

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

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

**Auditor's Report and Financial Statements  
June 30, 2014 and 2013**

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

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

**Table of Contents:**

	Page
Independent Auditor's Report .....	1
Management's Discussion and Analysis (Unaudited).....	3
Statements of Net Position.....	13
Statements of Revenues, Expenses and Changes in Net Position.....	14
Statements of Cash Flows.....	15
Notes to Financial Statements.....	16
Required Supplementary Information .....	28

## Independent Auditor's Report

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

We have audited the accompanying basic financial statements, which are comprised of statements of net position as of June 30, 2014 and 2013, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended and the related notes to the basic financial statements, as listed in the table of contents, of the University of Louisville Research Foundation, Inc. (Research Foundation), a component unit of the University of Louisville.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Research Foundation's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Research Foundation's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## **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, 2014 and 2013, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Emphasis of Matter**

As discussed in Note 11 to the financial statements, the 2013 financial statements have been restated to correct a misstatement. Our opinion is not modified with respect to this matter.

## **Other Matter**

### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and postemployment benefit information listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*BKD, LLP*

Louisville, Kentucky  
September 29, 2014

# 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, 2014, 2013, and 2012. 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 metropolitan research university located in Kentucky's largest city. 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, 2014, total awards were \$109.1 million, a decrease of \$9.8 million or 8%, as compared to fiscal year 2013. This decrease is partially attributed to a reduction in federal grant funding. Some of the funding highlights include:

- \$7.3 million Kosair Charities Pediatric Neurosurgery gift to support rehabilitation of children who have suffered spinal cord injuries
- \$4.8 million from the National Institute for Health for multiple cardiology research projects
- \$2.2 million from the National American Heart Association – AHA Tobacco Regulations and Addiction Center (A-TRAC) to research the effects of nicotine on heart health
- \$2.1 million from Regenerex for research of stem cells to treat a variety of human diseases

Research Foundation continues to receive national recognition, with a member of research administration selected as a recipient for the Hartford-Nicholsen Award for Distinguished Contributions to Research Administration on behalf of the Board of Directors of the Society of Research Administrators International.

#### Financial Highlights

- The Research Foundation's financial position remains strong at June 30, 2014, with total assets of \$121.3 million and liabilities of \$43.5 million as compared to June 30, 2013 at \$124.9 million of total assets and \$31.1 million of liabilities. Net position, which represent the residual interest in the Research Foundation's assets after liabilities are deducted, were \$77.8 million and \$93.8 million for the years ended June 30, 2014 and 2013, respectively.
- The Research Foundation's total liabilities of \$43.5 million contain grant advances. Grant advances represent the unearned portion of grants and sponsored programs and comprise \$10.3 million or 24% of total liabilities.
- Operating revenues amounted to \$325.7 million and \$292.9 million and operating expenditures were \$369.1 million and \$361.3 million resulting in a net operating loss of \$43.4 million and \$68.4 million for the years ended June 30, 2014 and 2013, respectively. When adjusted for net

nonoperating revenues of \$27.4 million and \$45.3 million, net position of the Research Foundation decreased by \$16.0 million and \$23.1 million for the years ended June 30, 2014, and 2013, respectively.

### **Using the Financial Statements**

The Research Foundation's financial report includes three financial statements: the Statement of Net Position; the Statement of Revenues, Expenses and Changes in Net Position; 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 Position and Statement of Revenues, Expenses and Changes in Net Position. 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 \$41.7 million and \$39.8 million in nonexchange grants and contract revenue for the years ended June 30, 2014 and 2013, 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 grant advances rather than as income when received. Such grant advances totaled \$10.3 million and \$10.5 million as of June 30, 2014 and 2013, respectively.
- Capital assets are depreciated and reported net of accumulated depreciation. The Research Foundation's capital assets as of June 30, 2014 and 2013 consist primarily of buildings, equipment and library materials with a net position value of \$74.4 million and \$72.4 million, respectively.

### **Statements of Net Position**

The statements of net position present the financial position of the Research Foundation at the end of the fiscal year and include all assets and liabilities. Net position represents the difference between total assets and total liabilities and provides a snapshot of the current financial condition of the Research Foundation at the end of a fiscal year. The change in net position 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 position at June 30, 2014, 2013, and 2012 is summarized on the following page:

**Condensed Statements of Net Position**  
**June 30, 2014, 2013, and 2012**  
(In Thousands)

	<b>2014</b>	<b>Restated 2013</b>	<b>Restated 2012</b>	<b>2014 - 2013 Change</b>	<b>2013 - 2012 Change</b>
<b>ASSETS</b>					
Current assets	\$ 46,347	\$ 51,330	\$ 73,108	\$ (4,983)	\$ (21,778)
Capital assets	74,365	72,405	77,567	1,960	(5,162)
Other noncurrent assets	617	1,161	489	(544)	672
Total assets	<u>121,329</u>	<u>124,896</u>	<u>151,164</u>	<u>(3,567)</u>	<u>(26,268)</u>
<b>LIABILITIES</b>					
Current liabilities	34,657	23,098	27,493	11,559	(4,395)
Noncurrent liabilities	8,889	7,979	6,753	910	1,226
Total liabilities	<u>43,546</u>	<u>31,077</u>	<u>34,246</u>	<u>12,469</u>	<u>(3,169)</u>
<b>NET POSITION</b>					
Net investment in capital assets	74,365	72,405	77,567	1,960	(5,162)
Restricted - expendable	1,689	4,387	4,651	(2,698)	(264)
Unrestricted	1,729	17,027	34,700	(15,298)	(17,673)
Total net position	<u>\$ 77,783</u>	<u>\$ 93,819</u>	<u>\$ 116,918</u>	<u>\$ (16,036)</u>	<u>\$ (23,099)</u>

### Assets

A review of the Research Foundation's statement of net position at June 30, 2014 indicates that the Research Foundation is highly liquid with only \$8.9 million in long-term liabilities. Of the \$46.3 million in current assets, \$45.5 million, or 98%, consists of accounts receivable that are to be collected within the next year. As detailed in the Statements of Cash Flows, the cash decreased during the year by \$22.0 million due primarily to payments of salaries and benefits of \$229.7 million.

