

UNIVERSITY OF LOUISVILLE RESEARCH FOUNDATION, INC.

A Component Unit of the University of Louisville

**Auditor's Report and Financial Statements
June 30, 2016 and 2015**

UNIVERSITY OF LOUISVILLE RESEARCH FOUNDATION, INC.

A Component Unit of the University of Louisville

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INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of 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, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Research Foundation's basic financial statements as listed in the table of contents.

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 entity'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 entity'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 that 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, 2016 and 2015, and the changes in its financial position and its cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 12, and the Schedule of Funding Progress on page 29, to be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by 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.

Crowe Horwath LLP

Crowe Horwath LLP

Louisville, Kentucky
November 18, 2016

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, 2016, 2015, and 2014. 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 maintained progress towards the goals established by the Kentucky Council on Postsecondary Education. During the fiscal year ended June 30, 2016, total awards were \$134.6 million, a decrease of \$2.3 million or 1.7%, as compared to fiscal year 2015. Some of the funding highlights include:

- \$7.1 million from the National Institutes of Health (NIH) for Kentucky IDeA Networks of Biomedical Research Excellence
- \$3.3 million from the National Institutes of Health (NIH) for Griffiths in-based Rectal Microbicides for PREvention of Viral ENTry (PREVENT)
- \$2.5 million from the National Institutes of Health (NIH) for Protection of Ischemic Myocardium-CORE A
- \$2.3 million from the National Institutes of Health (NIH) for COBRE-CORE A Center for Excellence in Diabetes

The Research Foundation faculty continued to receive national recognition. In an effort to understand how specific genetic factors coupled with lifetime exposure to cigarette smoking and secondhand smoke may influence a woman's ability to conceive, University of Louisville researchers have been awarded a three-year, \$440,000 grant from the Eunice Kennedy Shriver National Institute of Child Health & Human Development.

Financial Highlights

- The Research Foundation's financial position remains strong at June 30, 2016, with total assets of \$116.5 million and liabilities of \$54.5 million as compared to June 30, 2015 at \$112.8 million of total assets and \$40.0 million of liabilities. Net position, which represent the residual interest in the Research Foundation's assets after liabilities are deducted, was \$62.0 million and \$72.7 million for the years ended June 30, 2016 and 2015, respectively.
- The Research Foundation's total liabilities of \$54.5 million contain grant advances. Grant advances represent the unearned portion of grants and sponsored programs and comprise \$2.0 million or 3.6% of total liabilities.

- Operating revenues amounted to \$365.6 million and \$337.1 million and operating expenditures were \$409.6 million and \$369.6 million resulting in a net operating loss of \$44.0 million and \$59.5 million for the years ended June 30, 2016 and 2015, respectively. When adjusted for net nonoperating revenues of \$33.2 million and \$54.4 million, net position of the Research Foundation decreased by \$10.8 million and \$5.1 million for the years ended June 30, 2016, and 2015, respectively.

Using the Financial Statements

The Research Foundation's financial report includes 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 \$43.4 million and \$43.3 million in nonexchange grants and contract revenue for the years ended June 30, 2016 and 2015, 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 \$2.0 million and \$7.9 million as of June 30, 2016 and 2015, respectively.
- Capital assets are depreciated and reported net of accumulated depreciation. The Research Foundation's capital assets as of June 30, 2016 and 2015 consist primarily of buildings, equipment and library materials with a net position value of \$66.0 million and \$70.1 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, 2016, 2015, and 2014 is summarized on the following page:

Condensed Statements of Net Position
June 30, 2016, 2015, and 2014
(In Thousands)

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2016 - 2015</u> <u>Change</u>	<u>2015 - 2014</u> <u>Change</u>
ASSETS					
Current assets	\$ 49,750	\$ 41,899	\$ 46,347	\$ 7,851	\$ (4,448)
Capital assets	65,989	70,132	74,365	(4,143)	(4,233)
Other noncurrent assets	719	735	617	(16)	118
Total assets	<u>116,458</u>	<u>112,766</u>	<u>121,329</u>	<u>3,692</u>	<u>(8,563)</u>
LIABILITIES					
Current liabilities	41,822	28,926	34,657	12,896	(5,731)
Noncurrent liabilities	12,684	11,120	8,889	1,564	2,231
Total liabilities	<u>54,506</u>	<u>40,046</u>	<u>43,546</u>	<u>14,460</u>	<u>(3,500)</u>
NET POSITION					
Net investment in capital assets	65,990	70,132	74,365	(4,142)	(4,233)
Restricted - expendable	21,791	7,490	1,689	14,301	5,801
Unrestricted	(25,829)	(4,902)	1,729	(20,927)	(6,631)
Total net position	<u>\$ 61,952</u>	<u>\$ 72,720</u>	<u>\$ 77,783</u>	<u>\$ (10,768)</u>	<u>\$ (5,063)</u>

Assets

A review of the Research Foundation's statement of net position at June 30, 2016 indicates that the Research Foundation is highly liquid with nearly \$50 million in current assets. Of the \$49.8 million in current assets, \$49.0 million, or 99%, consists of accounts receivable that are to be collected within the next year.

Noncurrent assets consist mainly of \$66.0 million of capital assets, which decreased due to additional capital assets of \$3.8 million offset by \$7.9 million in depreciation and \$1.8 million disposals.

