

FINANCIAL REPORT

2012 2013

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Current as of June 30, 2013

**Northern Kentucky University and Affiliate
A Component Unit of the Commonwealth of Kentucky
Annual Financial Report
2012-2013**

Table of Contents

Letter from the President	2
Report of Independent Auditors.....	3
Management’s Discussion and Analysis.....	5
Financial Statements	
Northern Kentucky University and Affiliate Consolidated Statements of Net Position.....	12
Northern Kentucky University Foundation, Inc. Consolidated Statements of Financial Position	13
Northern Kentucky University and Affiliate Consolidated Statements of Revenues, Expenses and Changes in Net Position	14
Northern Kentucky University Foundation, Inc. Consolidated Statements of Activities	15
Northern Kentucky University and Affiliate Consolidated Statements of Cash Flows.....	17
Northern Kentucky University and Affiliate Notes to the Consolidated Financial Statements	18

September 25, 2013

Northern Kentucky University Board of Regents
Highland Heights, KY 41099



Dear Members of the Board:

I am pleased to share the University's 2012-13 Annual Financial Report. The firm of Dean Dorton Allen Ford, PLLC, has audited the following statements and accompanying footnotes. The University ends the fiscal year and begins the new academic year in a strong financial position.

The University's financial performance for the year was strong. The University's unrestricted net position increased by nearly \$6 million for the year as a result of positive operating performance. Excellent investment returns for the year contributed to a significant growth in the University's endowment funds that are managed by the NKU Foundation. For the five-year period ending June 30, 2013, the endowment funds managed by the Foundation have grown from \$51 million to \$83 million. The continued growth in funds provided through endowments, gifts, and other sources of revenues will be essential as the University strives to meet the needs of our students, despite declining state and federal funding.

As a result of sound fiscal management and generous philanthropic support, our faculty, staff and students produced many achievements this past year.

This year's freshman class is the most academically qualified class in our University's history. This achievement is the result of a deliberate enrollment strategy to recruit outstanding students. That strategy included allocating more resources for student scholarships.

We are not just attracting more students. We are also producing more graduates. This past year, NKU graduated nearly 3,000 students, including the largest undergraduate class in the University's history.

In support of improving our retention and graduation rates, we invested in the creation of a Student Success Center. The facility, located on the first two floors of University Center, now contains our most important student support activities. This center is more than a shared location. Within it we have integrated the activities of these support offices to provide a seamless experience for our students.

In the area of scholarship, NKU'S commitment to research and creative activity is stronger than ever. Last year, nearly 600 students collaborated with 126 faculty on research or creative projects, the highest numbers for student and faculty participation in the University's history.

It is no secret that substantial challenges are ahead for higher education. But our future is filled with many opportunities and with great potential.

In January 2014, NKU launches a new five-year strategic plan. This plan represents an important opportunity for us to focus our efforts and continue our progress on behalf of our students. Our paramount institutional goal will continue to be student success.

I am optimistic that we will succeed, because this institution has a history of success — and because of the quality and character of the people this University attracts and retains.

Sincerely,

A handwritten signature in black ink, appearing to read "G Mearns". The signature is fluid and cursive, with the first name "Geoffrey" and last name "Mearns" clearly distinguishable.

Geoffrey S. Mearns
President

DEAN||DORTON||ALLEN||FORD

Report of Independent Auditors

Members of the Board of Regents and
Mr. Geoffrey S. Mearns, President
Northern Kentucky University

And

Secretary of Finance and
Administration Cabinet of the
Commonwealth of Kentucky

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of the business-type activities and discretely presented component unit of Northern Kentucky University (the University), as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, which collectively comprise the University'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 consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these consolidated 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 consolidated 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 consolidated 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 consolidated 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 consolidated financial statements.

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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 consolidated financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the discretely presented component unit of Northern Kentucky University as of June 30, 2013 and 2012, and the respective changes in financial position and 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 5 through 13 be presented to supplement the basic financial statements. Such information, although not a 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 audits 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.

Dean Dotson Allen Ford, PLLC

October 2, 2013
Lexington, Kentucky

Northern Kentucky University and Affiliate Management's Discussion and Analysis

Northern Kentucky University's (the University) Management Discussion and Analysis of its financial condition provides an overview of the financial performance of the University for the year ended June 30, 2013, with selected comparative information for the years ended June 30, 2012 and 2011. This discussion has been prepared by management and should be read in conjunction with the accompanying financial statements and notes.