Noncurrent assets consist mainly of \$74.4 million of capital assets, which increased due to additional capital assets of \$11.4 million offset by depreciation and disposals.

### Liabilities

The Research Foundation's current liabilities consist mainly of \$10.3 million of unexpended cash advances for sponsored research activities, similar to June 30, 2013. The Research Foundation is required to set up a liability when awards are paid in advance, as they are responsible for paying back any unused funds to the sponsor. The remaining \$24.4 million of current liabilities relates to trade accounts payable and other accrued liabilities and amounts due to the University. The Research Foundation's allocated portion of other post-employment benefits totals \$10.6 million, with the \$1.7 million current portion included in accounts payable and accrued expenses and the remainder shown as other long-term liabilities.

### Net Position

Net position represents the residual interest in the Research Foundation's assets after liabilities are deducted. The Research Foundation's net position at June 30, 2014 and 2013 was \$77.8 million and

\$93.8 million, respectively. They are summarized into the three major categories in accordance with GASB Statement No. 35 and GASB Statement No. 63 reporting requirements as follows:

**Net investment in capital assets - \$74.4 million**

The Research Foundation's net investments in capital assets represents 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 \$2.0 million increase over prior year reflects the addition of \$11.4 million in capital assets, offset by \$9.2 million of depreciation and \$0.2 million of disposals.

**Restricted expendable net position - \$1.7 million**

Restricted expendable net position represents funds primarily from fixed payment contracts that are subject to externally imposed restrictions governing their use. Net position results from the excess of contract revenues over expenses incurred through June 30, 2014. The amounts remain restricted until the contract is completed.

Restricted expendable net position decreased \$2.7 million, or 61%. The overall decrease is due mainly to a decrease in the number of federal and state grant awards.

**Unrestricted net position - \$1.7 million**

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

**Fiscal Year 2013**

The Research Foundation's financial position as of the fiscal year ended June 30, 2013 shows a decrease in assets and liabilities with an overall decrease in net position. Assets decreased during the fiscal year ended June 30, 2013 by \$26.3 million, or 17%, as compared to the fiscal year ended June 30, 2012. This decrease was due mainly to the \$17.1 million decrease in cash and cash equivalents related to decreased grant and clinical revenue. The decrease in liabilities mainly resulted from the decrease in accounts payable, which decreased \$4.4 million from the fiscal year ended June 30, 2012.

Net position decreased \$23.1 million, or 20%, compared to net position at June 30, 2013 due mainly to the \$17.7 million decrease in unrestricted net position.

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

The statements of revenues, expenses and changes in net position present the Research Foundation's results of operations. A condensed version of the Research Foundation's revenues, expenses and changes in net position for the years ended June 30, 2014, 2013, and 2012 is shown on the following page:



**Condensed Statements of Revenues, Expenses and Changes in Net Position**  
**Years ended June 30, 2014, 2013, and 2012**  
(In Thousands)

	<u>2014</u>	<u>Restated 2013</u>	<u>Restated 2012</u>	<u>2014 - 2013 Change</u>	<u>2013 - 2012 Change</u>
<b>OPERATING REVENUES</b>					
Clinical services	\$ 205,879	\$ 173,880	\$ 187,163	\$ 31,999	\$ (13,283)
Grants and contracts	91,405	92,474	106,189	(1,069)	(13,715)
Facilities and administrative cost recoveries	21,965	24,011	26,899	(2,046)	(2,888)
Other operating revenues	6,419	2,549	908	3,870	1,641
Total operating revenues	<u>325,668</u>	<u>292,914</u>	<u>321,159</u>	<u>32,754</u>	<u>(28,245)</u>
<b>OPERATING EXPENSES</b>					
Depreciation	9,205	9,481	10,091	(276)	(610)
Other operating expenses	359,890	351,874	353,077	8,016	(1,203)
Total operating expenses	<u>369,095</u>	<u>361,355</u>	<u>363,168</u>	<u>7,740</u>	<u>(1,813)</u>
Operating loss	<u>(43,427)</u>	<u>(68,441)</u>	<u>(42,009)</u>	<u>25,014</u>	<u>(26,432)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>					
Nonexchange grants and contracts	41,706	39,770	40,885	1,936	(1,115)
Transfers	(14,349)	(10,893)	(15,447)	(3,456)	4,554
Other nonoperating revenues	34	16,465	(5,376)	(16,431)	21,841
Total nonoperating revenues	<u>27,391</u>	<u>45,342</u>	<u>20,062</u>	<u>(17,951)</u>	<u>25,280</u>
Decrease in net position	<u>(16,036)</u>	<u>(23,099)</u>	<u>(21,947)</u>	<u>7,063</u>	<u>(1,152)</u>
<b>NET POSITION</b>					
Net position, beginning of year, as previously reported	-	-	136,094		
Adjustment applicable to prior years	-	-	2,771		
Net position, beginning of year, as restated	<u>93,819</u>	<u>116,918</u>	<u>138,865</u>	<u>(23,099)</u>	<u>(21,947)</u>
Net position, end of year	<u>\$ 77,783</u>	<u>\$ 93,819</u>	<u>\$ 116,918</u>	<u>\$ (16,036)</u>	<u>\$ (23,099)</u>

### Operating Revenues

The Research Foundation recognized \$325.7 million in operating revenues for the year ended June 30, 2014. This represents an 11% increase in revenues from the \$292.9 million reported for the year ended June 30, 2013.

Revenues from clinical services were \$205.9 million for the year ended June 30, 2014. This is an increase of approximately \$32.0 million, or 18%, compared to \$173.9 million in similar revenues reported for the year ended June 30, 2013. The increase in revenues is due mainly from increased clinical operations of \$26.0 million primarily related to the increased number of Medicaid patients served. Additionally, affiliation revenues with hospitals increased \$11.3 million.