Liabilities

The Research Foundation's current liabilities consist of amounts due to the University of \$26.5 million for funding of operational expenses. This amount increases \$20.6 million from the prior year. Additionally, current liabilities include \$2.0 million of unexpended cash advances for sponsored research activities, a decrease of \$5.8 million compared to June 30, 2015. 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. Decrease is due to fewer cash advances from the expiration of grants. The remaining \$13.3 million of current liabilities relates to trade accounts payable and other accrued liabilities. The Research Foundation's allocated portion of other post-employment benefits totals \$14.3 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, 2016 and 2015 was \$62.0 million and \$72.7 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

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. Capital assets decreased by \$4.1 million from 2015. This decrease reflects \$7.9 million of depreciation and \$1.8 million of disposals partially offset by additions of \$3.8 million.

Restricted expendable net position

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, 2016. The amounts remain restricted until the contract is completed.

Restricted expendable net position increased \$14.3 million, or 191%. The overall increase is due mainly to an increase in nongovernmental grants.

Unrestricted net position

Unrestricted net position decreased by \$20.9 million. The decrease in unrestricted net position results primarily from actual operating expenses exceeding clinical services and fixed contract revenues.

Fiscal Year 2015

The Research Foundation's financial position as of the fiscal year ended June 30, 2015 shows a decrease in assets and an increase in liabilities with an overall decrease in net position. Assets decreased during the fiscal year ended June 30, 2015 by \$8.6 million, or 7%, as compared to the fiscal year ended June 30, 2014. This decrease was due mainly to the \$4.4 million decrease in current accounts receivable and \$4.2 million decrease in capital assets. The increase in liabilities mainly resulted from the increase in accounts payable, which increased \$2.4 million from the fiscal year ended June 30, 2014.

Net position decreased \$5.1 million, or 7%, compared to net position at June 30, 2014 due mainly to the \$6.6 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, 2016, 2015, and 2014 is shown on the following page:

Condensed Statements of Revenues, Expenses and Changes in Net Position
Years ended June 30, 2016, 2015, and 2014
(In Thousands)

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2016 - 2015</u> <u>Change</u>	<u>2015 - 2014</u> <u>Change</u>
OPERATING REVENUES					
Clinical services	\$ 233,866	\$ 222,445	\$ 205,879	\$ 11,421	\$ 16,566
Grants and contracts	103,120	89,924	91,405	13,196	(1,481)
Facilities and administrative cost recoveries	24,611	22,596	21,965	2,015	631
Other operating revenues	3,989	2,160	6,419	1,829	(4,259)
Total operating revenues	<u>365,586</u>	<u>337,125</u>	<u>325,668</u>	<u>28,461</u>	<u>11,457</u>
OPERATING EXPENSES					
Depreciation	7,914	8,470	9,205	(556)	(735)
Other operating expenses	401,651	388,139	359,890	13,512	28,249
Total operating expenses	<u>409,565</u>	<u>396,609</u>	<u>369,095</u>	<u>12,956</u>	<u>27,514</u>
Operating loss	<u>(43,979)</u>	<u>(59,484)</u>	<u>(43,427)</u>	<u>15,505</u>	<u>(16,057)</u>
NONOPERATING REVENUES (EXPENSES)					
Nonexchange grants and contracts	43,417	43,313	41,706	104	1,607
Other nonoperating revenues	(10,206)	11,108	(14,315)	(21,314)	25,423
Total nonoperating revenues	<u>33,211</u>	<u>54,421</u>	<u>27,391</u>	<u>(21,210)</u>	<u>27,030</u>
Decrease in net position	<u>(10,768)</u>	<u>(5,063)</u>	<u>(16,036)</u>	<u>(5,705)</u>	<u>10,973</u>
NET POSITION					
Net position, beginning of year	72,720	77,783	93,819	(5,063)	(16,036)
Net position, end of year	<u>\$ 61,952</u>	<u>\$ 72,720</u>	<u>\$ 77,783</u>	<u>\$ (10,768)</u>	<u>\$ (5,063)</u>

Operating Revenues

The Research Foundation recognized \$365.6 million in operating revenues for the year ended June 30, 2016. This represents an 8% increase in revenues from the \$337.1 million reported for the year ended June 30, 2015.

