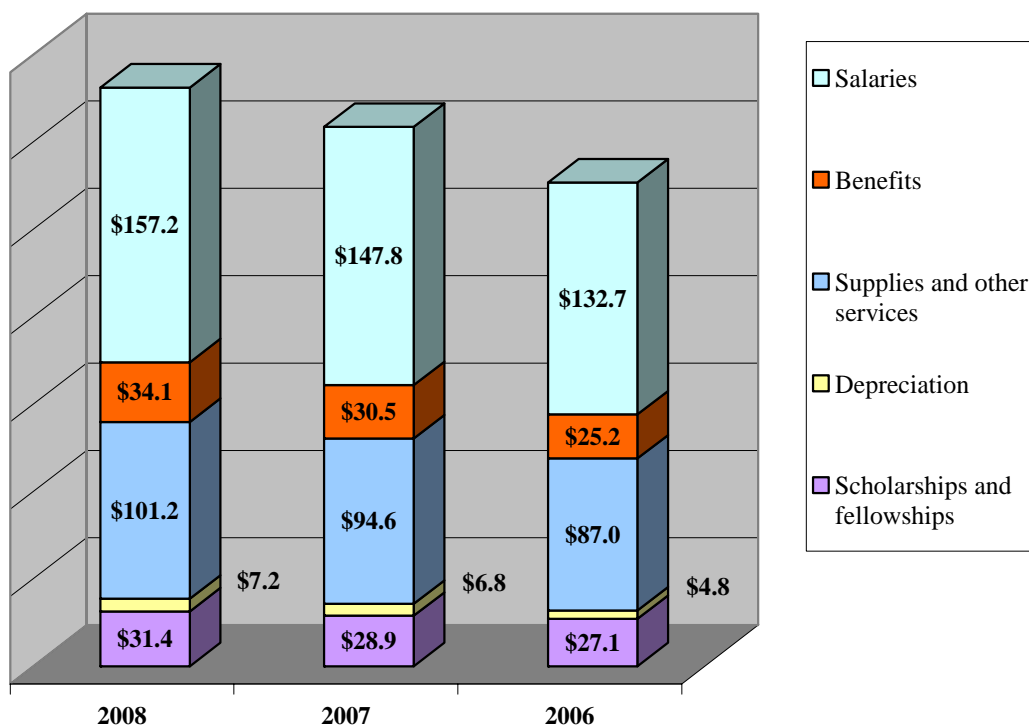
The following is a graphic illustration of total operating expenses by function for the years ended June 30, 2008, 2007 and 2006 (in millions):

**Operating Expenses - Functional**  
**Years ended June 30, 2008, 2007, and 2006**



The following is a graphic illustration of total operating expenses by natural classification for the years ended June 30, 2008, 2007 and 2006 (in millions):

**Operating Expenses: Natural Classification  
Years Ended June 30, 2008, 2007, and 2006**



**Nonoperating Revenues (Expense)**

The Research Foundation’s total nonoperating expense of \$8.7 million for fiscal year ended June 30, 2008, was mostly comprised of non-exchange gift revenues of \$5.1 million and transfer expenses of \$14.2 million. Included in the transfers total was an \$11.9 million transfer to the University, related to the facilities and administrative revenue, for administrative expenses incurred for sponsored research. Total nonoperating expense increased by \$3.5 million or 67% as compared to fiscal year ended June 30, 2007. The increase relates to the transfer of funds in the amount of \$3.4 million to the University for capital project funding.

**Fiscal Year 2007**

For the year ended June 30, 2007, Research Foundation reported \$320.3 million in operating revenues. This was a 9% increase from the \$294.0 million reported for the year ended June 30, 2006.

Revenues from clinical services were \$144.3 million for fiscal year 2007, an increase of 12% from the fiscal year ended June 30, 2006. The increase is partially related to the \$9.4 million income received from intergovernmental transfer transactions from the state Medicaid office.

Revenues from grants and contracts were \$154.8 million during the fiscal year ended June 30, 2007 an \$8.0 million increase from the fiscal year ended June 30, 2006. The increase is primarily attributable to additional federal grants of \$5.3 million and state and local grants of \$5.0 million, offset by a \$2.3 million decrease in nongovernmental grants and contracts. Revenues from facilities and administrative

cost recoveries increased 10% as compared to the fiscal year ended June 30, 2006. In conjunction with the facilities and administrative cost recoveries, \$10.4 million was transferred to the University, an increase of \$0.7 million from the \$9.7 million transferred in the fiscal year ended June 30, 2006.