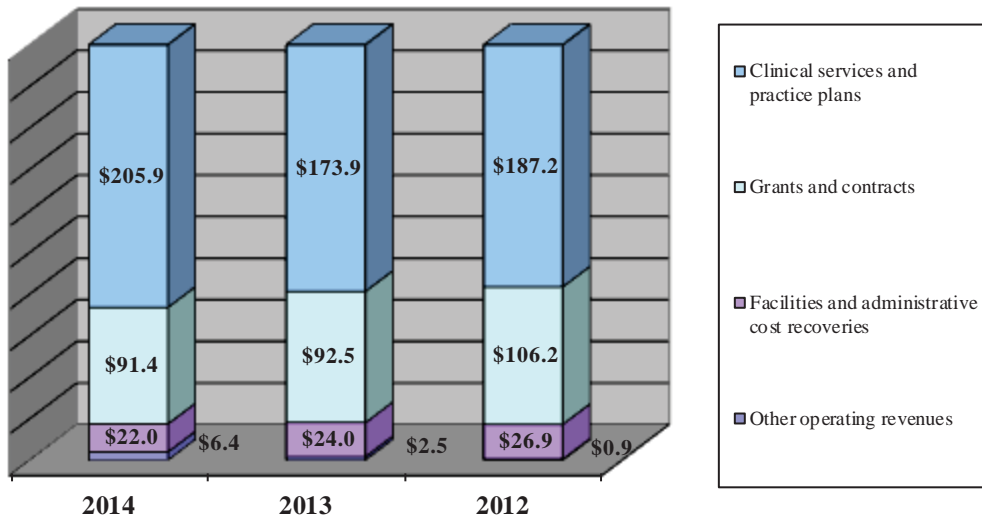
Revenues from grants and contracts were \$91.4 million for the year ended June 30, 2014 as compared to \$92.5 million in revenues reported in the previous year. This includes decreases of \$2.5 million in federal grants and contracts and \$1.2 million in state and local grants for the year ended June 30, 2014, as compared to the previous year.

Revenue from facilities and administrative cost recoveries were \$22.0 million and \$24.0 million for the years ended June 30, 2014 and 2013, respectively. This represents the reduction in 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, which is consistent with the decrease in grant and contract revenue. 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, 2014 and 2013, approximately \$9.5 million and \$10.5 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, 2014, 2013, and 2012 (in millions).

**Operating Revenues**  
**Years Ended June 30, 2014, 2013, and 2012**

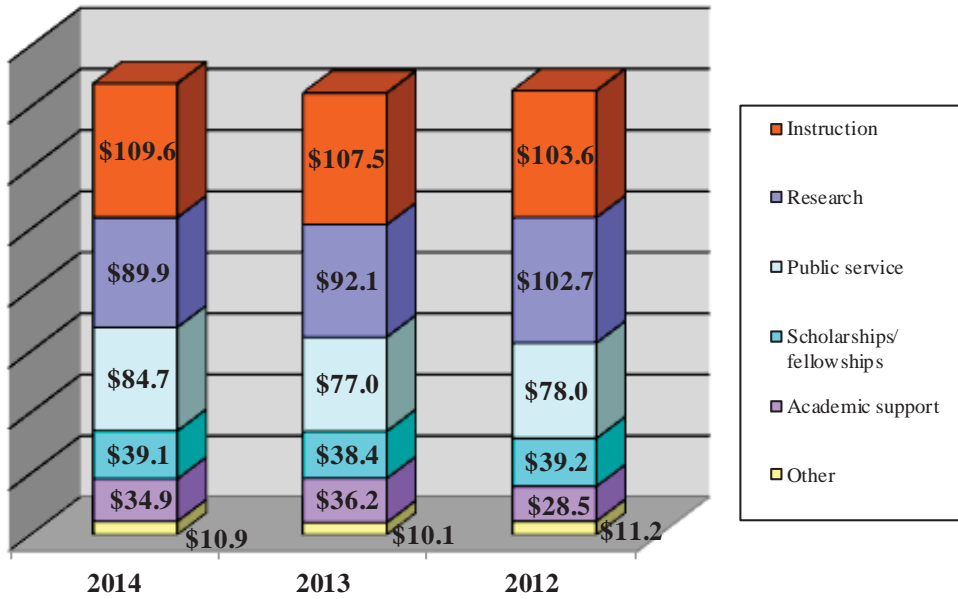


**Operating Expenses by Functional and Natural Class**

Total operating expenses were \$369.1 million and \$361.3 million for the fiscal years ended June 30, 2014 and 2013, respectively. The primary reason for the increase of \$7.7 million, or 2%, is an increase in public service expenses related to increased bad debt expense and additional operational costs associated with the increased number of Medicaid patients.

