

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

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

**Accountants' Report and Financial Statements  
June 30, 2011 and 2010**

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

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

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

Board of Directors  
University of Louisville Research Foundation, Inc.  
Louisville, Kentucky

We have audited the accompanying basic financial statements of the University of Louisville Research Foundation, Inc. (Research Foundation), a component unit of the University of Louisville, 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 Research Foundation'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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Research Foundation 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.

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

*BKD, LLP*

September 28, 2011

# **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, 2011, 2010, and 2009. 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, 2011, total awards were \$145.6 million, a decrease of \$36.5 million or 25%, as compared to fiscal year 2010. The decrease is attributed to federal grant stimulus supplements in fiscal year 2010 that were not available in the current fiscal year ended June 30, 2011. Some of the funding highlights include:

- \$4.5 million from the U.S. Department of Education to support the National Research Center on Career and Technical Education.
- \$1.6 million from the Center for Disease Control for the Development of a Neural Recovery Rehabilitation and Research Center.
- \$1.5 million from the National Institutes of Health for the study of Molecular Determinants of Developmental Defects.
- \$1.3 million to study the Novel Use of Clinical Drugs to Prevent Major Eye Injury Associated Complication.
- \$1.3 million from the U.S. Office of Naval Research for Additive Manufacturing Research.

The Research Foundation continues to expand its research base by promoting collaborative research efforts within the University. Additional funds of \$9.8 million were secured in fiscal year 2010 from a National Institute for Health (NIH) award to expand the Center for Predictive Medicine, which was placed in service in fiscal year 2009. Total additional space exceeds a third of the current space and will be placed into service in fiscal year 2012.

The University of Louisville supports these research missions by providing the capital investments needed to complete the research. The Clinical Translational Research Building, which was the first research building in Kentucky to receive the Gold Leadership in Energy and Environmental Design (LEED) certification, houses 5 floors of biomedical research labs including 4 Biosafety Level 3 labs. The investigators housed in the 288,000 square-foot Clinical and Translational Research Building pursues clinically relevant translational and interdisciplinary research.

## Financial Highlights

- The Research Foundation's financial position remains strong at June 30, 2011, with total assets of \$174.8 million and liabilities of \$34.2 million as compared to June 30, 2010 at \$162.4 million of total assets and \$39.0 million of liabilities. Net assets, which represent the residual interest in the Research Foundation's assets after liabilities are deducted, were \$140.6 million and \$123.4 million for the years ended June 30, 2011 and 2010, respectively.
- The Research Foundation's total liabilities of \$34.2 million consist primarily of deferred revenue. Deferred revenue represents the unearned portion of grants and sponsored programs and comprises \$16.7 million or 49% of total liabilities.
- Operating revenues amounted to \$333.9 million and \$316.8 million and operating expenditures were \$343.4 million and \$348.7 million resulting in a net operating loss of \$9.5 million and \$31.9 million for the years ended June 30, 2011 and 2010, respectively. When adjusted for net nonoperating revenues of \$26.8 million and \$29.9 million, respectively, net assets of the Research Foundation increased by \$17.2 million and decreased by \$2.0 million for the years ended June 30, 2011, and 2010, 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, Pell and similar nonexchange grants, and investment income (loss) are considered nonoperating, as defined by GASB Statement No. 35. The Research Foundation's nonoperating revenues consist mainly of \$38.6 million and \$37.2 million in nonexchange grants and contract revenue for the years ended June 30, 2011 and 2010, respectively. These revenues relate to nonexchange 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 \$16.7 million and \$16.9 million for the fiscal years ended June 30, 2011 and 2010, respectively.
- Capital assets are depreciated and reported net of accumulated depreciation. The Research Foundation's capital assets as of June 30, 2011 and 2010 consist primarily of equipment and library materials with a net asset value of \$78.0 million and \$74.9 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, 2011, 2010, and 2009 is summarized below:

### Condensed Statements of Net Assets June 30, 2011, 2010, and 2009 (In Thousands)

	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2011 - 2010</u> <u>Change</u>	<u>2010 - 2009</u> <u>Change</u>
<b>ASSETS</b>					
Current assets	\$ 96,421	\$ 83,379	\$ 76,330	\$ 13,042	\$ 7,049
Capital assets	78,030	74,860	73,952	3,170	908
Other noncurrent assets	390	4,191	3,940	(3,801)	251
Total assets	<u>174,841</u>	<u>162,430</u>	<u>154,222</u>	<u>12,411</u>	<u>8,208</u>
<b>LIABILITIES</b>					
Current liabilities	27,652	29,767	24,020	(2,115)	5,747
Noncurrent liabilities	6,554	9,221	4,771	(2,667)	4,450
Total liabilities	<u>34,206</u>	<u>38,988</u>	<u>28,791</u>	<u>(4,782)</u>	<u>10,197</u>
<b>NET ASSETS</b>					
Invested in capital assets, net of related debt	78,030	74,491	73,952	3,539	539
Restricted - expendable	2,438	2,133	1,893	305	240
Unrestricted	60,167	46,818	49,586	13,349	(2,768)
Total net assets	<u>\$140,635</u>	<u>\$123,442</u>	<u>\$125,431</u>	<u>\$ 17,193</u>	<u>\$ (1,989)</u>

## Assets

A review of the Research Foundation's statement of net assets at June 30, 2011 indicates that the Research Foundation is highly liquid with only \$6.6 million in long-term liabilities. Of the \$96.4 million in current assets, \$69.5 million, or 72%, consists of cash and cash equivalents. Of the remaining \$26.9 million, \$25.8 million, or 27% 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 increased during the year by \$10.0 million.