Total operating expenses were \$308.6 million and \$276.8 million for the years ended June 30, 2007 and 2006, respectively. The increase of \$31.8 million, or 11%, is directly related to the \$12.6 million increase in research expense along with the \$10.6 million increase in expenses related to instruction. Increases of \$10.1 million in sponsored programs' research expense account for the majority of the total increase. This is directly related to the increased revenue from grants and sponsored program revenue. In addition, there was a \$9.0 million increase in clinical expenses as it relates to instruction due mainly to increased costs associated with teaching staff.

## Statements of Cash Flows

The statements of cash flows provide information about the Research Foundation's cash position by reporting the sources and uses of cash during the year. Cash inflows and outflows are categorized as operating, noncapital financing, capital financing and investing activities. A summary of the Research Foundation's cash flow activity for the years ended June 30, 2008, 2007, and 2006 is as follows:

**Condensed Statements of Cash Flows**  
**Years ended June 30, 2008, 2007, and 2006**  
(In Thousands)

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2008 - 2007</u> <u>Change</u>	<u>2007 - 2006</u> <u>Change</u>
Cash provided/(used) by:					
Operating activities	\$ 32,834	\$ 11,206	\$ 43,455	\$ 21,628	\$ (32,249)
Noncapital and related financing activities	(8,917)	(4,044)	(4,131)	(4,873)	87
Capital financing activities	(27,218)	(11,456)	(15,479)	(15,762)	4,023
Investing activities	-	(4,000)	-	4,000	(4,000)
Net (decrease)/increase in cash	<u>(3,301)</u>	<u>(8,294)</u>	<u>23,845</u>	<u>4,993</u>	<u>(32,139)</u>
Cash and cash equivalents, beginning of year	<u>43,423</u>	<u>51,717</u>	<u>27,872</u>	<u>(8,294)</u>	<u>23,845</u>
Cash and cash equivalents, end of year	<u>\$ 40,122</u>	<u>\$ 43,423</u>	<u>\$ 51,717</u>	<u>\$ (3,301)</u>	<u>\$ (8,294)</u>

## Operating Activities

The Research Foundation operating activities provided approximately \$32.8 million in net cash in the fiscal year ended June 30, 2008, due mainly to a \$25.0 million increase in cash from grants and contracts. The cash provided by operating activities increased \$21.6 million as compared to the prior year. Cash outflows from operations during the fiscal year ended June 30, 2008 increased due largely to expenses related to salaries, which increased \$9.4 million, and benefits, which increased \$3.8 million, as compared to the fiscal year ended June 30, 2007.

## Other Activities

The \$8.9 million cash used by noncapital and related financing activities includes the Research Foundation's payment of \$11.9 million to the University as reimbursement for indirect charges to support the use of buildings and labs. In total, cash used by noncapital and related financing had a \$4.9 million increase from the fiscal year ended June 30, 2007, as transfers to the University were offset by the receipt of \$5.1 million in non-exchange revenue classified as gifts.

Cash used for capital financing activities increased to \$27.2 million during the fiscal year ended June 30, 2008, due to an increase in the amount of capital assets purchased.

### **Fiscal year 2007**

The Research Foundation's cash and cash equivalents decreased by \$8.3 million during the fiscal year ended June 30, 2007. The Research Foundation's operating activities provided approximately \$11.2 million in net cash, a decrease of \$32.3 million or 74%, compared to the cash provided by operations in the fiscal year ended June 30, 2006. Total cash received from operations was \$313.1 million, which was a \$0.4 million increase from the fiscal year ended June 30, 2006. The cash increase is mostly due to a \$13.3 million and \$2.0 million increase in cash generated from clinical services and facilities and administrative cost recoveries, respectively, in the fiscal year ended June 30, 2007. These increases were offset by a \$15.2 million decrease in cash received from grants & sponsored programs.

Cash outflows from operations during the fiscal year ended June 30, 2007, were \$301.9 million. This was an increase of \$32.6 million as compared to the fiscal year ended June 30, 2006. The increase in cash outflows is largely due to a \$15.1 million increase in the Research Foundation's expenses related to salaries and a \$10.9 million increase in cash paid for supplies and other services during the fiscal year ended June 30, 2007, as compared to the prior year.

The \$4.0 million of cash used for noncapital and related financing activities includes the Research Foundation's payment of \$10.4 million to the University as reimbursement for indirect charges to support the use of buildings and labs. Transfers to the University were offset by the \$5.8 million in cash received related to gifts, which was a \$0.3 million decrease when compared to the \$6.1 million of cash received for gifts in the fiscal year ended June 30, 2006. Cash used for capital financing activities was \$11.4 million, representing the purchase of capital equipment, a 26% decrease from the fiscal year ended June 30, 2006. The \$4.0 million in investing activities relates to the investments held by the Foundation for the School of Dentistry.