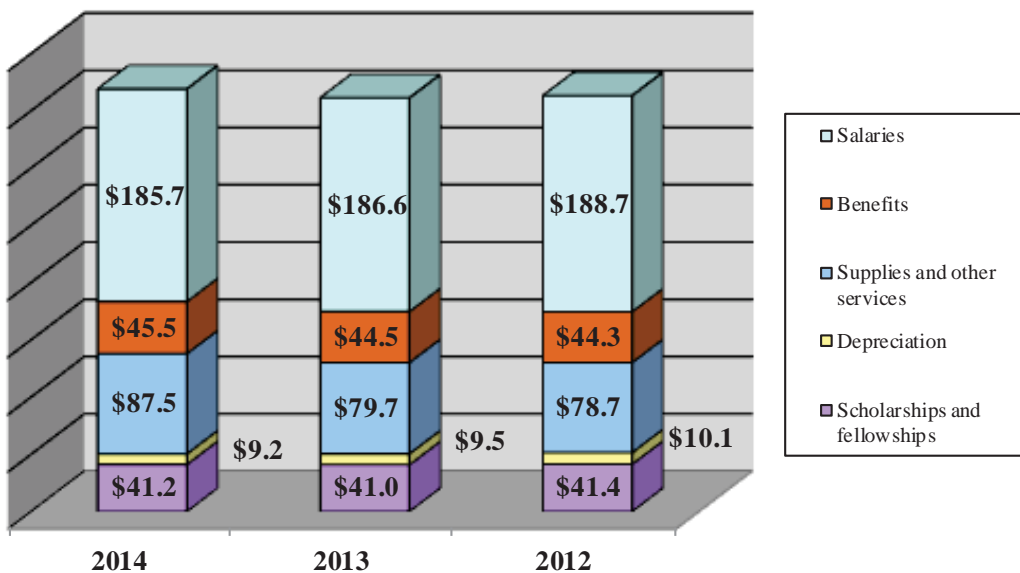
The following is a graphic illustration of total operating expenses by function for the years ended June 30, 2014, 2013 and 2012 (in millions):

**Operating Expenses by Functional Classification**  
**Years ended June 30, 2014, 2013, and 2012**



The following is a graphic illustration of total operating expenses by natural classification for the years ended June 30, 2014, 2013 and 2012 (in millions):

**Operating Expenses by Natural Classification**  
**Years ended June 30, 2014, 2013, and 2012**



## **Nonoperating Revenues (Expenses)**

The Research Foundation's total nonoperating revenues of \$27.4 million for fiscal year ended June 30, 2014, was mostly comprised of nonexchange grants and contract revenues of \$41.7 million and transfer expenses of \$14.3 million. Included in the transfers total was a \$9.5 million transfer to the University, related to the facilities and administrative revenue, for administrative expenses incurred for sponsored research. Total nonoperating revenues decreased by \$18.0 million as compared to fiscal year ended June 30, 2013. The decrease is due primarily to the \$16.2 million of refunds received in 2013 by the Research Foundation related to the employer portion of FICA tax on medical residents paid in years prior to April 2005 that was not received in 2014.

### **Fiscal Year 2013**

For the year ended June 30, 2013, Research Foundation reported \$292.9 million in operating revenues, a decrease of 9% compared to the \$321.2 million reported for the year ended June 30, 2012.

Revenues from clinical services were \$173.9 million for fiscal year 2013, a decrease of 7% from the fiscal year ended June 30, 2012. The decrease in revenues was due mainly to a \$15.8 million decrease in clinical operations as the kidney disease program was sold to a third party on June 30, 2012 and other units moved to University of Louisville Physicians, Inc. (ULP) during the year. This decrease was offset by the \$4.7 million increase in Academic Program Support funds from the Practice Plans and \$3.5 million increase in amounts received from affiliation agreements with area hospitals.

Revenue from facilities and administrative cost recoveries were \$24.0 million and \$26.9 million for the years ended June 30, 2013 and 2012, respectively. The Research Foundation transferred to the University, approximately \$10.5 million and \$11.2 million during the years ended June 30, 2013 and 2012, respectively, in recognition of indirect support provided by the University.

Total operating expenses were \$361.3 million and \$363.2 million for the fiscal years ended June 30, 2013 and 2012, respectively. The decrease of \$1.8 million, or 1%, reflects the Research Foundations efforts to operate as efficiently as possible.

### **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, 2014, 2013, and 2012, are summarized on the following page:

**Condensed Statements of Cash Flows**  
**Years ended June 30, 2014, 2013, and 2012**  
(In Thousands)

	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2014 - 2013</u> <u>Change</u>	<u>2013 - 2012</u> <u>Change</u>
Cash (used)/provided by:					
Operating activities	\$ (47,977)	\$ (52,859)	\$ (41,055)	\$ 4,882	\$ (11,804)
Noncapital and related financing activities	37,374	40,194	20,237	(2,820)	19,957
Capital financing activities	(11,359)	(4,412)	(9,654)	(6,947)	5,242
Investing activities	-	-	35	-	(35)
Net decrease in cash	(21,962)	(17,077)	(30,437)	(4,885)	13,360
Cash and cash equivalents, beginning of year	21,962	39,039	69,476	(17,077)	(30,437)
Cash and cash equivalents, end of year	<u>\$ -</u>	<u>\$ 21,962</u>	<u>\$ 39,039</u>	<u>\$ (21,962)</u>	<u>\$ (17,077)</u>

### Operating Activities

The Research Foundation's operating activities used approximately \$48.0 million of cash during the fiscal year ended June 30, 2014, representing a decrease of \$4.9 million compared to the prior year. While cash received from clinical services increased \$15.7 million it was offset by a decrease of \$9.9 million of cash received from grants and contracts and facilities and administrative cost recoveries. Cash outflows from operations during the fiscal year ended June 30, 2014 increased due largely to expenses related to payments to suppliers, which increased \$7.3 million, as compared to the fiscal year ended June 30, 2013, due in part to additional costs associated with increased number of patients.

### Other Activities

The \$37.4 million cash provided by noncapital and related financing activities relates mainly to the \$42.7 million provided by nonexchange grants and contracts. It also includes the Research Foundation's transfer of \$14.3 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 activities decreased \$2.8 million from the fiscal year ended June 30, 2013, due in part to the receipt of \$11.6 million of refunds of the employer portion of FICA tax paid for medical residents that occurred in 2013 but not in 2014, offset by the funds received from the University to maintain the deficit cash balance.

Cash used for capital financing activities increased \$6.9 million to \$11.4 million during the fiscal year ended June 30, 2014, due to an increase in the amount of capital assets purchased.