Noncurrent assets consist mainly of \$78.0 million of capital assets. 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 \$16.7 million of unexpended cash advances for sponsored research activities. This deferred revenue decreased by less than \$0.3 million

from the fiscal year ended June 30, 2010, due to an increase in cost reimbursable grant. 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 \$11.0 million of current liabilities that are due at June 30, 2011. Other long-term liabilities of \$6.6 million and \$1.3 million included within accounts payable and accrued liabilities at June 30, 2011 relate to the Research Foundation's allocated portion of other post-employment benefits.

### **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, 2011 and 2010 were \$140.6 million and \$123.4 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 - \$78.0 million**

The Research Foundation's \$78.0 million in net capital assets represent construction in progress, buildings, equipment and depreciable library materials, net of accumulated depreciation. There is no debt attributable to the acquisition, construction or improvement of those assets. The \$3.5 million increase over prior year reflects \$12.7 million of capital asset additions, offset by recognition of depreciation expense.

#### **Restricted expendable net assets - \$2.4 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, 2011. The net assets remain restricted until the contract is completed.

Restricted expendable net assets increased \$0.3 million or 1%. As new contracts are awarded it is expected that there will be excess net assets until the contract is fully utilized.

#### **Unrestricted net assets - \$60.2 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.

### **Fiscal Year 2010**

The Research Foundation's financial position as of the fiscal year ended June 30, 2010 shows an increase in assets and an increase in liabilities with an overall decrease in net assets. Assets increased during the fiscal year ended June 30, 2010 by \$8.2 million, or 5%, as compared to the fiscal year ended June 30, 2009. This increase was due mainly to the \$8.0 million increase in cash and cash equivalents and a \$0.9 million increase in capital assets. The increase in liabilities mainly resulted from the increase in long-term liabilities which increased \$4.4 million from the fiscal year ended June 30, 2009 due to the requirement to record other postemployment benefits.

Net assets decreased \$2.0 million, or 2%, compared to net assets at June 30, 2009 due mainly to the \$2.7 million decrease in unrestricted, net assets. This decrease in unrestricted net assets was offset by a \$0.5 million increase in investments in capital assets and a \$0.2 million increase in restricted expendable net assets, as compared to fiscal year ended June 30 2009.

## 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, 2011, 2010, and 2009 is below:

### Condensed Statements of Revenues, Expenses and Changes in Net Assets Years ended June 30, 2011, 2010, and 2009 (In Thousands)

	2011	2010	2009	2011 - 2010 Change	2010 - 2009 Change
<b>OPERATING REVENUES</b>					
Clinical services	\$ 197,124	\$ 179,978	\$ 167,087	\$ 17,146	\$ 12,891
Grants and contracts	107,991	108,873	111,697	(882)	(2,824)
Facilities and administrative cost recoveries	27,582	27,050	24,958	532	2,092
Other operating revenues	1,166	923	667	243	256
Total operating revenues	<u>333,863</u>	<u>316,824</u>	<u>304,409</u>	<u>17,039</u>	<u>12,415</u>
<b>OPERATING EXPENSES</b>					
Depreciation	9,605	8,809	7,791	796	1,018
Other operating expenses	333,828	339,934	309,744	(6,106)	30,190
Total operating expenses	<u>343,433</u>	<u>348,743</u>	<u>317,535</u>	<u>(5,310)</u>	<u>31,208</u>
Operating loss	<u>(9,570)</u>	<u>(31,919)</u>	<u>(13,126)</u>	<u>22,349</u>	<u>(18,793)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>					
Gifts	663	393	6,781	270	(6,388)
Nonexchange grants and contracts	38,563	37,235	31,860	1,328	5,375
Realized and unrealized (gain)/loss on investments	610	326	(1,089)	284	1,415
Transfers	(14,299)	(14,028)	(9,892)	(271)	(4,136)
Other nonoperating revenues	1,226	6,004	45	(4,778)	5,959
(Decrease)/increase in net assets	<u>17,193</u>	<u>(1,989)</u>	<u>14,579</u>	<u>19,182</u>	<u>(16,568)</u>
<b>NET ASSETS</b>					
Net assets, beginning of year	123,442	125,431	110,852	(1,989)	14,579
Net assets, end of year	<u>\$ 140,635</u>	<u>\$ 123,442</u>	<u>\$ 125,431</u>	<u>\$ 17,193</u>	<u>\$ (1,989)</u>

### Operating Revenues

The Research Foundation recognized \$333.9 million in operating revenues for the year ended June 30, 2011. This represents a 5% increase in revenues from the \$316.8 million reported for the year ended June 30, 2010.

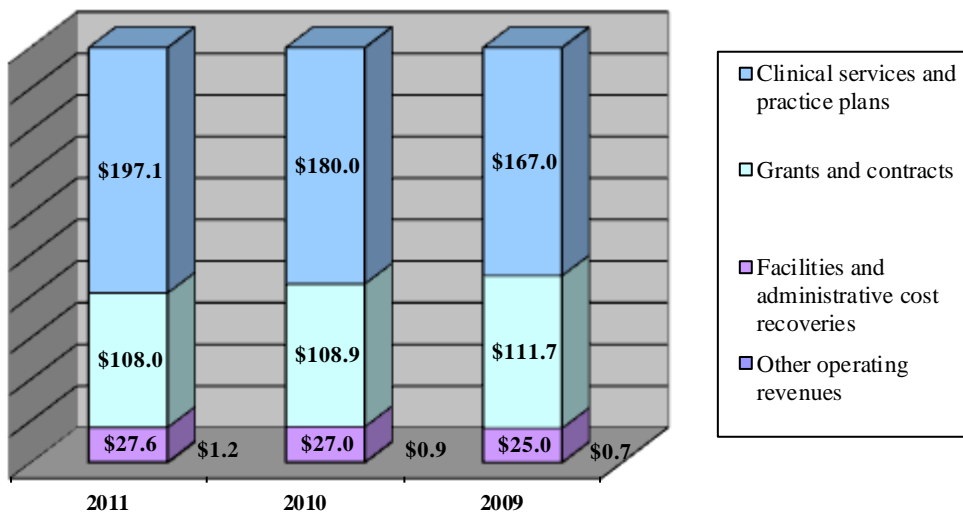
Revenues from clinical services were \$197.1 million for the year ended June 30, 2011. This is an increase of approximately \$17.1 million, or 10%, compared to \$180.0 million in similar revenues reported for the year ended June 30, 2010. The increase in revenues is partially related to a \$3.2 million increase in funds received in the DSH Matched Funds program for the university medicaid program. For the years ended June 30, 2011 and 2010, revenues earned for clinical services are reported net of \$29.1 million and \$28.6 million, respectively, in contractual allowances related to federal, state and private insurance providers.