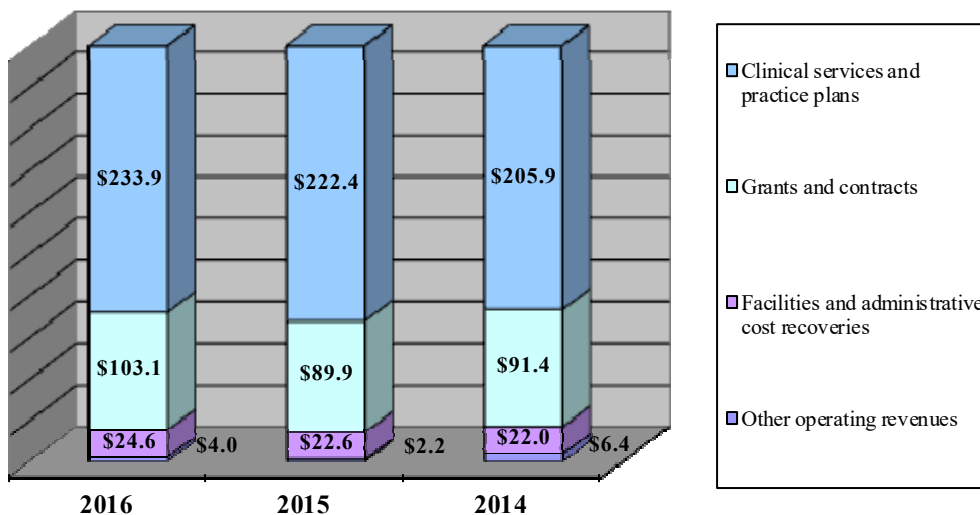
Revenues from clinical services were \$233.9 million for the year ended June 30, 2016. This is an increase of approximately \$11.4 million, or 5%, compared to \$222.4 million in similar revenues reported for the year ended June 30, 2015. The majority of the increase is attributed to increases in Medicaid related patient and intergovernmental transfers.

Revenues from grants and contracts were \$103.1 million for the year ended June 30, 2016 as compared to \$89.9 million in revenues reported in the previous year. This includes an increase of \$10.5 million in nongovernmental grants and contracts and an increase of \$5.4 million in federal grants and contracts. The increase was partially offset by a \$2.7 million decrease in state and local grants for the year ended June 30, 2016, as compared to the previous year.

Revenue from facilities and administrative cost recoveries were \$24.6 million and \$22.6 million for the years ended June 30, 2016 and 2015, respectively. The Research Foundation, compensates the University for a portion of the cost recoveries in support of expenditures. For the years ended June 30, 2016 and 2015, approximately \$10.0 million and \$9.0 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, 2016, 2015, and 2014 (in millions).

Operating Revenues
Years Ended June 30, 2016, 2015, and 2014

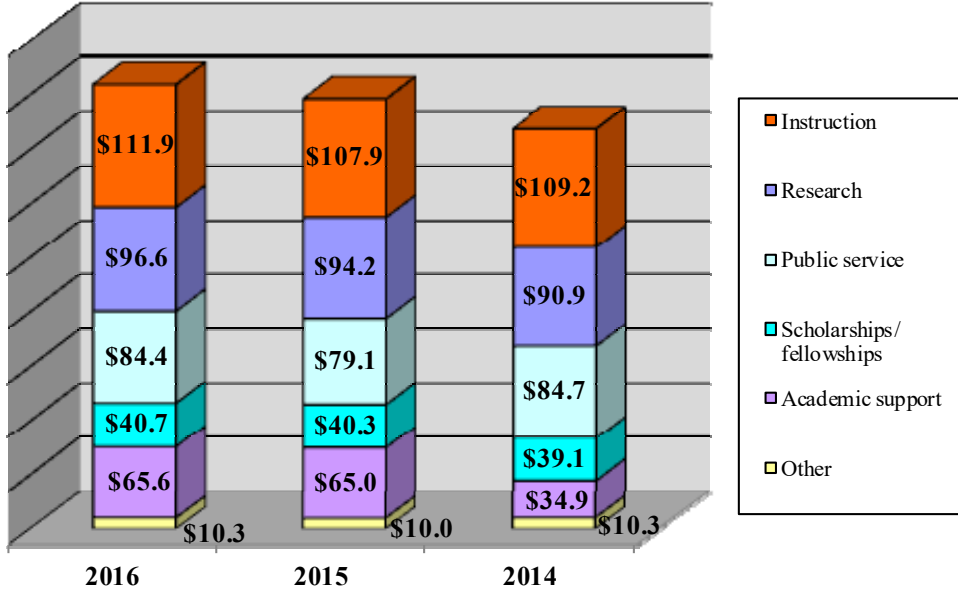


Operating Expenses by Functional and Natural Class

Total operating expenses were \$409.6 million and \$396.6 million for the fiscal years ended June 30, 2016 and 2015, respectively. The primary reason for the increase of \$13.0 million, or 3.2%, is an increase of \$10.2 million in salary expense as shown in the operating expenses by natural classification chart on the following page. Expenses in functional classification for instruction, research and public service all increased due to the increases in salaries.