### **Economic Factors that May Affect the Future**

As mandated by the 1997 House Bill 1 – Kentucky Postsecondary Education Improvement Act, the University is to become a premier, nationally recognized metropolitan research university. President Ramsey charged Executive Vice President and University Provost Shirley C. Willihnganz with the development of a new strategic plan. Through an inclusive process to include University constituents and community members at large, the Provost delivered “The 2020 Plan. Making It Happen” (Plan) a strategic plan that includes strategic goals and a long-range financial plan. This Plan builds the case for additional resources to fund new strategic initiatives through the year 2020.

The launch of the new Plan continues to be challenging. The University was told in December of 2007 to immediately implement a permanent 3 percent budget reduction in state appropriations. Then in April 2008, the Kentucky legislature enacted a comprehensive 2008-10 budget plan for the Commonwealth that included an additional 3 percent recurring cut in state funding for Kentucky colleges and universities. The University will not use these budget cuts as an excuse to step back from its mandate but instead will find other ways to continue the momentum and progress made with the Challenge.

Specifically, in the first year of the biennial budget, the University's base appropriation was reduced \$10.0 million. Also, the General Assembly moved the funding for the Metropolitan College initiative to the Cabinet for Economic Development. The University will work with the Cabinet Secretary to develop a Memorandum of Agreement to transfer these funds to the University, a fiscal agent, on a quarterly basis.

In its quest for preeminence, the University will not depend solely on state support to fund its strategic plan. The cyclical “up and down” trend of state funding and the uncertainty of the general business cycle are important environmental factors to consider, but the ambiguity and unpredictability of these revenue flows are cause for concern.

Recent economic reports indicate that significantly increased state appropriations are unlikely in the near future. The Economic Revenue Report projected the state ended the fiscal year June 30, 2008 with a revenue shortfall. Additionally, the pension issue continues to be a major public policy issue for state and local governments in Kentucky. These indications and other economic trends highlight the importance that for the foreseeable future the University must be creative in:

- Finding ways to generate new revenue;
- Managing expenses;
- Turning non-performing and under-performing assets into productive, fully-performing assets;
- Intensifying fundraising;
- Recognizing the importance of clinical partnerships and income for education and research; and
- Looking to sources other than the state for moving forward on projects

This financial report is designed to provide a general overview of the Research Foundation's finances and to show the Research Foundation's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Controller; University of Louisville; Louisville, KY 40292.

**University of Louisville Research Foundation, Inc.**  
**A Component Unit of the University of Louisville**  
**Statements of Net Assets**  
**As of June 30, 2008 and 2007**  
**(In Thousands)**

	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 40,122	\$ 43,423
Accounts receivable, net	26,976	26,160
Inventories	382	451
Other assets	264	317
Total current assets	<u>67,744</u>	<u>70,351</u>
Noncurrent Assets:		
Accounts receivable, net	355	693
Investments held with University of Louisville Foundation, Inc.	4,493	4,262
Capital assets, net	60,505	40,629
Total noncurrent assets	<u>65,353</u>	<u>45,584</u>
Total assets	<u>133,097</u>	<u>115,935</u>
<b>LIABILITIES</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	7,341	7,738
Accounts payable to University of Louisville Foundation, Inc.	-	68
Deferred revenue	13,871	12,995
Total current liabilities	<u>21,212</u>	<u>20,801</u>
Noncurrent Liabilities:		
Other long-term liabilities	1,033	-
Total noncurrent liabilities	<u>1,033</u>	<u>-</u>
Total liabilities	<u>22,245</u>	<u>20,801</u>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	60,505	40,548
Restricted - expendable for:		
Research	-	2,825
Instruction	713	1,409
Scholarships and fellowships	116	185
Student services	-	7
Unrestricted	49,518	50,160
Total net assets	<u>\$ 110,852</u>	<u>\$ 95,134</u>

See notes to the financial statements

**University of Louisville Research Foundation, Inc.**  
**A Component Unit of the University of Louisville**  
**Statements of Revenues, Expenses and Changes in Net Assets**  
**For the Years Ended June 30, 2008 and 2007**  
(In Thousands)