Revenues from grants and contracts were \$108.0 million for the year ended June 30, 2011 as compared to \$108.9 million in revenues reported in the previous year. The decrease is partially attributable to a \$2.3 million and \$0.4 million reduction in state and local grants and nongovernmental grants, respectively, for the year ended June 30, 2011 as compared to the previous year. The reduction relates to the reduction in the total number of state, local and nongovernmental grants.

Revenue from facilities and administrative cost recoveries were \$27.6 million and \$27.1 million for the years ended June 30, 2011 and 2010, 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. 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, 2011 and 2010, approximately \$11.2 million and \$11.4 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, 2011, 2010, and 2009 (in millions).

**Operating Revenues  
Years Ended June 30, 2011, 2010, and 2009**

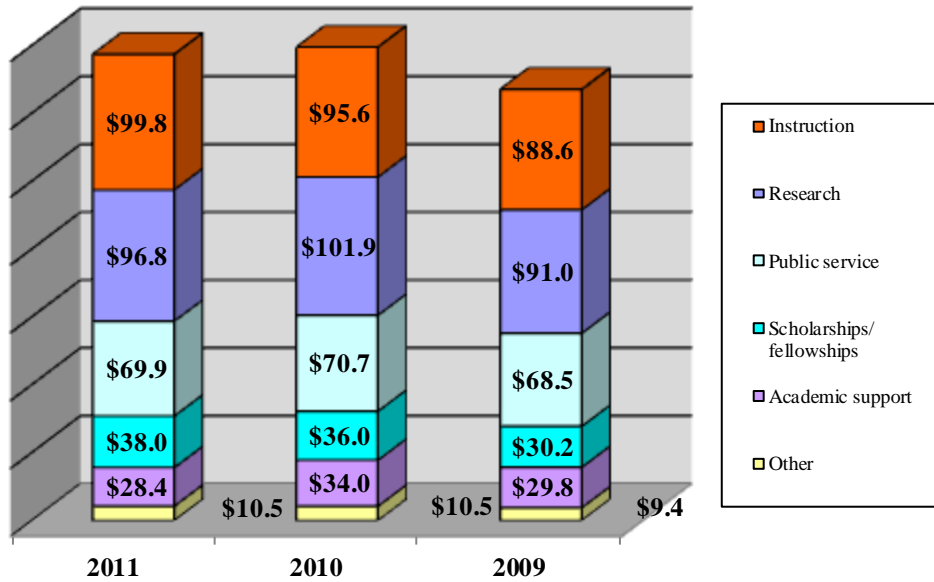


**Operating Expenses by Functional and Natural Class**

Total operating expenses were \$343.4 million and \$348.7 million for the fiscal years ended June 30, 2011 and 2010, respectively. The decrease of \$5.3 million, or 2%, is mainly related to an overall decrease of \$4.2 million in clinical expenses. Most notable is a \$5.6 million decrease in expenses related to academic support which is mostly made up of a \$5.7 million decrease in indigent care expenses funded by Passport.

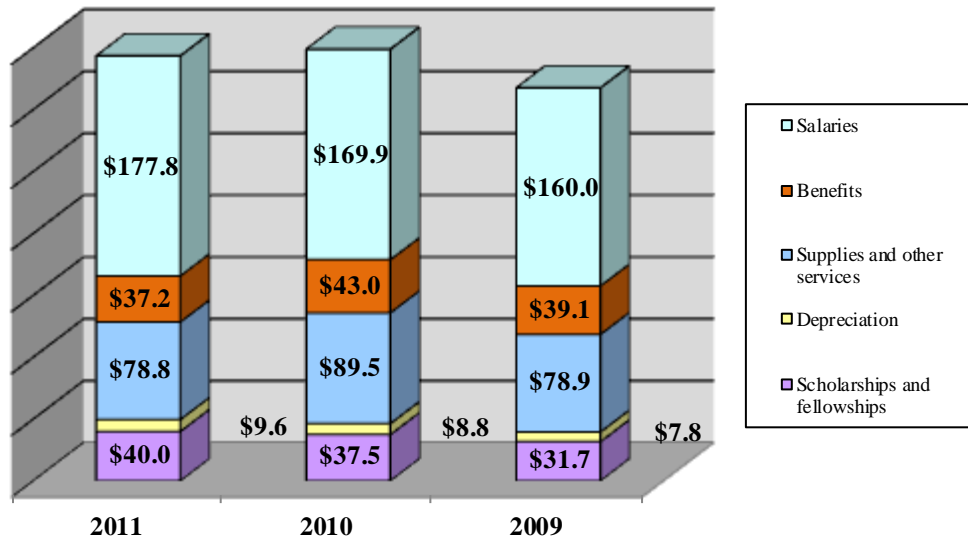
The following is a graphic illustration of total operating expenses by function for the years ended June 30, 2011, 2010 and 2009 (in millions):