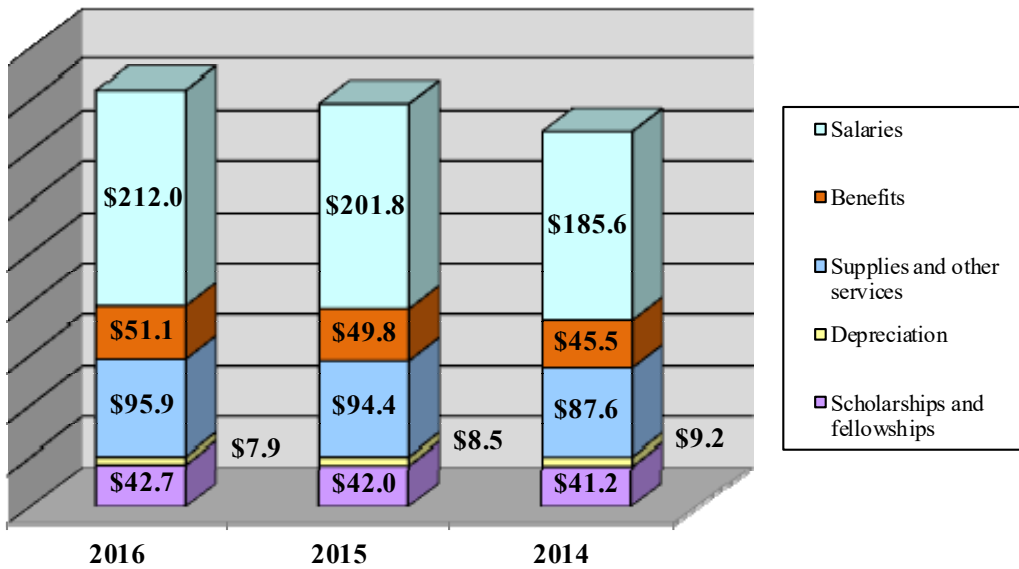
The following is a graphic illustration of total operating expenses by function for the years ended June 30, 2016, 2015 and 2014 (in millions):

**Operating Expenses by Functional Classification
Years ended June 30, 2016, 2015, and 2014**



The following is a graphic illustration of total operating expenses by natural classification for the years ended June 30, 2016, 2015 and 2014 (in millions):

**Operating Expenses by Natural Classification
Years ended June 30, 2016, 2015, and 2014**



Nonoperating Revenues (Expenses)

The Research Foundation's total nonoperating revenues of \$33.2 million for fiscal year ended June 30, 2016, was mostly comprised of nonexchange grants and contract revenues of \$43.4 million and transfer expenses of \$11.9 million. Total nonoperating revenues decreased by \$17.5 million as compared to fiscal year ended June 30, 2015. The decrease is due primarily to the Research Foundation received a gift of \$8.6 million from UPG (University Physician's Group) to ULRF in fiscal year ending June 30, 2015. There was no such grant in fiscal year ending June 30, 2016. The Foundation transferred \$3.1 million to the University of Louisville Real Estate Foundation, Inc. in fiscal year 2016 for shared cost of a pediatric office building.

Fiscal Year 2015

For the year ended June 30, 2015, Research Foundation reported \$337.1 million in operating revenues, an increase of 4% compared to the \$325.7 million reported for the year ended June 30, 2014.

Revenues from clinical services were \$222.4 million for fiscal year 2015, an increase of 8% from the fiscal year ended June 30, 2014. The increase in revenues was due mainly from increased clinical service and practice plan revenue of \$24.5 million primarily related to the increased number of Medicaid patients served.

Revenue from facilities and administrative cost recoveries were \$22.6 million and \$22.0 million for the years ended June 30, 2015 and 2014, respectively. The Research Foundation transferred to the University, approximately \$9.0 million and \$9.5 million during the years ended June 30, 2015 and 2014, respectively, in recognition of indirect support provided by the University.

Total operating expenses were \$396.6 million and \$369.1 million for the fiscal years ended June 30, 2015 and 2014, respectively. The increase of \$27.5 million, or 7%, was an increase in academic support expenses related to increased contractual expenses and additional operational costs associated with the increased number of Medicaid patients.

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, 2016, 2015, and 2014, are summarized on the following page:

Condensed Statements of Cash Flows
Years ended June 30, 2016, 2015, and 2014
(In Thousands)

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2016 - 2015</u> <u>Change</u>	<u>2015 - 2014</u> <u>Change</u>
Cash (used)/provided by:					
Operating activities	\$ (49,994)	\$ (47,088)	\$ (47,977)	\$ (2,906)	\$ 889
Noncapital and related financing activities	53,750	50,527	37,374	3,223	13,153
Capital financing activities	(3,809)	(4,247)	(11,359)	438	7,112
Investing activities	53	808	-	(755)	808
Net decrease in cash	-	-	(21,962)	-	21,962
Cash and cash equivalents, beginning of year	-	-	21,962	-	(21,962)
Cash and cash equivalents, end of year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Operating Activities

The Research Foundation's operating activities used approximately \$50.0 million of cash during the fiscal year ended June 30, 2016, representing an increase of \$2.9 million compared to the prior year. While all categories of operating activities experienced an increase in cash activities the most significant were the increase in cash inflow from grants and contracts of \$6.9 million and the increase in cash outflow for payments to employees of \$10.1 million from operations during the fiscal year ended June 30, 2016.

Other Activities

The \$53.8 million cash provided by noncapital and related financing activities relates mainly to the \$43.4 million provided by nonexchange grants and contracts and due to the University of \$20.6 million. It also includes the Research Foundation's transfer of \$10.0 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 increased \$3.2 million from the fiscal year ended June 30, 2015.

Cash used for capital financing activities decreased \$0.4 million to \$3.8 million during the fiscal year ended June 30, 2016, due to a decrease in capital assets purchased.

Fiscal Year 2015

The Research Foundation operating activities used approximately \$47.1 million of cash during the fiscal year ended June 30, 2015, representing a decrease of \$0.9 million compared to the prior year. While cash received from clinical services increased \$34.6 million it was offset by an increase of \$30.0 million of cash outflows from operations during the fiscal year ended June 30, 2015.