	<u>2008</u>	<u>2007</u>
<b>OPERATING REVENUES</b>		
Clinical services, net of contractual allowance of \$26,626 in 2008 and \$27,978 in 2007	\$ 160,490	\$ 144,267
Federal grants and contracts	127,850	111,853
State and local grants and contracts	33,631	30,996
Nongovernmental grants and contracts	11,592	11,962
Other operating revenue	701	622
Facilities and administrative cost recoveries	21,204	20,575
Total operating revenues	<u>355,468</u>	<u>320,275</u>
<b>OPERATING EXPENSES</b>		
Instruction	88,983	81,022
Research	114,191	111,023
Public service	67,265	64,081
Scholarships and fellowships	28,686	26,426
Academic support	23,837	17,695
Institutional support	678	688
Operation and maintenance of plant	248	812
Depreciation	7,168	6,855
Student services	5	10
Service centers	3	10
Total operating expenses	<u>331,064</u>	<u>308,622</u>
Operating income	<u>24,404</u>	<u>11,653</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Gifts	5,145	5,773
Net realized and unrealized gain on investments	231	262
Other nonoperating income	167	61
Net nonoperating revenues	<u>5,543</u>	<u>6,096</u>
Transfers	<u>(14,229)</u>	<u>(11,296)</u>
Total nonoperating expenses	<u>(8,686)</u>	<u>(5,200)</u>
Increase in net assets	15,718	6,453
<b>NET ASSETS</b>		
Net assets - beginning of year	95,134	88,681
Net assets - end of year	<u>\$ 110,852</u>	<u>\$ 95,134</u>

See notes to the financial statements

**University of Louisville Research Foundation, Inc.**  
**A Component Unit of the University of Louisville**  
**Statements of Cash Flows**  
**For the Years Ended June 30, 2008 and 2007**  
(In Thousands)

	<b>2008</b>	<b>2007</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Clinical services	\$ 161,598	\$ 143,449
Grants and contracts	173,396	148,423
Facilities and administrative cost recoveries	21,204	20,575
Other operating revenue	701	620
Payments to employees	(157,182)	(147,801)
Payments for benefits	(33,839)	(29,994)
Payments for scholarships and fellowships	(31,424)	(28,875)
Payments to suppliers	(101,620)	(95,191)
Net cash provided by operating activities	32,834	11,206
<b>CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Transfers to related entities	(14,230)	(11,029)
Gifts	5,145	5,773
Decrease in loan receivable from University of Louisville	-	1,151
Other noncapital financing activity	168	61
Net cash used by noncapital and related financing activities	(8,917)	(4,044)
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchases of capital assets	(27,218)	(11,456)
Net cash used by capital and related financing activities	(27,218)	(11,456)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of investments	-	(4,000)
Net cash used by investing activities	-	(4,000)
Net (decrease) in cash	(3,301)	(8,294)
Cash and cash equivalents - beginning of year	43,423	51,717
Cash and cash equivalents - end of year	\$ 40,122	\$ 43,423
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating income	\$ 24,404	11,653
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	7,168	6,855
Loss on disposal of equipment	93	119
Changes in assets and liabilities:		
Accounts receivable, net	(478)	(3,461)
Inventories	69	(10)
Other assets	53	(77)
Accounts payable and accrued liabilities	(384)	(118)
Deferred revenue	876	(3,755)
Other long-term liabilities	1,033	-
Net cash provided by operating activities	\$ 32,834	\$ 11,206
<b>NONCASH TRANSACTIONS</b>		
Transfer of assets (to)/from University of Louisville	\$ 1	\$ (267)
Capital asset additions in accounts payable	\$ -	\$ 81

See notes to the financial statements

**University of Louisville Research Foundation, Inc.**

**A Component Unit of the University of Louisville**

**Notes to Financial Statements**

**June 30, 2008 and 2007**

**1. Organizations and Summary of Significant Accounting Policies**

The University of Louisville Research Foundation, Inc. (the Research Foundation) is affiliated with the University of Louisville (the University) through a common Board of Directors and management. The Research Foundation is included within the University's financial statements. The Research Foundation is a separate corporation organized for the purpose of conducting the research, clinical operations, and other sponsored activities of the University. The significant accounting policies followed by the Research Foundation are described below.

**a. 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 Government Accounting Standards Board (GASB).

Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the University and the Research Foundation have elected to apply the provisions of 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.

**b. Cash on Deposit with the University of Louisville**

For administrative convenience, cash balances of the Research Foundation are included in bank accounts maintained by the University. Details of accounting transactions affecting cash are maintained in such a manner as to ensure an appropriate segregation of amounts maintained by each entity.

The University currently uses the Commonwealth of Kentucky (the Commonwealth) and a commercial bank as its depositories. At the Commonwealth, the University's accounts are pooled with other agencies of the Commonwealth. These Commonwealth-pooled deposits are substantially covered by federal depository insurance or by collateral held by the Commonwealth or in the Commonwealth's name.

The Research Foundation considers all investments (not held for long-term purposes) with an original maturity of three months or less to be cash equivalents.