**Operating Expenses by Functional Classification**  
**Years ended June 30, 2011, 2010, and 2009**



The following is a graphic illustration of total operating expenses by natural classification for the years ended June 30, 2011, 2010 and 2009 (in millions):

**Operating Expens by Natural Classification**  
**Years ended June 30, 20101, 2010, and 2009**



## **Nonoperating Revenues (Expenses)**

The Research Foundation's total nonoperating revenues of \$26.8 million for fiscal year ended June 30, 2011, was mostly comprised of nonexchange grants and contract revenues of \$38.6 million and transfer expenses of \$14.3 million. Included in the transfers total was an \$11.2 million transfer to the University, related to the facilities and administrative revenue, for administrative expenses incurred for sponsored research. Total nonoperating revenues decreased by \$3.2 million as compared to fiscal year ended June 30, 2010. There was a decrease of \$4.8 million related to other nonoperating revenues. In the fiscal year ended June 30, 2010 the Research Foundation recognized revenue received from the Internal Revenue Service relating to social security and medicare taxes paid on medical residents' compensation.

### **Fiscal Year 2010**

For the year ended June 30, 2010, Research Foundation reported \$316.8 million in operating revenues. This was a 4% increase compared to the \$304.4 million reported for the year ended June 30, 2009.

Revenues from clinical services were \$180.0 million for fiscal year 2010, an increase of 8% from the fiscal year ended June 30, 2009. The increase in revenues is partially related to a \$4.8 million increase in funds received in increased billings from the Kidney Dialysis Program. Revenues from grants and contracts were \$108.9 million during the fiscal year ended June 30, 2010 a \$2.8 million decrease from the fiscal year ended June 30, 2009. The decrease is primarily attributable to a reduction in the number of federal, state, and local grants.

Revenue from facilities and administrative cost recoveries was \$27.1 million and \$25.0 million for years ended June 30, 2010 and 2009, 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. 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, 2010 and 2009, approximately \$11.4 million and \$11.1 million, respectively, were transferred to the University for this purpose.

Total operating expenses were \$348.7 million and \$317.5 million for the years ended June 30, 2010 and 2009, respectively. The increase of \$31.2 million, or 10%, is mainly related to the \$14.4 million increase in clinical expenses. The increase is mostly related to the \$7.0 million increase in expenses related to instruction which is mostly made up of a \$5.9 million increase in employee salaries.

### **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. Condensed statements of the Research Foundation's cash flows for the years ended June 30, 2011, 2010, and 2009, are summarized on the following page:

**Condensed Statements of Cash Flows**  
**Years ended June 30, 2011, 2010, and 2009**  
(In Thousands)

	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2011 - 2010</u> <u>Change</u>	<u>2010 - 2009</u> <u>Change</u>
Cash provided/(used) by:					
Operating activities	\$ (7,380)	\$ (11,646)	\$ 3,666	\$ 4,266	\$ (15,312)
Noncapital and related financing activities	26,175	29,203	28,765	(3,028)	438
Capital financing activities	(13,072)	(9,601)	(21,066)	(3,471)	11,465
Investing activities	4,310	-	-	4,310	-
Net increase in cash	<u>10,033</u>	<u>7,956</u>	<u>11,365</u>	<u>2,077</u>	<u>(3,409)</u>
Cash and cash equivalents, beginning of year	<u>59,443</u>	<u>51,487</u>	<u>40,122</u>	<u>7,956</u>	<u>11,365</u>
Cash and cash equivalents, end of year	<u>\$ 69,476</u>	<u>\$ 59,443</u>	<u>\$ 51,487</u>	<u>\$ 10,033</u>	<u>\$ 7,956</u>

### Operating Activities

The Research Foundation operating activities used approximately \$7.4 million in net cash in the fiscal year ended June 30, 2011, due mainly to a \$6.8 million increase in cash related to grants and contracts. Clinics overall cash used increased by \$3.0 million as compared to fiscal year ended June 30, 2010, due mainly to a \$3.2 million increase in Medicaid funding for indigent care. The cash used by operating activities decreased by \$4.3 million as compared to the fiscal year ended June 30, 2010. Cash outflows from operations during the fiscal year ended June 30, 2011 increased due largely to expenses related to payments to employees, which increased \$8.3 million, and payments for scholarships and fellowships, which increased \$2.5 million, as compared to the fiscal year ended June 30, 2010.

### Other Activities

The \$26.2 million cash provided by noncapital and related financing activities relates mainly to the \$38.7 million provided by nonexchange grants. It also includes the Research Foundation's payment of \$11.2 million to the University as reimbursement for indirect charges to support the use of buildings and labs. In total, cash provided by noncapital and related financing had a \$3.0 million decrease from the fiscal year ended June 30, 2010, as transfers to the University were offset by the nonexchange grant cash receipts.

Cash used for capital financing activities increased \$3.5 million to \$13.1 million during the fiscal year ended June 30, 2011, due to an increase in the amount of capital assets purchased. Cash provided from investing activities was \$4.3 million during the fiscal year ended June 30, 2011, due to the sale of investments held with the University of Louisville Foundation.

### Fiscal Year 2010

The Research Foundation's cash and cash equivalents increased by \$8.0 million during the fiscal year ended June 30, 2010. The Research Foundation's operating activities used approximately \$11.7 million in net cash due mainly to a \$17.8 million increase in cash related to clinics. Grants and contracts overall cash use decreased by \$12.1 million as compared to fiscal year ended June 30, 2009, due mainly to the overall reduction in grants and contracts for the year ended June 30, 2010. Total cash received from operations was \$320.2 million, which was an \$8.0 million increase from the fiscal year ended June 30, 2009. The cash increase is mostly due to a \$17.8 million increase in cash generated from clinical services, in the fiscal year ended June 30, 2010.