The \$50.5 million cash provided by noncapital and related financing activities relates mainly to the \$43.3 million provided by nonexchange grants and contracts. It also includes the Research Foundation's transfer of \$8.2 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 activities decreased \$13.2 million from the fiscal year ended June 30, 2014, due in part to the receipt of \$9.7 million due to the grant from UPG to the Research Foundation. UPG had an investment in KMRRRG, a captive insurance, and withdrew from the captive during the year, in which an approximately \$8.9 million return of investment.

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 the University's 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 2016 budget.

Continued state appropriation cuts are anticipated for the future. The fiscal year 2017 budgeted state appropriations are \$132.8 million, a decrease of \$8.4 million, or 5%, from the fiscal year 2016 budget. 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 2017 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 "21st 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 continued budget cuts, 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. This progress is 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, 2016 and 2015
(In Thousands)

	2016	2015
ASSETS		
Current Assets:		
Accounts receivable, net	\$ 49,049	41,088
Inventories	395	374
Other assets	306	437
Total current assets	49,750	41,899
Noncurrent Assets:		
Accounts receivable, net	717	733
Other long-term assets	2	2
Capital assets, net	65,989	70,132
Total noncurrent assets	66,708	70,867
Total assets	116,458	112,766
LIABILITIES		
Current Liabilities:		
Accounts payable and accrued liabilities	13,275	15,131
Due to University of Louisville	26,533	5,938
Grant advances	2,014	7,857
Total current liabilities	41,822	28,926
Noncurrent Liabilities:		
Other long-term liabilities	12,684	11,120
Total noncurrent liabilities	12,684	11,120
Total liabilities	54,506	40,046
NET POSITION		
Net investment in capital assets	65,989	70,132
Restricted - expendable for:		
Research	14,888	5,320
Instruction	223	308
Public service	5,669	1,760
Scholarships and fellowships	-	96
Academic support	6	6
Institutional Support	1,005	-
Unrestricted	(25,828)	(4,902)
Total net position	\$ 61,952	\$ 72,720

See notes to 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, 2016 and 2015
(In Thousands)

	2016	2015
OPERATING REVENUES		
Clinical services, net of contractual allowances of \$88,870 in 2016 and \$83,594 in 2015	\$ 233,866	\$ 222,445
Federal grants and contracts	69,752	64,388
State and local grants and contracts	8,660	11,345
Nongovernmental grants and contracts	24,708	14,191
Other operating revenue	3,989	2,160
Facilities and administrative cost recoveries	24,611	22,596
Total operating revenues	365,586	337,125
OPERATING EXPENSES		
Instruction	111,925	107,945
Research	96,622	94,212
Public service	84,359	79,098
Scholarships and fellowships	40,739	40,260
Academic support	65,583	65,014
Institutional support	2,342	1,131
Operation and maintenance of plant	67	479
Depreciation	7,914	8,470
Student services	9	9
Service centers	5	(9)
Total operating expenses	409,565	396,609
Operating loss	(43,979)	(59,484)
NONOPERATING REVENUES (EXPENSES)		
Gifts	1,491	9,652
Nonexchange grants and contracts	43,417	43,313
Investment income	10	-
Net realized and unrealized gain on investments	53	808
Other nonoperating income	161	8,867
Net nonoperating revenues	45,132	62,640
Contributions to related entities	(8,833)	(8,219)
Contributions to University of Louisville Real Estate Foundation, Inc.	(3,088)	-
Total other revenues	33,211	54,421
Decrease in net position	(10,768)	(5,063)
NET POSITION		
Net position - beginning of year	72,720	77,783
Net position - end of year	\$ 61,952	\$ 72,720

See notes to 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, 2016 and 2015
(In Thousands)

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Clinical services	\$ 228,962	\$ 227,077
Grants and contracts	93,990	87,113
Facilities and administrative cost recoveries	24,611	22,596
Other operating revenue	4,234	2,131
Payments to employees	(211,528)	(201,431)
Payments for benefits	(49,644)	(47,486)
Payments for scholarships and fellowships	(42,716)	(42,020)
Payments to suppliers	(97,903)	(95,068)
Net cash used by operating activities	<u>(49,994)</u>	<u>(47,088)</u>
CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES		
Contributions to/from related entities	(11,921)	(8,219)
Gifts	1,491	9,652
Nonexchange grants and contracts	43,417	43,314
Due to (due from) University of Louisville	20,595	(3,085)
Other noncapital financing activity	168	8,865
Net cash provided by noncapital and related financing activities	<u>53,750</u>	<u>50,527</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchases of capital assets	(3,809)	(4,247)
Net cash used by capital and related financing activities	<u>(3,809)</u>	<u>(4,247)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Sales of investments	53	808
Net cash provided by investing activities	<u>53</u>	<u>808</u>
Net decrease in cash and cash equivalents	-	-
Cash and cash equivalents - beginning of year	-	-
Cash and cash equivalents - end of year	<u>\$ -</u>	<u>\$ -</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating loss	\$ (43,979)	\$ (59,484)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation	7,914	8,470
Loss on disposal of equipment	39	11
Changes in assets and liabilities:		
Accounts receivable, net	(7,944)	4,251
Inventories	(21)	(20)
Other assets	132	99
Accounts payable and accrued liabilities	(1,856)	(235)
Grant advances	(5,845)	(2,411)
Other long-term liabilities	1,566	2,231
Net cash used by operating activities	<u>\$ (49,994)</u>	<u>\$ (47,088)</u>

See notes to financial statements.