**c. Accounts Receivable**

Accounts receivable consists of clinical and sponsored agreement charges. Clinical receivables are comprised of patient and insurance charges. In some aspects healthcare entities are charged for staff support services. Sponsored agreement receivable's relate to sponsored programs that support the Research Foundation. Accounts receivable is recorded net of estimated uncollectible amounts.

d. Inventories

Inventories are stated at the lower of cost or market on a first-in, first-out (FIFO) basis.

e. Investments

Investments are stated at current market value. Investments held with the University of Louisville Foundation, Inc. (Foundation) are invested under the policies and objectives established for the Foundation's general endowment pool. In an effort to mitigate market risk, the Foundation has adopted a policy of maintaining a diverse investment pool through the use of target asset allocation guidelines. These guidelines require that the Foundation's investment pool be made up of a mix of publicly traded fixed income and equity securities, private equities and other nonmarketable securities, and real estate investments.

The market risk inherent in certain of the Foundation's investments is primarily the potential loss arising from adverse changes in quoted market prices on equity securities and in interest rates on fixed income securities.

The Foundation invests in various corporate debt, equity and mutual fund securities. Investment securities, in general, are exposed to various risks, such as interest rates, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the Foundation's statements of financial position.

f. Capital Assets

Equipment and library books of the Research Foundation are stated at cost or, in the case of donated capital assets, estimated market value at date of receipt from donors.

Movable equipment costing \$5,000 and greater and having a useful life greater than one year are capitalized. Renovations to buildings, infrastructure and land improvements, if any, that significantly increase the value or extend the useful life of the structure and are in excess of \$100,000 are capitalized. Necessary and routine repairs and maintenance are charged to operating expense in the year the expense is incurred.

Depreciation of capital assets is computed on a straight-line basis over the estimated useful lives of the respective assets as follows: buildings - 40 years, library books - 10 years, and equipment - 3 to 20 years. The Research Foundation capitalizes, but does not depreciate, works of art and rare books.

Prior to July 1, 2002 it was the policy of the University to record all capital assets purchased by the Research Foundation as property of the University.

g. Classification of Revenues

The Research Foundation has classified its revenues as either operating or nonoperating revenues according to the following criteria:

Operating revenues - Operating revenues include activities that have the characteristics of exchange transactions, such as (1) clinical services, (2) grants and contracts, and (3) facilities and administrative cost recoveries.

Nonoperating revenues - Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Government Entities That Use Proprietary Fund Accounting*, and GASB No. 34, such as investment income.

h. Net Clinical Services Revenue

The Research Foundation has agreements with third-party payers that provide for payments to the Research Foundation at amounts different from its established rates. Net clinical services revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for the services rendered and includes estimated retroactive revenue adjustments and a provision for uncollectible accounts. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

i. Revenue Recognition

The Research Foundation receives revenues relative to sponsored agreements via grants, cooperative agreements, or contracts. The flow of funds relative to these sponsored agreements is in the form of cost reimbursement or advanced funding.

In the case of cost reimbursement, the Research Foundation incurs costs on behalf of the granting authority and is then reimbursed for such costs pursuant to the terms of the sponsored agreement. Grant revenues are recognized as reimbursable costs are incurred.

In the case of advanced funding, the Research Foundation receives funds prior to incurring costs pursuant to the sponsored agreement, with the stipulation that these funds may have to be returned to the sponsor in the event the project is not completed to the sponsor's satisfaction. These funds, totaling approximately \$13.9 million and \$13.0 million at June 30, 2008 and 2007, respectively, are recorded in the Research Foundation's financial statements as deferred revenue.

j. Net Assets

Net assets of the Research Foundation are classified in three components. Net assets invested in capital assets, net of related debt, consist of capital assets net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net assets are noncapital assets that must be used for a particular purpose as specified by creditors, grantors or donors external to the Research Foundation, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. Unrestricted net assets are remaining assets less remaining liabilities that do not meet the definition of invested in capital assets, net of related debt or restricted expendable.

k. Government Grants

Support funded by grants is recognized as the Research Foundation performs the contracted services or incurs outlays eligible for reimbursement under the grant agreements. Grant activities and outlays are subject to audit and acceptance by the granting agency and, as a result of such audit, adjustments could be made.

l. Tax Status

As an affiliate of a state institution of higher education, the income of the Research Foundation is generally exempt from federal and state income taxes under Section 115(a) of the Internal Revenue Code and a similar provision of state law. However, the Research Foundation is subject to federal income tax on any unrelated business taxable income.

m. 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.

n. Reclassifications

Certain 2007 amounts have been reclassified to conform with the 2008 presentation. These reclassifications had no effect on the change in net assets.

2. Transactions with Related Organizations

a. University of Louisville

The University provides certain facilities and administrative services to the Research Foundation for a share of the facilities and administrative cost recoveries. The current agreement provides for a transfer of 80%, after certain deductions, of the amount realized. Transfers from the Research Foundation to the University for their portion of cost recoveries totaled \$11.9 million and \$10.4 million for the years ended June 30, 2008 and 2007, respectively.

b. University of Louisville Foundation, Inc. (Foundation)

The Foundation is a separate corporation organized as a supporting organization of the University for the purpose of promoting the University's educational, scientific, literary and cultural interests. The Foundation held funds of the Research Foundation in the amount of \$4.5 million and \$4.3 million for the years ended June 30, 2008 and 2007, respectively, for investment purposes.