Cash outflows from operations during the fiscal year ended June 30, 2010, were \$331.8 million. This was an increase of \$23.3 million as compared to the fiscal year ended June 30, 2009. The increase in cash outflows is largely due to a \$9.1 million and \$8.7 million increase in the Research Foundation's expenses related to salaries and supplies, respectively, during the fiscal year ended June 30, 2010, as compared to the prior year.

The \$29.2 million of cash provided for noncapital and related financing activities relates mainly to the \$36.6 million received from nonexchange grants and includes the Research Foundation's payment of \$11.4 million to the University as reimbursement for indirect charges to support the use of buildings and labs. Also included was the \$0.4 million in cash received related to gifts, which was a \$6.4 million decrease when compared to the \$6.8 million of cash received for gifts in the fiscal year ended June 30, 2009. Cash used for capital financing activities was \$9.6 million, representing the purchase of capital equipment, a 54% decrease from the fiscal year ended June 30, 2009.

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

As mandated by House Bill 1, the University is to become a premier, nationally recognized metropolitan research university. The next important step towards achieving that mandate was introduced in Fall 2008. The 2020 Plan is the blueprint for the University to achieve preeminence by year 2020. This plan was drafted after the Board of Trustees instructed President James R. Ramsey to aggressively move ahead towards the next level in the University's pursuit of excellence.

Since launching the 2020 Plan, the University has faced many other challenges that have impacted campus operations. Since the first year of the 2008-10 biennial budget, the University has sustained state-mandated recurring budget reductions each year, including a new \$2 million reduction in the fiscal year 2012 operating budget. Overall, since 2008, recurring state reductions total \$56.4 million. In addition, in fiscal year 2009, a state-mandated, non-recurring mid-year budget reduction of \$3.2 million was implemented. This \$3.2 million was made recurring for fiscal year 2010 and beyond.

The 2010-12 biennial budget passed by the 2010 General Assembly in May 2010 reflected a net 1.0 percent reduction, or \$2.0 million, in state support for the University in fiscal year 2012. The budget was subsequently amended by the 2011 General Assembly in March 2011 to increase the University's state support by \$2.9 million in fiscal year 2011 and reduced state support by the same amount in fiscal year 2012. This movement of funds was necessary for the Commonwealth to meet the federal maintenance of effort requirements for the Education Jobs Fund program. As a result of these actions, the University's state support for fiscal year 2011, including the federal State Fiscal Stabilization Funds was \$164.1 million and the University's fiscal year 2012 state support is expected to be \$175.6 million.

On top of the continued reductions in state appropriation, available spending on many of the University's endowments has declined as a result of the economic and financial market downturn. Though the value of the University's endowment rebounded some during 2010, continuing economic concerns may erode some of these gains.

The University will not use the current fiscal environment and challenges as an excuse to step back from its House Bill 1 mandates but will instead find other ways to maintain the momentum and continue progress towards achieving its strategic goals and mandates. In its quest for preeminence, the University cannot 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.

The tangible expression of the University's plan to diversify revenue streams and lessen the effects of uncertain business cycles may be found in the business model entitled, "Business Plan 2020". This

plan was developed by Leadership and various constituencies. It is intended to complement the broader vision set forth by the 2020 Plan with the intent of creating the underpinning financial structure necessary to successfully implement the 2020 Plan. An important outcome of “Business Plan 2020” is the ability of leadership to synthesize data and develop a cogent seven-point business strategy to guide the University through the tough and uncertain fiscal environment.

The seven-strategies of the “Business Plan 2020” and some examples include:

- Reengineer operations – The recent energy performance contract with Siemens, Inc. will enable the University to update energy systems and save money.
- Utilize underperforming assets – Continued development of the Shelby Campus includes a proposal for UofL Physicians (ULP) building.
- Increase fundraising – The “Charting Our Course” campaign aims to raise \$750 million in private support by 2013.
- Expand clinical activities – Cardinal Care continues to enjoy broad participation in its health plans, and recent benefit enhancements provide incentive for further growth.
- Develop partnerships – The Nucleus project will work with Signature HealthCARE to develop an International Center for Long-Term Care at the Haymarket site.
- Improve contract research/commercialization – The University provides flexible employment options for faculty members participating in Small Business Innovation Research activities, benefiting the community and the University.
- Be creative – Using Tax-Increment Financing (TIF) to help fund the downtown life sciences research park.

This financial report is designed to provide a general overview of the University’s finances and to show the University’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, 2011 and 2010**  
**(In Thousands)**

	<u>2011</u>	<u>2010</u>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 69,476	\$ 59,443
Accounts receivable, net	25,762	22,949
Inventories	473	502
Other assets	710	485
Total current assets	<u>96,421</u>	<u>83,379</u>
Noncurrent Assets:		
Accounts receivable, net	351	452
Investments held with University of Louisville Foundation, Inc.	35	3,731
Other long-term assets	4	8
Capital assets, net	78,030	74,860
Total noncurrent assets	<u>78,420</u>	<u>79,051</u>
Total assets	<u>174,841</u>	<u>162,430</u>
<b>LIABILITIES</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	11,002	12,845
Deferred revenue	16,650	16,922
Total current liabilities	<u>27,652</u>	<u>29,767</u>
Noncurrent Liabilities:		
Other long-term liabilities	6,554	9,221
Total noncurrent liabilities	<u>6,554</u>	<u>9,221</u>
Total liabilities	<u>34,206</u>	<u>38,988</u>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	78,030	74,491
Restricted - expendable for:		
Research	1,297	919
Instruction	469	420
Public service	-	116
Scholarships and fellowships	667	673
Academic support	5	5
Unrestricted	60,167	46,818
Total net assets	<u>\$ 140,635</u>	<u>\$ 123,442</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, 2011 and 2010**  
(In Thousands)