University of Louisville Research Foundation, Inc.

A Component Unit of the University of Louisville

Notes to Financial Statements

June 30, 2016 and 2015

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, 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 online at the following:
<http://louisville.edu/finance/controller/univacct/finst-1>

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 acquisition 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, *Basic Financial Statements-And Managements Discussion and Analysis-For State and Local Governments*, such as investment income.

g. Deferred Inflows of Resources and Net Position

In addition to assets, GASB No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, 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 \$2.0 million and \$7.9 million as of June 30, 2016 and 2015, 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 2015 amounts have been reclassified to conform to the 2016 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 Foundation's 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 \$10.0 million and \$9.0 million for the years ended June 30, 2016 and 2015, respectively. Additional research support transfers to the University totaled \$1.2 million for the year ending June 30, 2015.

The Research Foundation transferred \$5.2 million and \$2.3 million related to capital projects and debt service payments during the fiscal years ended June 30, 2016 and 2015, 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, 2016 and 2015, the Research Foundation was the recipient of \$5.0 million and \$4.1 million, respectively, from related entities to assist in funding cost share required by certain sponsored programs and grants.

Additionally, the Research Foundation received transfers of \$1.4 million and \$0.2 million from related entities for the years ended June 30, 2016 and 2015, respectively.

The Research Foundation transferred \$3.1 million to the University of Louisville Real Estate Foundation, Inc. to fund shared construction cost of a pediatric building enhancements.

4. Accounts Receivable, net

Accounts receivable, net as of June 30, 2016 and 2015, are summarized as follows (in thousands):

	2016		
	Gross		Net
	Receivable	Allowance	Receivable
Patient care	\$ 72,045	\$ (42,072)	\$ 29,973
Sponsored agreements	22,533	(2,740)	19,793
Total	<u>\$ 94,578</u>	<u>\$ (44,812)</u>	49,766
Current portion			49,049
Noncurrent portion			<u>\$ 717</u>
	2015		
	Gross		Net
	Receivable	Allowance	Receivable
Patient care	\$ 63,313	\$ (37,663)	\$ 25,650
Sponsored agreements	18,651	(2,740)	15,911
Other receivables	260	-	260
Total	<u>\$ 82,224</u>	<u>\$ (40,403)</u>	41,821
Current portion			41,088
Noncurrent portion			<u>\$ 733</u>

5. Capital Assets, net

Capital assets at historical cost as of June 30, 2016 and 2015 are summarized as follows (in thousands):

	2016				
	Beginning Balance	Additions	Retire- ments	Transfers	Ending Balance
Cost - Non depreciable					
Land	\$ 352	\$ -	\$ -	\$ -	\$ 352
Construction in progress	-	-	-	-	-
Subtotal	<u>352</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>352</u>
Cost - Depreciable					
Building	70,727	-	-	-	70,727
Infrastructure	929	-	-	-	929
Land improvements	237	-	-	-	237
Equipment	82,525	3,809	(1,841)	-	84,493
Leasehold improvements	818	-	-	-	818
Library materials	44	-	-	-	44
Subtotal	<u>155,280</u>	<u>3,809</u>	<u>(1,841)</u>	<u>-</u>	<u>157,248</u>
Total capital assets - cost	<u>155,632</u>	<u>3,809</u>	<u>(1,841)</u>	<u>-</u>	<u>157,600</u>
Accumulated depreciation					
Buildings	14,357	2,874	-	-	17,231
Infrastructure	24	15	-	-	39
Land improvements	34	6	-	-	40
Equipment	70,340	5,009	(1,802)	-	73,547
Leasehold improvements	708	6	-	-	714
Library materials	37	3	-	-	40
Subtotal	<u>85,500</u>	<u>7,913</u>	<u>(1,802)</u>	<u>-</u>	<u>91,611</u>
Capital assets, net	<u>\$ 70,132</u>	<u>\$ (4,104)</u>	<u>\$ (39)</u>	<u>\$ -</u>	<u>\$ 65,989</u>

	2015				
	Beginning Balance	Additions	Retire- ments	Transfers (to)/ from Affiliates	Ending Balance
Cost - Non depreciable					
Land	\$ 352	\$ -	\$ -	\$ -	\$ 352
Construction in progress	8,515	641	-	(9,156)	-
Subtotal	<u>8,867</u>	<u>641</u>		<u>(9,156)</u>	<u>352</u>
Cost - Depreciable					
Building	61,534	37	-	9,156	70,727
Infrastructure	930	-	-	-	930
Land improvements	237	-	-	-	237
Equipment	79,434	3,454	(362)	-	82,526
Leasehold improvements	702	116	-	-	818
Library materials	44	-	-	-	44
Subtotal	<u>142,881</u>	<u>3,607</u>	<u>(362)</u>	<u>9,156</u>	<u>155,282</u>
Total capital assets - cost	<u>151,748</u>	<u>4,248</u>	<u>(362)</u>	<u>-</u>	<u>155,634</u>
Accumulated depreciation					
Buildings	11,580	2,778	-	-	14,358
Infrastructure	9	15	-	-	24
Land improvements	26	6	-	-	32
Equipment	65,032	5,662	(351)	-	70,343
Leasehold improvements	702	6	-	-	708
Library materials	34	3	-	-	37
Subtotal	<u>77,383</u>	<u>8,470</u>	<u>(351)</u>	<u>-</u>	<u>85,502</u>
Capital assets, net	<u>\$ 74,365</u>	<u>\$ (4,222)</u>	<u>\$ (11)</u>	<u>\$ -</u>	<u>\$ 70,132</u>