As a public comprehensive university located in a major metropolitan area, Northern Kentucky University delivers innovative, learner-centered education and engages in impactful scholarly and creative activities, all of which empower students for fulfilling careers and meaningful lives, while contributing to the social and economic vitality of the region. The University is vital to the economic and social progress of this region and the Commonwealth.

Financial Highlights

The University's financial position remains relatively strong at June 30, 2013. An increase in nonrecurring reserves and positive auxiliary enterprise operating results contributed to a \$5.8 million increase in unrestricted net position for the year. The University's total net position decreased by \$3.8 million, or 1.2 percent, for the year as a result of a \$6.1 million decrease in net invested in capital assets net position and a \$3.5 million decrease in restricted expendable net position for the year.

A \$4.4 million increase in net tuition and fees contributed to a \$5.0 million increase in operating revenues for the year. Net nonoperating revenues declined by \$1.9 million for the year primarily due to a \$2.9 million decline in the University's state appropriations and a \$0.5 million decrease in federal nonoperating grant revenues due to a decline in federal financial aid program revenues. These declines were partially offset by a \$1.3 million increase in investment income which was driven by excellent endowment returns for the year.

The University's state-funded endowments totaled \$11.3 million and \$10.2 million as of June 30, 2013 and 2012, respectively. These funds, along with the private endowed gifts donated to benefit the University, are managed by Northern Kentucky University Foundation, Inc. (Foundation). The endowment funds managed by the Foundation, including the University's endowment funds, totaled \$82.7 million and \$74.3 million at June 30, 2013 and 2012, respectively. For the five-year period ended June 30, 2013, the endowment funds managed by the Foundation have grown from \$51.0 million to \$82.7 million as a result of excellent investment returns and the receipt of several major endowment gifts.

Using the Financial Statements

The University's financial report includes three financial statements: the statements of net position; the statements of revenues, expenses and changes in net position and the statement of cash flows. These financial statements and accompanying footnotes are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities and require that financial statements be presented on a consolidated basis to focus on the University as a whole.

The University is a component unit of the Commonwealth of Kentucky. The financial statements of the University include the University and its blended component unit, the Northern Kentucky University Research Foundation, Inc. (Research Foundation). Financial statements for the University's discretely presented component unit, Northern Kentucky University Foundation, Inc., have also been included in accordance with the requirements of GASB Statement No. 39. Financial statements presented for the Foundation consist of the statement of financial position and the statement of activities. These statements are prepared in accordance with Financial Accounting Standards Board (FASB) pronouncements.

Statement of Net Position

The statement of net position includes all assets and liabilities. It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. Net position, consisting of the net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources, is one indicator of the current financial condition of the University. Assets and liabilities are generally measured using current values. A major exception is capital assets, which are stated at historical cost less accumulated depreciation.

A three year summarized comparison of the University's assets, liabilities and net position at June 30 follows:

Condensed Statements of Net Position (in thousands)

	2013	2012	2011
ASSETS			
Current assets	\$ 95,653	\$ 98,187	\$ 81,448
Capital assets, net	319,115	326,938	334,866
Noncurrent assets	43,213	45,220	33,098
Total assets	<u>457,981</u>	<u>470,345</u>	<u>449,412</u>
LIABILITIES			
Current liabilities	29,936	31,490	34,319
Noncurrent liabilities	108,762	115,513	94,341
Total liabilities	<u>138,698</u>	<u>147,003</u>	<u>128,660</u>
DEFERRED INFLOWS OF RESOURCES	<u>1,785</u>	<u>2,049</u>	<u>2,313</u>
NET POSITION			
Invested in capital assets, net of related debt	224,099	230,200	239,790
Restricted			
Nonexpendable	7,616	7,616	7,616
Expendable	5,175	8,661	9,117
Unrestricted	80,608	74,816	61,916
Total net position	<u>\$ 317,498</u>	<u>\$ 321,293</u>	<u>\$ 318,439</u>

The statement of net position at June 30, 2013 reflects the University's strong financial position.

Assets

The University's assets decreased by \$12.4 million, or 2.6 percent, for the year ended June 30, 2013 and now total \$458.0 million. A \$2.5 million decrease in current assets for the year ended June 30, 2013 combined with a \$16.7 million increase for the year ended June 30, 2012, resulted in a combined increase of \$14.2 million, or 17.4 percent, since June 30, 2011. Noncurrent assets, excluding net capital assets, grew by \$10.1 million since 2011 due to a \$12.2 increase in agency deposits held in a stream and wetland restoration fund by the Research Foundation pursuant to a memorandum of agreement with a federal agency. This increase was partially offset by a decrease in bond reserve accounts that were liquidated to pay the final debt service payments on several Consolidated Educational Building Revenue Bond issues that matured in 2012 and 2013.