	<u>2011</u>	<u>2010</u>
<b>OPERATING REVENUES</b>		
Clinical services, net of contractual allowances of \$29,142 in 2011 and \$28,614 in 2010	\$ 197,124	\$ 179,978
Federal grants and contracts	90,724	88,983
State and local grants and contracts	9,125	11,375
Nongovernmental grants and contracts	8,142	8,515
Other operating revenue	1,166	923
Facilities and administrative cost recoveries	27,582	27,050
Total operating revenues	<u>333,863</u>	<u>316,824</u>
<b>OPERATING EXPENSES</b>		
Instruction	99,764	95,636
Research	96,761	101,853
Public service	69,904	70,723
Scholarships and fellowships	37,974	36,021
Academic support	28,421	34,032
Institutional support	463	627
Operation and maintenance of plant	536	993
Depreciation	9,605	8,809
Student services	5	49
Total operating expenses	<u>343,433</u>	<u>348,743</u>
Operating loss	<u>(9,570)</u>	<u>(31,919)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Gifts	663	393
Nonexchange grants and contracts	38,563	37,235
Investment loss	-	(28)
Realized and unrealized gain on investments	610	326
Other nonoperating income	1,226	6,032
Net nonoperating revenues	<u>41,062</u>	<u>43,958</u>
Transfers	<u>(14,299)</u>	<u>(14,028)</u>
Total nonoperating revenues	<u>26,763</u>	<u>29,930</u>
Increase/(decrease) in net assets	17,193	(1,989)
<b>NET ASSETS</b>		
Net assets - beginning of year	123,442	125,431
Net assets - end of year	<u>\$ 140,635</u>	<u>\$ 123,442</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, 2011 and 2010**  
(In Thousands)

	<u>2011</u>	<u>2010</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Clinical services	\$ 190,468	\$ 187,449
Grants and contracts	111,533	104,717
Facilities and administrative cost recoveries	27,582	27,050
Other operating revenue	1,166	962
Payments to employees	(177,347)	(169,062)
Payments for benefits	(40,047)	(37,921)
Payments for scholarships and fellowships	(39,967)	(37,480)
Payments to suppliers	(80,768)	(87,361)
Net cash used by operating activities	<u>(7,380)</u>	<u>(11,646)</u>
<b>CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Transfers to related entities	(14,408)	(13,801)
Gifts	663	393
Nonexchange grants and contracts	38,694	36,579
Other noncapital financing activity	1,226	6,032
Net cash provided by noncapital and related financing activities	<u>26,175</u>	<u>29,203</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchases of capital assets	(13,072)	(9,601)
Net cash used by capital and related financing activities	<u>(13,072)</u>	<u>(9,601)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Sales of investments	4,310	-
Net cash provided by investing activities	<u>4,310</u>	<u>-</u>
Net increase in cash and cash equivalents	10,033	7,956
Cash and cash equivalents - beginning of year	59,443	51,487
Cash and cash equivalents - end of year	<u>\$ 69,476</u>	<u>\$ 59,443</u>
<b>RECONCILIATION OF OPERATING (LOSS)/INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating loss	\$ (9,570)	\$ (31,919)
Adjustments to reconcile operating loss to net cash (used)/provided by operating activities:		
Depreciation	9,605	8,809
Loss on disposal of equipment	37	26
Changes in assets and liabilities:		
Accounts receivable, net	(2,843)	1,611
Inventories	29	(81)
Other assets	(225)	80
Accounts payable and accrued liabilities	(1,474)	3,634
Deferred revenue	(272)	1,744
Other long-term liabilities	(2,667)	4,450
Net cash used by operating activities	<u>\$ (7,380)</u>	<u>\$ (11,646)</u>
<b>NONCASH TRANSACTIONS</b>		
Transfer of assets from/(to) University of Louisville	<u>\$ 109</u>	<u>\$ (227)</u>
Capital asset additions in accounts payable	<u>\$ -</u>	<u>\$ 369</u>

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, 2011 and 2010**

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.

The financial statements of the Research Foundation can be found at the following:  
<http://louisville.edu/finance/controller/finst>

b. Cash and Cash Equivalents

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 receivables relate to sponsored programs that support the Research Foundation. Accounts receivable are 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 Research Foundation's statements of net assets.

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 Pell and other grants and contracts, 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. Deferred Revenue

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 \$16.7 million and \$16.9 million at June 30, 2011 and 2010, respectively, are recorded in the Research Foundation's financial statements as deferred revenue.

j. Compensated Absences

Research Foundation policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as vacation or sick benefits are earned, whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay and termination 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.

k. 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.

1. 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.

m. 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.

n. Use of Estimates

The preparation of the 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.

o. Reclassifications

Certain 2010 amounts have been reclassified to conform to the 2011 presentation. These reclassifications had no effect on the change in net assets.