6. Other Liabilities

Other liabilities of the Research Foundation consisted of the following at June 30, 2016 and 2015 (in thousands):

	2016					
	Beginning Balance	Additions	Retire- ments	Ending Balance	Current Portion	Noncurrent Portion
Other postemployment benefits	\$ 12,884	\$ 2,294	\$ (841)	\$ 14,337	\$ 1,653	\$ 12,684
Total	<u>\$ 12,884</u>	<u>\$ 2,294</u>	<u>\$ (841)</u>	<u>\$ 14,337</u>	<u>\$ 1,653</u>	<u>\$ 12,684</u>
	2015					
	Beginning Balance	Additions	Retire- ments	Ending Balance	Current Portion	Noncurrent Portion
Other postemployment benefits	\$ 10,605	\$ 3,436	\$ (1,157)	\$ 12,884	\$ 1,764	\$ 11,120
Total	<u>\$ 10,605</u>	<u>\$ 3,436</u>	<u>\$ (1,157)</u>	<u>\$ 12,884</u>	<u>\$ 1,764</u>	<u>\$ 11,120</u>

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, 2016 and 2015.

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 \$118.2 million and \$109.5 million for the years ended June 30, 2016 and 2015, 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 \$1.1 million and \$1.5 million for the years ended June 30, 2016 and 2015, 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 \$1.2 million and \$0.9 million for the years ended June 30, 2016 and 2015, 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, 2016 and 2015 was approximately \$60.7 million and \$61.2 million, respectively. This agreement addresses the patient care needs of the Hospital's inpatients.

d. Norton Healthcare

In December 17, 2015, Norton Healthcare, Inc., (Norton) and the University of Louisville and the Commonwealth of Kentucky agreed to a Settlement Agreement, a First Amendment to Lease and a First Amendment to Master Affiliation Agreement. These agreements provide for \$30.0 million annual support payments from Norton to the University and its affiliates through Individual Agreements for research, academic support, residences and fellowships and related costs. In addition, the agreement stipulates that Norton provide additional financial support to the University of Louisville Pediatrics Department of \$24.0 million over eight years and expend at least \$35.0 million in facility improvements and other capital expenditures at Kosair Children's Hospital. Payments received by the University and its affiliates are included in clinical services and practice plan revenues in the statements of revenues, expenses, and changes in net position. Funding for the agreement for the years ended June 30, 2016 and 2015 was \$35.0 million and

\$31.7 million, respectively. The Settlement Agreement also included a payment of \$8.0 million to the Research Foundation for expenses incurred.

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 \$17.6 million and \$18.3 million for the years ended June 30, 2016 and 2015, respectively.

8. Expenses

Operating expenses by natural classification for the years ended June 30, 2016 and 2015 were approximately (in thousands):

	<u>2016</u>	<u>2015</u>
Salaries and wages	\$ 211,954	\$ 201,938
Employee benefits	51,098	49,765
Supplies and services	95,883	94,416
Depreciation	7,914	8,470
Scholarships and fellowships	42,716	42,020
	<u>\$ 409,565</u>	<u>\$ 396,609</u>

9. Retirement Plan

University personnel participate in a contributory retirement plan administered by the University. The University of Louisville 403(b) Retirement Plan (Retirement Plan) was established by the University and approved by the Board of Trustees. Permanent, full-time employees become eligible to participate in a defined contribution plan upon completion of one year's service and attainment of age 21. Eligible employees not contributing to the Retirement Plan are entitled to a 7.5% of base salary contribution on their behalf by the University. The University also matches up to an additional 2.5% of employee contributions. The Retirement Plan requires three years of continuous service for employees to vest in employer contributions.

The Research Foundation recorded expenses related to the defined contribution plan of approximately \$13.9 million and \$13.5 million during the years ended June 30, 2016 and 2015, respectively. As of June 30, 2016 and 2015, the Research Foundation had no outstanding liability related to the Retirement Plan.