### 3. Investments

#### Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer, excluding investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools and other pooled investments.

The asset allocation for investments held with the Foundation as of June 30, 2008 and 2007 were as follows:

	<u>2008</u>	<u>2007</u>
Preferred and common stock	20%	32%
Corporate bonds	3%	2%
Mutual funds	45%	44%
Real estate	2%	2%
Investment in partnerships	11%	9%
U.S. Government securities	3%	4%
Marketable alternatives	16%	7%
Total	<u>100%</u>	<u>100%</u>

### 4. Accounts Receivable, net

Accounts receivable, net as of June 30, 2008 and 2007 are summarized as follows (in thousands):

	<u>2008</u>		
	<u>Gross</u>		<u>Net</u>
	<u>Receivable</u>	<u>Allowance</u>	<u>Receivable</u>
Patient care	\$ 12,172	\$ (3,668)	\$ 8,504
Sponsored agreements	20,514	(1,687)	18,827
Total	<u>\$ 32,686</u>	<u>\$ (5,355)</u>	27,331
Current portion			26,976
Noncurrent portion			<u>\$ 355</u>

	<u>2007</u>		
	<u>Gross</u>		<u>Net</u>
	<u>Receivable</u>	<u>Allowance</u>	<u>Receivable</u>
Patient care	\$ 12,860	\$ (4,278)	\$ 8,582
Sponsored agreements	19,685	(1,414)	18,271
Total	<u>\$ 32,545</u>	<u>\$ (5,692)</u>	26,853
Current portion			26,160
Noncurrent portion			<u>\$ 693</u>

5. Capital Assets, net

Capital assets at historical cost as of June 30, 2008 and 2007 are summarized as follows (in thousands):

	<b>2008</b>				
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Retire- ments</b>	<b>Transfers (to)/ from Affiliates</b>	<b>Ending Balance</b>
<b>Cost - Non depreciable</b>					
Construction in progress	\$ 1,935	\$ 21,733		\$ (95)	\$ 23,573
Subtotal	1,935	21,733	\$ -	(95)	23,573
<b>Cost - Depreciable</b>					
Building	19,223	-	-	8	19,231
Equipment	37,504	5,399	(220)	70	42,753
Library materials	19	5	-	20	44
Subtotal	56,746	5,404	(220)	98	62,028
Total capital assets - cost	58,681	27,137	(220)	3	85,601
<b>Accumulated depreciation</b>					
Buildings	644	482	-	-	1,126
Equipment	17,398	6,682	(126)	2	23,956
Library materials	10	4	-	-	14
Subtotal	18,052	7,168	(126)	2	25,096
Capital assets, net	\$ 40,629	\$ 19,969	\$ (94)	\$ 1	\$ 60,505
<b>2007</b>					
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Retire- ments</b>	<b>Transfers (to)/ from Affiliates</b>	<b>Ending Balance</b>
<b>Cost - Non depreciable</b>					
Construction in progress	\$ 290	\$ 2,235		\$ (590)	\$ 1,935
Subtotal	290	2,235	\$ -	(590)	1,935
<b>Cost - Depreciable</b>					
Building	18,418	524	-	281	19,223
Equipment	29,037	8,768	(371)	70	37,504
Library materials	30	10	-	(21)	19
Subtotal	47,485	9,302	(371)	330	56,746
Total capital assets - cost	47,775	11,537	(371)	(260)	58,681
<b>Accumulated depreciation</b>					
Buildings	169	473	-	2	644
Equipment	11,265	6,380	(252)	5	17,398
Library materials	8	2	-	-	10
Subtotal	11,442	6,855	(252)	7	18,052
Capital assets, net	\$ 36,333	\$ 4,682	\$ (119)	\$ (267)	\$ 40,629

6. Other Liabilities

Other liabilities of the Research Foundation consisted of the following at June 30, 2008 (in thousands):

	2008					
	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retire-ments</u>	<u>Ending Balance</u>	<u>Current Portion</u>	<u>Noncurrent Portion</u>
Other long-term liabilities	-	1,562	-	1,562	529	1,033
Total	<u>\$ -</u>	<u>\$ 1,562</u>	<u>\$ -</u>	<u>\$ 1,562</u>	<u>\$ 529</u>	<u>\$ 1,033</u>

Other long-term liabilities as of June 30, 2008, consist of the Research Foundation's portion of other post-employment benefits, as discussed in Note 10 – Post Employment Healthcare Benefits. The current portion is included in accounts payable and accrued liabilities in the statements of net assets as of June 30, 2008.