Net capital assets decreased by \$7.8 million for the year ended June 30, 2013 and decreased by \$7.9 million for the year ended June 30, 2012, resulting in a combined decrease of \$15.7 million, or 4.7 percent, since June 30, 2011. This decline is the net result of a \$25.8 million increase in capitalized construction project costs, land improvements, equipment and other capital assets, less \$41.5 million in depreciation. Net capital assets totaled \$319.1 million, or 69.7 percent of total assets as of June 30, 2013.

Liabilities

At June 30, 2013, the University's liabilities totaled \$138.7 million compared to the previous year's \$147.0 million. This \$8.3 million decrease in liabilities resulted from a \$6.1 million reduction in long-term liabilities, including a \$6.0 million decline in outstanding bonds, notes and capital leases, and a \$2.2 million net decrease in accounts payable, accrued liabilities and other liabilities. Bonds, notes and capital leases payable, net of discounts, premiums and deferred losses on bond refundings, represented \$93.4 million, or 67.4 percent, of total liabilities at June 30, 2013.

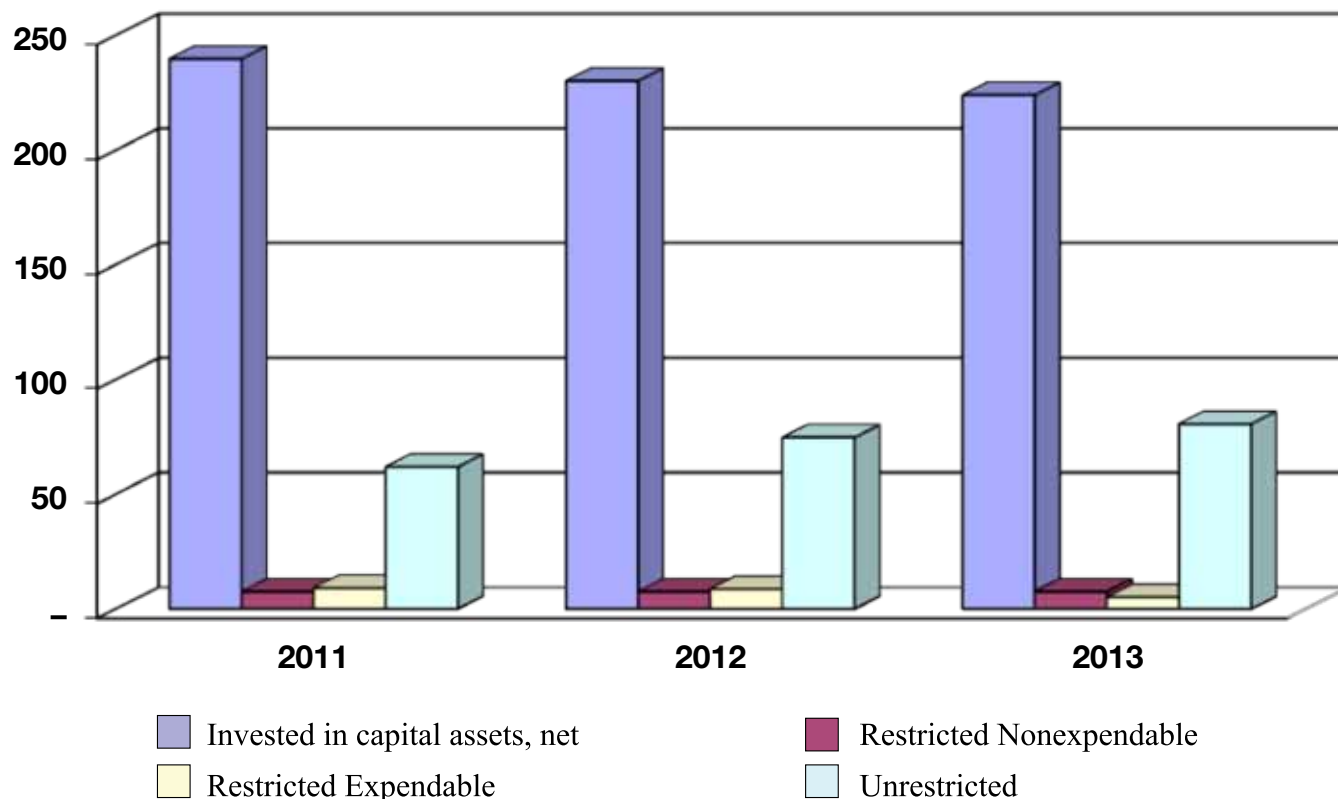
The University's total liabilities increased by \$10.0 million, or 7.8 percent, from June 30, 2011 to June 30, 2013. Current liabilities declined by \$4.4 million while noncurrent liabilities increased by \$14.4 million, primarily due to a \$12.2 million increase in agency deposits held by the Research Foundation.