2. Cash and Investments

The Research Foundation maintains various investments and deposits. Investment securities are exposed to various risks, such as interest rate, market, and credit 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 changes could materially affect the investment amounts reported in the statements of net assets. The following sections discuss the risks related to deposits and investments held by the Research Foundation.

a. Custodial Credit Risk

Custodial credit risk for deposits is the risk that in the event of a bank failure, the Research Foundations' deposits or collateral securities may not be returned to it. 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 commercial banks and the Commonwealth of Kentucky (the Commonwealth) as its depositories. Deposits with commercial banks are substantially covered by federal depository insurance or collateral held by the bank in the University's name. 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 in the Commonwealth's name.

b. Interest Rate Risk

Interest rate risk is the risk a government may face should interest rate variances affect the fair value of investments. The Research Foundation had no investments subject to interest rate risk at June 30, 2011 and 2010.

c. Credit Risk

Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. Total investments held by the Foundation were less than \$0.1 million and \$3.7 million for the years ended June 30, 2011 and 2010, respectively. Investments held by the Foundation are considered pooled investments and not rated as to credit risk.

d. 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, 2011 and 2010 was as follows:

	<u>2011</u>	<u>2010</u>
Investment in partnerships	54%	54%
Mutual funds	11%	12%
Marketable alternatives	19%	19%
Preferred and common stock	12%	10%
Corporate bonds	3%	4%
Certificate of deposit	1%	1%
	<u>100%</u>	<u>100%</u>

The Foundation's investments do not have a significant concentration of credit risk within any industry or specific institution.

e. Foreign Currency Risk

This risk relates to adverse affects on the fair value of an investment from changes in exchange rates. The Research Foundation had no investments denominated in foreign currency at June 30, 2011 or 2010.

3. 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 \$11.2 million and \$11.4 million for the years ended June 30, 2011 and 2010, respectively.

b. University of Louisville Foundation, Inc

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 less than \$0.1 million and \$3.7 million for the years ended June 30, 2011 and 2010, respectively, for investment purposes.

4. Accounts Receivable, net

Accounts receivable, net as of June 30, 2011 and 2010 are summarized as follows (in thousands):

	<b>2011</b>		
	<b>Gross</b>		<b>Net</b>
	<b>Receivable</b>	<b>Allowance</b>	<b>Receivable</b>
Patient care	\$ 12,599	\$ (2,537)	\$ 10,062
Sponsored agreements	18,353	(2,302)	16,051
Total	<u>\$ 30,952</u>	<u>\$ (4,839)</u>	26,113
Current portion			25,762
Noncurrent portion			<u>\$ 351</u>

	<b>2010</b>		
	<b>Gross</b>		<b>Net</b>
	<b>Receivable</b>	<b>Allowance</b>	<b>Receivable</b>
Patient care	\$ 12,393	\$ (4,153)	\$ 8,240
Sponsored agreements	17,496	(2,335)	15,161
Total	<u>\$ 29,889</u>	<u>\$ (6,488)</u>	23,401
Current portion			22,949
Noncurrent portion			<u>\$ 452</u>

5. Capital Assets, net

Capital assets at historical cost as of June 30, 2011 and 2010 are summarized as follows (in thousands):

	2011				Ending Balance
	Beginning Balance	Additions	Retire- ments	Transfers (to)/ from Affiliates	
<b>Cost - Non depreciable</b>					
Construction in progress	\$ 1,065	\$ 1,908		\$ (1,492)	\$ 1,481
Subtotal	1,065	1,908		(1,492)	1,481
<b>Cost - Depreciable</b>					
Building	56,892	444		973	58,309
Land improvements	230	-		-	230
Equipment	58,219	10,351	\$ (597)	(80)	67,893
Leasehold improvements	-	-	-	702	702
Library materials	45	-	-	-	45
Subtotal	115,386	10,795	(597)	1,595	127,179
Total capital assets - cost	116,451	12,703	(597)	103	128,660
<b>Accumulated depreciation</b>					
Buildings	3,138	1,443	-	5	4,586
Land improvements	4	5	-	-	9
Equipment	38,427	7,801	(560)	(11)	45,657
Leasehold improvements	-	352	-	-	352
Library materials	22	4	-	-	26
Subtotal	41,591	9,605	(560)	(6)	50,630
Capital assets, net	\$ 74,860	\$ 3,098	\$ (37)	\$ 109	\$ 78,030
<b>2010</b>					
	Beginning Balance	Additions	Retire- ments	Transfers (to)/ from Affiliates	Ending Balance
<b>Cost - Non depreciable</b>					
Construction in progress	\$ 4,966	\$ 2,069		\$ (5,970)	\$ 1,065
Subtotal	4,966	2,069		(5,970)	1,065
<b>Cost - Depreciable</b>					
Building	51,106	478		5,308	56,892
Land improvements	-	6		224	230
Equipment	50,689	7,416	\$ (191)	305	58,219
Library materials	44	1	-	-	45
Subtotal	101,839	7,901	(191)	5,837	115,386
Total capital assets - cost	106,805	9,970	(191)	(133)	116,451
<b>Accumulated depreciation</b>					
Buildings	1,794	1,344	-	-	3,138
Land improvements	-	4	-	-	4
Equipment	31,041	7,457	(165)	94	38,427
Library materials	18	4	-	-	22
Subtotal	32,853	8,809	(165)	94	41,591
Capital assets, net	\$ 73,952	\$ 1,161	\$ (26)	\$ (227)	\$ 74,860

6. Other Liabilities

Other liabilities of the Research Foundation consisted of the following at June 30, 2011 and 2010 (in thousands):

	2011					
	<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	\$ 11,016	\$ (2,246)	\$ (897)	\$ 7,873	\$ 1,319	\$ 6,554
Total	<u>\$ 11,016</u>	<u>\$ (2,246)</u>	<u>\$ (897)</u>	<u>\$ 7,873</u>	<u>\$ 1,319</u>	<u>\$ 6,554</u>

	2010					
	<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	\$ 6,117	\$ 5,494	\$ (595)	\$ 11,016	\$ 1,795	\$ 9,221
Total	<u>\$ 6,117</u>	<u>\$ 5,494</u>	<u>\$ (595)</u>	<u>\$ 11,016</u>	<u>\$ 1,795</u>	<u>\$ 9,221</u>

Other long-term liabilities as of June 30, 2011 and 2010, consist of the Research Foundation's portion of other postemployment benefits, as discussed in Note 10 – Postemployment Healthcare Benefits, and other contractual obligations. The current portion is included in accounts payable and accrued liabilities in the statements of net assets as of June 30, 2011 and 2010.