### Fiscal Year 2013

The Research Foundation operating activities used approximately \$52.9 million representing an increase of \$11.8 million during the fiscal year ended June 30, 2013, due to a \$4.0 million decrease in cash received from clinical services, which relates to the sale of the kidney disease program and movement of other clinical units to ULP. Additionally, cash provided by grants decreased by \$6.4 million due to the lower number of grants. Cash outflows from operations during the fiscal year ended June 30, 2013 decreased due largely to expenses related to payments to employees, which decreased \$1.2 million, as compared to the fiscal year ended June 30, 2012.

The \$40.2 million cash provided by noncapital and related financing activities relates mainly to the \$39.2 million provided by nonexchange grants and contracts. In total, cash provided by noncapital and related financing activities increased \$20.0 million from the fiscal year ended June 30, 2012, due primarily to the receipt of \$11.6 million of refunds of the employer portion of FICA tax paid for medical residents prior to April 2005.

Cash used for capital financing activities decreased \$5.2 million to \$4.4 million during the fiscal year ended June 30, 2013, due to a decrease in the amount of capital assets purchased.

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

As mandated by House Bill 1 of the 1997 General Assembly, the University is to become a nationally recognized metropolitan research university by 2020. The first important step towards achieving that mandate was the Fall 2008 introduction of the 2020 Plan. The 2020 Plan is the strategic blueprint for the University to achieve House Bill 1's mandate. This plan was drafted after the Board of Trustees empowered President James Ramsey to aggressively move ahead towards the next level in the University's pursuit of excellence.

The University has faced many fiscal challenges that have impacted campus operations both prior to, and subsequent to, The 2020 Plan's introduction. The national recession of 2007 to 2009 has exacerbated the decline in state general fund support. State appropriations in constant dollars have decreased each year from the beginning of the recession in fiscal year 2008 through the current fiscal year 2015 budget. The constant dollar decrease for this period is 26.4%, over one-quarter of fiscal year 2008 levels. The effect on constant dollar State Appropriation per Full-Time Equivalent (FTE) student has been even more dramatic during this period—a decrease of 32.3%.

The 2014-16 biennial budget passed by the 2014 General Assembly in April 2014 reflected a net 1.5% reduction, or \$2.1 million, in state support for the University in fiscal year 2015. The fiscal year 2016 budget is flat lined from fiscal year 2015. The reduced state funding continues to impact daily operations. The University has not received maintenance and operation funding for new buildings in several years.

The budgetary decisions that support and shape the fiscal year 2015 budget reflect the current and foreseeable economic realities facing public higher education institutions in general and the University in particular.

Due to the changing landscape of higher education across the United States, the University has embarked on a consultative process aimed at re-shaping and re-engineering the financial and physical landscape of the University. The "21<sup>st</sup> Century Initiative" led by the University Provost is a broad-based, campus-wide initiative to position the University to not only meet the 2020 Plan goals, but also to address ways of better serving students and the community in the future.

Again this year, the annual budget focused on the University's "Upward Trajectory". Despite fourteen budget cuts in fifteen years, the lack of maintenance and operations funding, and the dramatic shift in public policy that has, and continues to direct funding away from higher education, the University has made tremendous progress in meeting its 2020 goals. The President outlined the University's successes across a myriad of key academic, research, and public service metrics noting, "it's not just about the numbers, it's about the people." These successes—the result of hard work by the University's faculty, staff and students—has the University well positioned to meet House Bill 1's aggressive mandate to become a premier metropolitan research university.

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 Position**  
**As of June 30, 2014 and 2013**  
**(In Thousands)**

	<u>2014</u>	<u>Restated 2013</u>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents		\$ 21,962
Accounts receivable, net	\$ 45,457	28,585
Inventories	354	361
Other assets	536	422
Total current assets	<u>46,347</u>	<u>51,330</u>
Noncurrent Assets:		
Accounts receivable, net	615	1,159
Other long-term assets	2	2
Capital assets, net	74,365	72,405
Total noncurrent assets	<u>74,982</u>	<u>73,566</u>
Total assets	<u>121,329</u>	<u>124,896</u>
<b>LIABILITIES</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	15,366	12,588
Due to University of Louisville	9,023	-
Grant advances	10,268	10,510
Total current liabilities	<u>34,657</u>	<u>23,098</u>
Noncurrent Liabilities:		
Other long-term liabilities	8,889	7,979
Total noncurrent liabilities	<u>8,889</u>	<u>7,979</u>
Total liabilities	<u>43,546</u>	<u>31,077</u>
<b>NET POSITION</b>		
Net investment in capital assets	74,365	72,405
Restricted - expendable for:		
Research	418	3,489
Instruction	391	448
Public service	753	252
Scholarships and fellowships	121	189
Academic support	6	9
Unrestricted	1,729	17,027
Total net position	<u>\$ 77,783</u>	<u>\$ 93,819</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 Position**  
**For the Years Ended June 30, 2014 and 2013**  
**(In Thousands)**

	<b>2014</b>	<b>Restated 2013</b>
<b>OPERATING REVENUES</b>		
Clinical services, net of contractual allowances of \$107,003 in 2014 and \$56,832 in 2013	\$ 205,879	\$ 173,880
Federal grants and contracts	69,805	72,314
State and local grants and contracts	9,319	10,553
Nongovernmental grants and contracts	12,281	9,607
Other operating revenue	6,419	2,549
Facilities and administrative cost recoveries	21,965	24,011
Total operating revenues	325,668	292,914
<b>OPERATING EXPENSES</b>		
Instruction	109,595	107,451
Research	89,890	92,079
Public service	84,720	77,015
Scholarships and fellowships	39,053	38,416
Academic support	34,875	36,179
Institutional support	871	648
Operation and maintenance of plant	820	55
Depreciation	9,205	9,481
Student services	11	11
Service centers	55	20
Total operating expenses	369,095	361,355
Operating loss	(43,427)	(68,441)
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Gifts	51	67
Nonexchange grants and contracts	41,706	39,770
Investment loss	-	5
Other nonoperating (expense)/income	(17)	16,393
Net nonoperating revenues	41,740	56,235
Transfers	(14,349)	(10,893)
Total other revenues	27,391	45,342
Decrease in net position	(16,036)	(23,099)
<b>NET POSITION</b>		
Net position - beginning of year, as previously reported	-	108,775
Adjustment applicable to prior years	-	8,143
Net position - beginning of year, as restated	93,819	116,918
Net position - end of year	\$ 77,783	\$ 93,819