7. Revenues From Clinical Services

a. Clinics and Laboratories

The University's School of Medicine operates various clinics, which generate revenues from the treatment of patients, as well as laboratory services. Revenues associated with the operations of these clinics totaled approximately \$70.9 million and \$67.9 million for the years ended June 30, 2008 and 2007, respectively.

b. University of Louisville School of Medicine Practice Plan (the Plan)

The Plan requires each clinical department of the University of Louisville School of Medicine to establish a departmental entity, which bears the financial obligation pursuant to the Plan. The departmental entity must receive contributions from the faculty practice groups and remit the contributions as specified in the Plan.

The faculty practice groups remit funds in two forms. The first portion, Academic Program Support, as defined in the Plan, is remitted directly to the Research Foundation to support the academic programs in the clinical departments. Academic Program Support remitted to the Research Foundation totaled approximately \$27.1 million and \$21.1 million for the years ended June 30, 2008 and 2007, respectively. The second portion, the Dean's Fund, as defined in the Plan, is collected by the University of Louisville Medical School Fund (Medical School Fund) from the departmental entities and is used by the Dean to provide additional support for the clinical, academic programs and other activities of the Medical School. Amounts remitted to the Research Foundation by the Medical School Fund totaled approximately \$3.5 million and \$3.6 million for the years ended June 30, 2008 and 2007, respectively.

c. University Medical Center, Inc. Affiliation Agreement

Effective February 6, 1996, the University entered into an affiliation agreement with Jewish Hospital Healthcare Services, Inc., now Jewish Hospital and St. Mary's Healthcare Services, Inc. (Jewish Hospital); Alliant Health System, Inc., now Norton Healthcare Inc, (Norton); and University Medical Center, Inc. (UMC) for the joint operation of the University of Louisville Hospital (the Hospital). The initial term of the affiliation agreement is 15 years with renewal

periods as defined in the agreement. Effective June 15, 1997, an amendment to the affiliation agreement constituted an exercise of the first of three potential five-year renewal terms permitted by the February 6, 1996 agreement. Effective July 1, 2007, Jewish Hospital and Norton withdrew from the affiliation agreement.

This agreement calls for, among other things, UMC to provide funding (salary, benefits, and malpractice coverage) for certain full-time equivalent resident positions over the term of the affiliation agreement. Funding for residents will be a budget item annually determined and will take into account (a) staffing at comparable academic medical centers, (b) the services provided by the Hospital, and (c) the clinical load at the Hospital and related facilities. Funding from the Hospital for the years ended June 30, 2008 and 2007 was approximately \$25.0 million and \$23.3 million, respectively, is included in clinical services revenue. This agreement addresses the patient care needs of the Hospital's inpatients.

d. University Physicians' Group, Inc. (UPG)

Faculty of the School of Medicine also participate in UPG. UPG was established to operate the outpatient services located in the ambulatory care building on a more coordinated basis. The University historically had operated certain clinics, including the Primary Care Center, in the ambulatory care building. UPG assumed the budgetary responsibility and became the legal operator of the clinics in August 1999. On July 1, 2003, UPG transferred its clinical operations to the Medical School Practice Association (MSPA) doing business as University Physician Associates. At the same time, certain funding from the UMC affiliation agreement was transferred to the MSPA, along with funding received from the Medicaid HMO, Passport Health Plan (safety net funding).

The Medical School Fund, UMC, UPG, and MSPA are legally distinct organizations with separate governing bodies. Their financial statements are not included with those of the Research Foundation.

e. Other Clinical Revenues

The Research Foundation works with other area hospitals by providing support services, such as residents and other staff. Revenues associated with these activities totaled approximately \$34.0 million and \$28.4 million for the years ended June 30, 2008 and 2007, respectively.

8. Expenses

Operating expenses by natural classification for the years ended June 30, 2008 and 2007 were approximately (in thousands):

	<u>2008</u>	<u>2007</u>
Salaries and wages	\$ 157,182	\$ 147,801
Employee benefits	34,157	30,474
Supplies and services	101,133	94,617
Depreciation	7,168	6,855
Scholarships and fellowships	31,424	28,875
	<u>\$ 331,064</u>	<u>\$ 308,622</u>

9. Retirement Plan

University personnel participate in a contributory retirement plan. The Research Foundation recorded expenses related to the defined contribution plan of approximately \$9.1 million and \$8.4 million during the years ended June 30, 2008 and 2007, respectively.