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 \$74.2 million and \$71.6 million for the years ended June 30, 2011 and 2010, 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 \$26.5 million and \$25.2 million for the years ended June 30, 2011 and 2010, 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 \$3.8 million and \$3.5 million for the years ended June 30, 2011 and 2010, respectively.

c. University Medical Center, Inc. Affiliation Agreement

The University and University Medical Center (UMC) have entered into an agreement that 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, 2011 and 2010 was approximately \$40.1 million and \$35.5 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 \$52.5 million and \$44.1 million for the years ended June 30, 2011 and 2010, respectively.

8. Expenses

Operating expenses by natural classification for the years ended June 30, 2011 and 2010 were approximately (in thousands):

	<u>2011</u>	<u>2010</u>
Salaries and wages	\$ 177,760	\$ 169,925
Employee benefits	37,163	42,950
Supplies and services	78,938	89,579
Depreciation	9,605	8,809
Scholarships and fellowships	39,967	37,480
	<u>\$ 343,433</u>	<u>\$ 348,743</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 \$11.2 million and \$10.9 million during the years ended June 30, 2011 and 2010, 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 employee's 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 years ended June 30, 2011 and 2010, the University contributed approximately \$0.5 million and \$0.8 million, approximately 42 percent and 53 percent of total premiums, respectively. Retired Plan members under age 65 receiving benefits contributed approximately \$0.7 million for each of the years ended June 30, 2011 and 2010, approximately 58 percent and 47 percent of total premiums, respectively, through their required monthly contributions according to the following schedule:

	<u>PPO</u>	<u>Cardinal Care Plan</u>	<u>EPO</u>	<u>PCA High</u>	<u>PCA Low</u>	<u>Out of Area</u>
Employee	\$ 337	\$ 364	\$ 375	\$ 236	\$ 171	\$ 354
Employee and Spouse	\$ 679	\$ 738	\$ 759	\$ 514	\$ 393	\$ 685

Medicare-eligible retirees receive a monthly benefit of \$108 per individual covered. For each of the years ended June 30, 2011 and 2010, the University contributed \$1.1 million, respectively, 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 following table 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>2011</b>	<b>2010</b>
Normal cost	\$ 5,033	\$ 5,429
AAL amortization	4,215	4,556
Annual required contribution (ARC)	9,248	9,985
Interest on above	710	943
Adjustment to ARC	(789)	(1,130)
OPEB liability (gain)/loss	(15,256)	4,825
Annual OPEB (gain)/cost (AOC)	(6,087)	14,623
Contributions made	(1,643)	(1,916)
(Decrease)/increase in net OPEB obligation	(7,730)	12,707
Net OPEB obligation - beginning of year	30,463	17,756
Net OPEB obligation - end of year	<u>\$ 22,733</u>	<u>\$ 30,463</u>

The University's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal Year Ended June 30,	Annual OPEB (Gain)/Cost	Percentage of Annual OPEB (Gain)/Cost Contributed	Net OPEB Obligation
2011	\$ (6,087)	-27%	\$ 22,733
2010	\$ 14,623	13%	\$ 30,463
2009	\$ 13,475	15%	\$ 17,756

The University allocates a portion of the AOC, and the corresponding OPEB obligation, to its affiliated corporations, including the Research Foundation. For the years ended June 30, 2011 and 2010, the Research Foundation's portion of the AOC was \$2.2 million and \$5.5 million, respectively. The Research Foundation's net OPEB obligation for the years ended June 30, 2011 and 2010 was \$7.9 million and \$10.9 million, of which \$6.6 million and \$9.2 million was recorded in other long term liabilities and \$1.3 million and \$1.7 million was recorded in accounts payable and accrued expenses as of June 30, 2011 and 2010, respectively.

d. Funded Status and Funding Progress

As of July 1, 2010, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability for benefits was \$79.9 million and \$88.8 million and there were no assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$79.9 million and \$88.8 million as of June 30, 2011 and 2010, respectively. The covered payroll (annual payroll of active employees covered by the plan) was \$400.9 million and \$378.1 million, and the ratio of the UAAL to the covered payroll was 20 percent and 23 percent, for the years ended June 30, 2011 and 2010, respectively.

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, 2010, 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 9 years. The gain on the benefit obligation is due to updates made on expected future health claims. Expected claims have decreased based on a review of actual claims over the last three years as well as current COBRA rates. The UAAL is being amortized on a straight line basis over 30 years. The remaining amortization period at June 30, 2011 was 26 years.

11. Commitments and Contingencies

a. Commitments

At June 30, 2011 and 2010, respectively, the Research Foundation had approximately \$10.0 million and \$6.8 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.

d. Current Economic Conditions

The current protracted economic decline continues to present not-for profit organizations with difficult circumstance and challenges, which in some cases have resulted in large declines in the fair value of investments and other assets. The financial statements have been prepared using values and information currently available to the Research Foundation.

In addition, given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments in investment values that could negatively impact the Research Foundation's ability to maintain sufficient liquidity.

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

<u>Actuarial Value Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Accrued Liability (AAL) (b)</u>	<u>Unfunded AAL (UAAL) (b - a)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>	<u>UAAL as a Percentage of Covered Payroll ((b-a) / c)</u>
7/1/2010	-	\$ 79,892	\$ 79,892	0%	\$ 400,911	20%
7/1/2009	-	\$ 88,808	\$ 88,808	0%	\$ 378,059	23%
7/1/2008	-	\$ 78,455	\$ 78,455	0%	\$ 358,680	22%

The gain on the benefit obligation is due to updates made on expected future health claims. Expected claims have decreased based on a review of actual claims over the last three years as well as current COBRA rates.