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, 2014 and 2013**  
(In Thousands)

	<b>2014</b>	<b>Restated 2013</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Clinical services	\$ 192,500	\$ 176,778
Grants and contracts	87,254	95,152
Facilities and administrative cost recoveries	21,965	24,011
Other operating revenue	6,418	1,434
Payments to employees	(185,549)	(187,892)
Payments for benefits	(44,156)	(43,428)
Payments for scholarships and fellowships	(41,160)	(40,991)
Payments to suppliers	(85,249)	(77,923)
Net cash used by operating activities	(47,977)	(52,859)
<b>CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Transfers to related entities	(14,349)	(10,934)
Gifts	51	67
Nonexchange grants and contracts	42,664	39,205
Due to University of Louisville	9,023	-
Other noncapital financing activity	(15)	11,856
Net cash provided by noncapital and related financing activities	37,374	40,194
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Purchases of capital assets	(11,359)	(4,412)
Net cash used by capital and related financing activities	(11,359)	(4,412)
Net decrease in cash and cash equivalents	(21,962)	(17,077)
Cash and cash equivalents - beginning of year	21,962	39,039
Cash and cash equivalents - end of year	\$ -	\$ 21,962
<b>RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Operating loss	\$ (43,427)	\$ (68,441)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation	9,205	9,481
Loss on disposal of equipment	194	129
Changes in assets and liabilities:		
Accounts receivable, net	(17,288)	4,430
Inventories	7	48
Other assets	(114)	123
Accounts payable and accrued liabilities	2,778	116
Grant advances	(242)	29
Other long-term liabilities	910	1,226
Net cash used by operating activities	\$ (47,977)	\$ (52,859)
<b>NONCASH TRANSACTIONS</b>		
Transfer of assets from University of Louisville	\$ -	\$ 42

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, 2014 and 2013**

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 common management and substantially the same Board of Directors. 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).

The financial statements of the University have been prepared on the accrual basis of accounting. Revenues, expenses, gains, losses, assets, liabilities and deferred inflows and outflows of resources from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally federal and state grants and state appropriations) are recognized when all applicable eligibility requirements are met. Internal activity and balances are eliminated in preparation of the financial statements unless they relate to services provided and used internally. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Government-mandated nonexchange transactions that are not program specific (such as state appropriations), investment income and interest on capital asset-related debt are included in nonoperating revenues and expenses. The University first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position are available.

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. 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.

f. 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.

g. Deferred Outflows/Inflows of Resources

In addition to assets, GASB No. 63 requires the presentation of a separate financial statement element, deferred outflows of resources, which represents a consumption of net position that applies to future periods. The Research Foundation has no items that qualify for reporting in this category.

In addition to liabilities, GASB No. 63 requires the presentation of a separate financial statement element, deferred inflows of resources, which represents an acquisition of net position that applies to future periods. The Research Foundation has no items that qualify for reporting in this category.

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. Grant Advances

The Research Foundation receives revenues relative to sponsored agreements via grants, contracts, or cooperative agreements. 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 \$10.3 million and \$10.5 million as of June 30, 2014 and 2013, respectively, are recorded as a liability in the Research Foundation's financial statements as grant advances.

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 the 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 position 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 Position

The net position of the Research Foundation is classified in three components. Net investment in capital assets 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 position consists of noncapital assets that must be used for a particular purpose as specified by creditors, grantors or donors external to the Research Foundation. Unrestricted net position consists of the remaining assets less remaining liabilities that do not meet the definition of net investment in capital assets or restricted net position.

l. 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 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 2013 amounts have been reclassified to conform to the 2014 presentation. These reclassifications had no effect on the change in net position.

2. Cash and Cash Equivalents

The Research Foundation maintains various deposits. 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 covered up to the limits 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. The custodial credit risk for deposits is the risk that, in the event of failure of the counterparty to a transaction, a government will not be able to recover the value of the deposits. The Research Foundation does not have a formal policy addressing custodial credit risk.

3. Transactions with Related Entities

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 \$9.5 million and \$10.5 million for the years ended June 30, 2014 and 2013, respectively. Additional research support transfers to the University totaled \$0.1 million for the year ended June 30, 2013.

The Research Foundation transferred \$5.0 million and \$3.3 million related to capital projects and debt service payments during the fiscal years ended June 30, 2014 and 2013, respectively, to the University. These transfers relate to certain capital projects, which are financed by the University, and as such, are recorded as assets of the University.

For each of the years ended June 30, 2014 and 2013, the Research Foundation was the recipient of \$2.4 million from related entities to assist in funding cost share required by certain sponsored programs and grants.

Additionally, the Research Foundation transferred \$2.2 million and received \$0.6 million to related entities for the years ended June 30, 2014 and 2013, respectively.