10. Postemployment Healthcare Benefits

a. Plan Description

University personnel are eligible for postemployment healthcare benefits as described in The University of Louisville Group Health Plan (Plan), administered by the University. To be eligible for the Plan, a retired employee must be the earlier of the attainment of age 60 with seven years of service in eligible faculty or staff status, or the date that the sum of the employees age and years of regular service of not less than 80% full-time equivalent at the University equals or exceeds 75.

b. Funding Policy

The Plan is funded on a pay-as-you-go basis. During the year ended June 30, 2008, the University contributed approximately \$1.0 million, approximately 50 percent of total premiums. Retired Plan members under age 65 receiving benefits contributed approximately \$1.0 million, approximately 50 percent of total premiums, through their required monthly contributions according to the following schedule:

	<u>PPO</u>	<u>EPO</u>	<u>HRA High</u>	<u>HRA Low</u>	<u>Out of Area</u>
Employee	\$ 270	\$ 304	\$ 178	\$ 119	\$ 286
Employee and Spouse	\$ 581	\$ 653	\$ 431	\$ 321	\$ 586

Medicare-eligible retirees receive a monthly benefit of \$108 per individual covered. For the year ended June 30, 2008, the University contributed \$1.0 million for Medicare-eligible retirees.

c. Annual Other Postemployment Benefit (OPEB) Cost and Net OPEB Obligation

The University's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45 – *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (GASB Statement No. 45). The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial accrued liabilities (AAL) over a period not to exceed thirty years. The table on the following page shows the components of the University's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the University's net OPEB obligation (in thousands):

	<b>2008</b>
Normal Cost	\$ 4,687
AAL Amortization	3,427
Interest on above	243
Annual Required Contribution	<u>8,357</u>
Contributions made	(2,020)
Increase in net OPEB obligation	<u>6,337</u>
Net OPEB obligation - beginning of year	-
Net OPEB obligation - end of year	<u><u>6,337</u></u>

The University's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the fiscal year ended June 30, 2008 were as follows:

Fiscal Year Ended June 30,	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2008	\$ 8,357	24%	\$ 6,337

The University allocates a portion of the ARC, and the corresponding OPEB obligation, to its affiliated corporations, including the Research Foundation. For the year ended June 30, 2008, the Research Foundation's portion of the ARC was \$1.6 million. As of June 30, 2008, the Research Foundation's net OPEB obligation was \$1.6 million, of which \$1.0 million was recorded in other long term liabilities and \$0.6 million was recorded in accounts payable and accrual liabilities.

d. Funded Status and Funding Progress

As of July 1, 2007, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability for benefits was \$69.2 million and there were no assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$69.2 million. The covered payroll (annual payroll of active employees covered by the plan) was \$345.6 million, and the ratio of the UAAL to the covered payroll was 20 percent.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents information about whether the actuarial value of plan assets is increasing or decreasing relative to the actuarial accrued liabilities for benefits.

e. Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs

between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the July 1, 2007, actuarial valuation, the unit credit method actuarial cost method was used. The actuarial assumptions included a 3.0 percent investment rate of return (net of administrative expenses) which is based on the estimated return on the University's general assets, and an annual healthcare cost trend rate of 10 percent initially, reduced by decrements to an ultimate rate of 5 percent after 10 years. The UAAL is being amortized on a straight line basis over 30 years. The remaining amortization period at June 30, 2008 was 29 years.

## 11. Commitments and Contingencies

### a. Commitments

At June 30, 2008 and 2007, respectively, the Research Foundation had approximately \$6.2 million and \$5.4 million in encumbrances outstanding for future expenditures.

### b. Litigation

The University has been named as defendant in several lawsuits, including several actions initiated by patients involving alleged malpractice. It is the opinion of management and its legal counsel, based in part on the doctrine of sovereign immunity, commercial insurance coverage's and other statutory provisions, that the ultimate outcome of litigation will not have a material effect on the future operations or financial position of the University or the Research Foundation beyond the amounts already provided.

### c. Government Grants

The Research Foundation is currently participating in numerous grants from various departments and agencies of the federal and state governments. The expenditures of grant proceeds must be for allowable and eligible purposes. Single audits and audits by the granting department or agency may result in requests for reimbursement of unused grant proceeds or disallowed expenditures. Upon notification of final approval by the granting department or agency, the grants are considered closed.

**REQUIRED SUPPLEMENTARY INFORMATION**  
**Schedule of Funding Progress by the University**  
**For Other Postemployment Benefits**  
**(in thousands)**

<b>Actuarial Value Date</b>	<b>Actuarial Value of Assets (a)</b>	<b>Actuarial Accrued Liability (AAL) (b)</b>	<b>Unfunded AAL (UAAL) (b - a)</b>	<b>Funded Ratio (a/b)</b>	<b>Covered Payroll (c)</b>	<b>UAAL as a Percentage of Covered Payroll ((b-a) / c)</b>
7/1/2007	\$ -	\$ 69,179	\$ 69,179	0%	\$ 345,636	20%