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. The Plan is a single-employer plan and the University's Board of Trustees determines the eligibility requirements related to the Plan. The Plan does not issue stand-alone financial reports and is not included in the report of any entity.

b. Funding Policy

The Plan is funded on a pay-as-you-go basis. The contribution requirements of the contributing members are determined by the University's management on an annual basis. During the years ended June 30, 2016 and 2015, the University contributed approximately \$1.9 million and \$1.7 million, approximately 66% and 65% of total premiums, respectively. Retired Plan members under age 65 receiving benefits contributed approximately \$1.0 million and \$0.9 million, approximately 35% of total premiums for the years ended June 30, 2016 and 2015, respectively, through their required monthly contributions according to the schedules below:

2016					
	PPO	Cardinal Care Plan	EPO	PCA High	PCA Low
Employee	\$ 335	\$ 447	\$ 353	\$ 281	\$ 248
Employee and Spouse	\$ 811	\$ 871	\$ 851	\$ 692	\$ 555
2015					
	PPO	Cardinal Care Plan	EPO	PCA High	PCA Low
Employee	\$ 335	\$ 407	\$ 353	\$ 281	\$ 248
Employee and Spouse	\$ 811	\$ 831	\$ 851	\$ 692	\$ 555

Medicare-eligible retirees receive a monthly benefit of \$108 per individual covered. For the years ended June 30, 2016 and 2015, the University contributed \$1.6 million and \$1.5 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):

	<u>2016</u>	<u>2015</u>
Normal cost	\$ 5,061	\$ 4,536
AAL amortization	5,252	5,095
Annual required contribution (ARC)	10,313	9,631
Interest on above	1,258	1,171
Adjustment to ARC	(1,825)	(1,669)
OPEB liability gain	(3,566)	(8)
Annual OPEB cost (AOC)	6,180	9,125
Contributions made	(2,437)	(3,195)
Increase in net OPEB obligation	3,743	5,930
Net OPEB obligation - beginning of year	36,999	31,069
Net OPEB obligation - end of year	<u>\$ 40,742</u>	<u>\$ 36,999</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 (in-thousands):

<u>Fiscal Year</u> <u>Ended June 30,</u>	<u>Annual</u> <u>OPEB</u> <u>Cost/(Gain)</u>	<u>Percentage of</u> <u>Annual OPEB</u> <u>Cost/(Gain)</u> <u>Contributed</u>	<u>Net OPEB</u> <u>Obligation</u>
2016	\$ 6,180	39%	\$ 40,742
2015	\$ 9,125	35%	\$ 36,999
2014	\$ 6,817	45%	\$ 31,069
2013	\$ 5,476	41%	\$ 27,300

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, 2016 and 2015, the Research Foundation's portion of the AOC was \$2.3 million and \$3.4 million, respectively. The Research Foundation's net OPEB obligation for the years ended June 30, 2016 and 2015 was \$14.3 million and \$12.9 million, of which \$12.7 million and \$11.1 million was recorded in other long-term liabilities and \$1.7 million and \$1.8 million was recorded in accounts payable and accrued liabilities as of June 30, 2016 and 2015, respectively.

d. Funded Status and Funding Progress

As of July 1, 2014, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability for benefits was \$89.7 million and \$89.1 million and there were no assets, resulting in an unfunded actuarial accrued liability (UAAL) of \$89.7 million and \$89.1 million as of June 30, 2016 and 2015, respectively. The covered payroll (annual payroll of active employees covered by the Plan) was \$478.2 million and \$459.6 million, and the ratio of the UAAL to the covered payroll was 19% for each of the years ended June 30, 2016 and 2015.

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, 2014, 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 7.3 percent initially, reduced by decrements to an ultimate rate of 4.5 percent after 11 years. The gains on the benefit obligation recognized during the fiscal years ended June 30, 2016 and 2015 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, 2016 was 21 years.

11. Commitments and Contingencies

a. Commitments

At June 30, 2016 and 2015, respectively, the Research Foundation had approximately \$5.2 million and \$0.3 million in encumbrances outstanding related mainly to operational expenses 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.

12. Recent Accounting Pronouncements

As of June 30, 2016, the GASB has issued the following statements which were implemented by the Research Foundation.

GASB Statement No. 72, *Fair Value Measurement and Application*. This standard requires state and local governments to measure certain assets and liabilities held as investments at fair value. This standard enhances financial statements by providing consistent and accepted valuation techniques for fair value measurement. The implementation of this Statement had no financial impact and additional disclosure requirements.

As of June 30, 2016, the following GASB statements wer implemented which did not have a financial or disclosure impact on the financial statements.

GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This Statement identifies, in the context of the current governmental financial reporting environment, the hierarchy of generally accepted accounting principles in the United States of America.

GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*. This Statement enhances comparability of financial statements among governments by establishing specific criteria used to determine whether a qualifying external investment pool may elect to use an amortized cost exception to fair value measurement.

As of June 30, 2016, the GASB has issued the following statements that could be applicable to the Research Foundation.

- a. GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. The Research Foundation has not yet adopted this standard and is evaluating the impact it may have on its financial statements.
- b. GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. The Research Foundation has not yet adopted this standard and is evaluating the impact it may have on its financial statements.
- c. GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. The Research Foundation has not yet adopted this standard and is evaluating the impact it may have on its financial statements.
- d. GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*. The Research Foundation has not yet adopted this standard and is evaluating the impact it may have on its financial statements.
- e. GASB Statement No. 80, *Blending Requirements for Certain Component Units-an amendment of GASB Statement No. 14*. The Research Foundation has not yet adopted this standard and is evaluating the impact it may have on its financial statements.

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

Actuarial Value Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a) / c)
7/1/2016	-	\$ 89,683	\$ 89,683	0%	\$ 478,201	19%
7/1/2015	-	\$ 89,098	\$ 89,098	0%	\$ 459,588	19%
7/1/2014	-	\$ 85,282	\$ 85,282	0%	\$ 444,970	19%