4. Accounts Receivable, net

Accounts receivable, net as of June 30, 2014 and 2013, are summarized as follows (in thousands):

<b>2014</b>			
	<b>Gross</b>		<b>Net</b>
	<b>Receivable</b>	<b>Allowance</b>	<b>Receivable</b>
Patient care	\$ 81,307	\$ (50,060)	\$ 31,247
Sponsored agreements	16,797	(2,740)	14,058
Other receivables	767	-	767
Total	<u>\$ 98,871</u>	<u>\$ (52,800)</u>	46,072
Current portion			45,457
Noncurrent portion			<u>\$ 615</u>
<b>2013 (Restated)</b>			
	<b>Gross</b>		<b>Net</b>
	<b>Receivable</b>	<b>Allowance</b>	<b>Receivable</b>
Patient care	\$ 33,752	\$ (17,568)	\$ 16,184
Sponsored agreements	15,041	(2,740)	12,301
Other receivables	1,259	-	1,259
Total	<u>\$ 50,052</u>	<u>\$ (20,308)</u>	29,744
Current portion			28,585
Noncurrent portion			<u>\$ 1,159</u>

5. Capital Assets, net

Capital assets at historical cost as of June 30, 2014 and 2013 are summarized as follows (in thousands):

	<b>2014</b>				<b>Ending Balance</b>
	<b>Beginning Balance</b>	<b>Additions</b>	<b>Retire- ments</b>	<b>Transfers</b>	
<b>Cost - Non depreciable</b>					
Land		\$ 352			\$ 352
Construction in progress	\$ 2,139	7,880		\$ (1,504)	8,515
Subtotal	<u>2,139</u>	<u>8,232</u>		<u>(1,504)</u>	<u>8,867</u>
<b>Cost - Depreciable</b>					
Building	60,805	65		664	61,534
Infrastructure	-	90		840	930
Land improvements	237	-		-	237
Equipment	77,002	2,972	\$ (540)	-	79,434
Leasehold improvements	702	-	-	-	702
Library materials	150	-	(106)	-	44
Subtotal	<u>138,896</u>	<u>3,127</u>	<u>(646)</u>	<u>1,504</u>	<u>142,881</u>
Total capital assets - cost	<u>141,035</u>	<u>11,359</u>	<u>(646)</u>	<u>-</u>	<u>151,748</u>
<b>Accumulated depreciation</b>					
Buildings	9,192	2,388	-	-	11,580
Infrastructure	-	9	-	-	9
Land improvements	20	6	-	-	26
Equipment	58,677	6,788	(433)	-	65,032
Leasehold improvements	702	-	-	-	702
Library materials	39	14	(19)	-	34
Subtotal	<u>68,630</u>	<u>9,205</u>	<u>(452)</u>	<u>-</u>	<u>77,383</u>
Capital assets, net	<u>\$ 72,405</u>	<u>\$ 2,154</u>	<u>\$ (194)</u>	<u>\$ -</u>	<u>\$ 74,365</u>

	2013				
	Beginning Balance	Additions	Retire- ments	Transfers (to)/ from Affiliates	Ending Balance
<b>Cost - Non depreciable</b>					
Construction in progress	\$ 3,476	\$ 963		\$ (2,300)	\$ 2,139
Subtotal	3,476	963		(2,300)	2,139
<b>Cost - Depreciable</b>					
Building	58,494	11		2,300	60,805
Land improvements	237	-		-	237
Equipment	74,868	3,333	\$ (1,245)	46	77,002
Leasehold improvements	702	-	-	-	702
Library materials	45	105	-	-	150
Subtotal	134,346	3,449	(1,245)	2,346	138,896
Total capital assets - cost	137,822	4,412	(1,245)	46	141,035
<b>Accumulated depreciation</b>					
Buildings	6,851	2,341	-	-	9,192
Land improvements	15	5	-	-	20
Equipment	52,657	7,132	(1,116)	4	58,677
Leasehold improvements	702	-	-	-	702
Library materials	30	9	-	-	39
Subtotal	60,255	9,487	(1,116)	4	68,630
Capital assets, net	\$ 77,567	\$ (5,075)	\$ (129)	\$ 42	\$ 72,405

## 6. Other Liabilities

Other liabilities of the Research Foundation consisted of the following at June 30, 2014 and 2013 (in thousands):

	2014					
	Beginning Balance	Additions	Retire- ments	Ending Balance	Current Portion	Noncurrent Portion
Other postemployment benefits	\$ 9,281	\$ 2,438	\$ (1,114)	\$ 10,605	\$ 1,716	\$ 8,889
Total	\$ 9,281	\$ 2,438	\$ (1,114)	\$ 10,605	\$ 1,716	\$ 8,889
	2013					
	Beginning Balance	Additions	Retire- ments	Ending Balance	Current Portion	Noncurrent Portion
Other postemployment benefits	\$ 8,213	\$ 1,967	\$ (899)	\$ 9,281	\$ 1,302	\$ 7,979
Total	\$ 8,213	\$ 1,967	\$ (899)	\$ 9,281	\$ 1,302	\$ 7,979

The current portion of other postemployment benefits is included in accounts payable and accrued liabilities in the statements of net position as of June 30, 2014 and 2013.



## 7. Revenues From Clinical Services

### a. Clinics and Laboratories

The University's Health Science Center 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 \$99.2 million and \$73.2 million for the years ended June 30, 2014 and 2013, 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 \$3.0 million and \$8.0 million for the years ended June 30, 2014 and 2013, 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 \$2.8 million and \$3.0 million for the years ended June 30, 2014 and 2013, respectively.

### c. KentuckyOne Health, Inc. Affiliation Agreement

In November, 2012, the University and KentuckyOne Health, Inc. (KentuckyOne) entered into an agreement that calls for, among other things, KentuckyOne to provide funding (salary, benefits, and malpractice coverage) for certain full-time equivalent resident positions over the term of the affiliation agreement at University of Louisville Hospital (Hospital). 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. Certain services continue to be provided by University Medical Center, Inc. (UMC). Funding from the affiliation agreements for the years ended June 30, 2014 and 2013 was approximately \$50.5 million and \$47.8 million, respectively. This agreement addresses the patient care needs of the Hospital's inpatients.

### d. University of Louisville Physicians, Inc. (ULP)

During the fiscal year ended June 30, 2013, most existing practice groups became subsidiary entities to ULP, which was established to integrate the faculty practice arrangement for clinical services. In March 2013, ULP reached an agreement with the Medical School Practice Association (MSPA) doing business as University Physician Associates to acquire substantially all the assets of MSPA and assume the remaining liability to Passport. At the same time certain funding from the Medicaid HMO, Passport Health Plan (safety net funding) was transferred to ULP.

The Medical School Fund, UMC, ULP, 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 \$50.4 million and \$41.9 million for the years ended June 30, 2014 and 2013, respectively.

8. Expenses

Operating expenses by natural classification for the years ended June 30, 2014 and 2013 were approximately (in thousands):

	<u>2014</u>	<u>2013</u>
Salaries and wages	\$ 185,672	\$ 186,659
Employee benefits	45,480	44,496
Supplies and services	87,578	79,728
Depreciation	9,205	9,481
Scholarships and fellowships	41,160	40,991
	<u>\$ 369,095</u>	<u>\$ 361,355</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 \$12.3 million and \$12.1 million during the years ended June 30, 2014 and 2013, 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.

Effective July 1, 2012, the life insurance benefit was restructured to be priced as a fully insured supplemental benefit for which the retirees pay 100% of the cost, so no obligation is assumed after the fiscal year ended June 30, 2012.

b. Funding Policy

The Plan is funded on a pay-as-you-go basis. During the years ended June 30, 2014 and 2013, the University contributed approximately \$1.7 million and \$1.0 million, approximately 68% and 56% of total premiums, respectively. Retired Plan members under age 65 receiving benefits contributed approximately \$0.8 million for each year, approximately 32% and 44% of total

premiums for the years ended June 30, 2014 and 2013, respectively, through their required monthly contributions according to the schedules below:

<b>2014</b>					
	<b>PPO</b>	<b>Cardinal Care Plan</b>	<b>EPO</b>	<b>PCA High</b>	<b>PCA Low</b>
Employee	\$ 389	\$ 459	\$ 431	\$ 279	\$ 208
Employee and Spouse	\$ 763	\$ 868	\$ 850	\$ 583	\$ 451
<b>2013</b>					
	<b>PPO</b>	<b>Cardinal Care Plan</b>	<b>EPO</b>	<b>PCA High</b>	<b>PCA Low</b>
Employee	\$ 389	\$ 419	\$ 431	\$ 279	\$ 208
Employee and Spouse	\$ 763	\$ 828	\$ 850	\$ 583	\$ 451

Medicare-eligible retirees receive a monthly benefit of \$108 per individual covered. For the years ended June 30, 2014 and 2013, the University contributed \$1.3 million and \$1.2 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>2014</b>	<b>2013</b>
Normal cost	\$ 4,188	\$ 4,190
AAL amortization	4,789	4,693
Annual required contribution (ARC)	8,977	8,883
Interest on above	994	717
Adjustment to ARC	(1,362)	(880)
OPEB liability gain	(1,792)	(3,244)
Annual OPEB cost (AOC)	6,817	5,476
Contributions made	(3,048)	(2,221)
Increase in net OPEB obligation	3,769	3,255
Net OPEB obligation - beginning of year	27,300	24,045
Net OPEB obligation - end of year	<u>\$ 31,069</u>	<u>\$ 27,300</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 Cost/(Gain)	Percentage of Annual OPEB Cost/(Gain) Contributed	Net OPEB Obligation
2014	\$ 6,817	45%	\$ 31,069
2013	\$ 5,476	41%	\$ 27,300
2012	\$ 3,337	61%	\$ 24,045

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, 2014 and 2013, the Research Foundation's portion of the AOC was \$2.4 million and \$2.0 million, respectively. The Research Foundation's net OPEB obligation for the years ended June 30, 2014 and 2013 was \$10.6 million and \$9.3 million, of which \$8.9 million and \$8.0 million was recorded in other long-term liabilities and \$1.7 million and \$1.3 million was recorded in accounts payable and accrued liabilities as of June 30, 2014 and 2013, respectively.

d. Funded Status and Funding Progress

As of July 1, 2013, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability for benefits was \$85.3 million and \$82.3 million and there were no assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$85.3 million and \$82.3 million as of June 30, 2014 and 2013, respectively. The covered payroll (annual payroll of active employees covered by the Plan) was \$445.0 million and \$426.8 million, and the ratio of the UAAL to the covered payroll was 19% for each of the years ended June 30, 2014 and 2013.

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 in time. 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, 2013, actuarial valuation, the unit credit method actuarial cost method was used. The actuarial assumptions included a 3 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 7.5 percent initially, reduced by decrements to an ultimate rate of 4.5 percent after 12 years. The gains on the benefit obligation recognized during the fiscal years ended June 30, 2014 and 2013 were due to updates made on expected future health claims and changes made to the retiree life insurance benefit. 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, 2014 was 23 years.

#### 11. Restatement of Prior Years' Financial Statements

The Research Foundation's audited financial statements for June 30, 2013, issued on October 2, 2013 have been restated to properly reflect amounts receivable from third parties not previously included in revenue. The net effect of this misstatement resulted in an increase of \$8.1 million in unrestricted net position as of July 1, 2012 and an increase in the decrease in net position of \$1.9 million for the year ended June 30, 2013, for a net increase in unrestricted net position of \$6.2 million as of June 30, 2013.

#### 12. Commitments and Contingencies

##### a. Commitments

At June 30, 2014 and 2013, respectively, the Research Foundation had approximately \$5.6 million and \$11.4 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 coverages 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 expenditure 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.

#### 13. Recent Accounting Pronouncements

GASB has issued additional standards, Statement No. 66, *Technical Corrections – 2012 – An Amendment of GASB Statements No. 10 and No. 62*; Statement No. 67, *Financial Reporting for Pension Plans – An Amendment of GASB Statement No. 25*; Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*; Statement No. 69, *Government Combinations and Disposals of Government Operations*; and Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. The Research Foundation does not believe the implementation of these standards will significantly impact the financial statements.

**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>
7/1/2013	-	\$ 85,282	\$ 85,282	0%	\$ 444,970	19%
7/1/2012	-	\$ 82,260	\$ 82,260	0%	\$ 426,752	19%
7/1/2011	-	\$ 79,912	\$ 79,912	0%	\$ 416,016	19%