Deferred Inflows of Resources

Deferred inflows of resources totaled \$1.8 million and \$2.0 million as of June 30, 2013 and 2012, respectively. The deferred inflows, which resulted from a service concession agreement between the University and a food service provider, are being amortized over the life of the service agreement.

Net Position

The following chart illustrates the University's net position for fiscal years 2011, 2012 and 2013 (presented in millions).



Net position represents the difference between the University's total of assets and deferred outflows of resources and the total of liabilities and deferred inflows of resources. The University's net position totaled \$317.5 million and \$321.3 million at June 30, 2013 and 2012, respectively. Net invested in capital assets totaled \$224.1 million, or 70.6 percent, of total net position. The University's restricted and unrestricted net position represented 4.0 percent and 25.4 percent of total net position, respectively. Total net position decreased by \$3.8 million, or 1.2 percent, for the year. Net invested in capital assets decreased \$6.1 million for the year resulting from depreciation expenses in excess of increases in new capital assets, net of debt. Restricted expendable resources declined \$3.5 million resulting from the expenditure of restricted construction funds. These declines in net position were partially offset by positive operating results which contributed to a \$5.8 million increase in unrestricted net position for the year.

The University's total net position decreased by \$0.9 million, or 0.3 percent, from June 30, 2011 to June 30, 2013. Depreciation expenses for the two year period exceeded additions to capital assets, net of related debt, resulting in a \$15.7 million decrease in invested in capital assets, net of related debt. The University's restricted expendable net position decreased by \$3.9 million while its unrestricted net position increased by \$18.7 million from June 30, 2011 to June 30, 2013.

Statement of Revenues, Expenses and Changes in Net Position

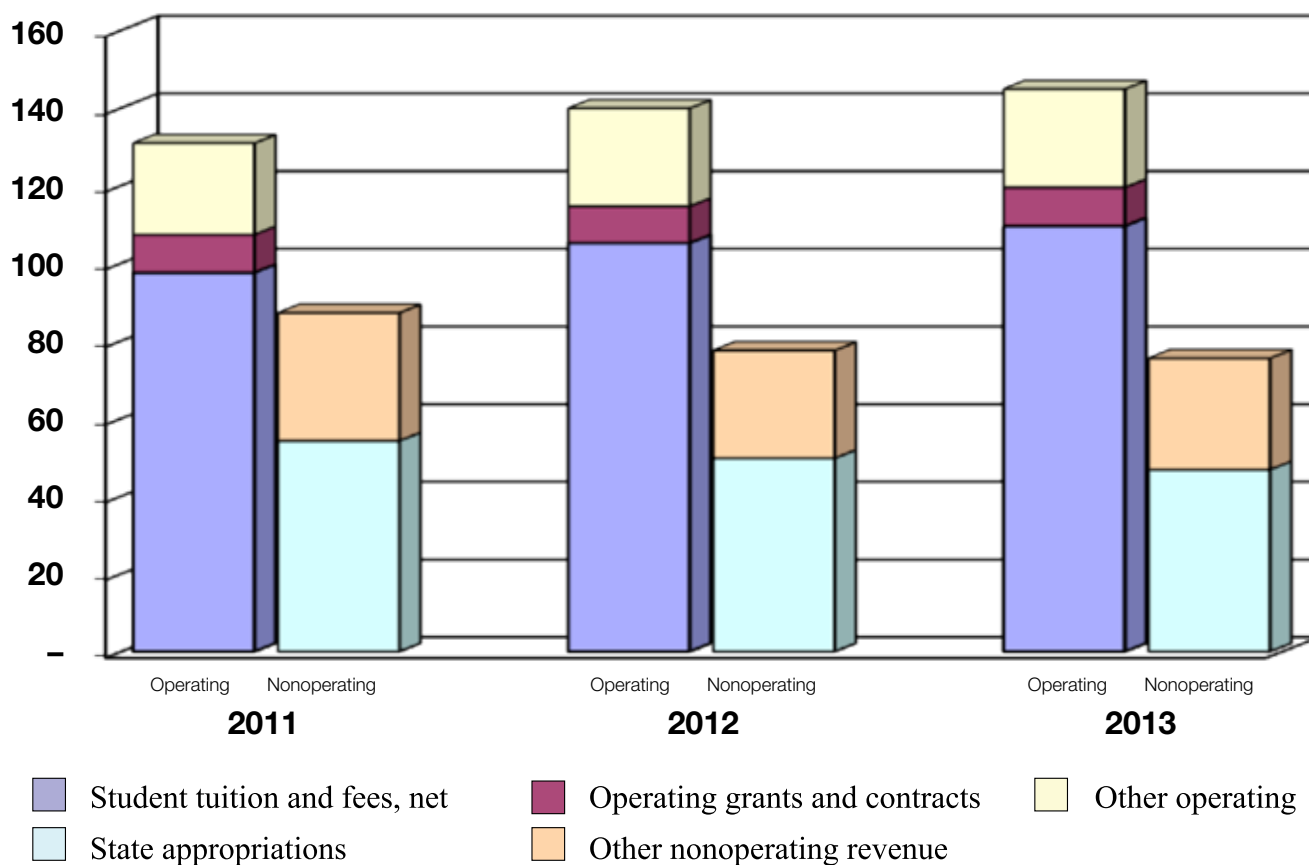
The statement of revenues, expenses and changes in net position presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. GASB requires state appropriations and nonexchange grants and contracts to be classified as nonoperating revenues. Accordingly, the University will generate an operating loss prior to the addition of nonoperating revenues. The utilization of long-lived assets, referred to as capital assets, is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life. A summarized comparison of the University's revenues, expenses and changes in net position for years ended June 30, 2013; June 30, 2012; and June 30, 2011 follows:

Condensed Statements of Revenues, Expenses and Changes in Net Position (in thousands)

	2013	2012	2011
OPERATING REVENUES			
Student tuition and fees, net	\$ 109,562	\$ 105,171	\$ 97,564
Grants and contracts	9,968	9,497	9,789
Sales and services of educational departments	4,751	4,407	4,066
Auxiliary enterprises	13,415	13,035	12,739
Other operating revenues	7,173	7,783	6,782
Total operating revenues	144,869	139,893	130,940
OPERATING EXPENSES			
Educational and general	193,772	188,176	178,443
Depreciation	17,954	17,963	16,280
Auxiliary enterprises (including depreciation)	9,022	8,231	10,249
Other expenses	44	64	43
Total operating expenses	220,792	214,434	205,015
Net loss from operations	(75,923)	(74,541)	(74,075)
NONOPERATING REVENUES (EXPENSES)			
State appropriations	46,835	49,744	54,258
Gifts, grants and contracts	27,150	27,567	30,205
Investment income	1,542	226	2,017
Interest on capital asset-related debt	(3,769)	(3,988)	(3,837)
Other nonoperating revenues (expenses)	(108)	(16)	742
Net nonoperating revenues	71,650	73,533	83,385
Income (loss) before other revenues, expenses, gains or losses	(4,273)	(1,008)	9,310
Capital appropriations	(80)	-	24,494
Capital grants and gifts	558	3,862	9,735
Total other revenues	478	3,862	34,229
Increase (decrease) in net position	(3,795)	2,854	43,539
Net position-beginning of year	321,293	318,439	274,900
Net position-end of year	\$ 317,498	\$ 321,293	\$ 318,439

Operating and Nonoperating Revenues

The following chart illustrates the University's revenues by source (both operating and nonoperating), which were used to fund its operating activities for fiscal years 2011, 2012 and 2013. Significant recurring sources of revenues, including state appropriations and nonexchange grants and contracts, are considered nonoperating revenues as defined by GASB. These revenues support operating expenses; therefore, they are included in the graph of revenues by source (presented in millions).



The University's operating and nonoperating revenues totaled \$220.4 million for the year ended June 30, 2013, an increase of \$3.0 million compared to 2012. Operating revenues totaled \$144.9 million, or 65.8 percent of revenues, while nonoperating revenues declined to \$75.5 million, or 34.2 percent of revenues, for the year. The most significant sources of revenue for the University are net student tuition and fees (49.7 percent) and state appropriations (21.2 percent).

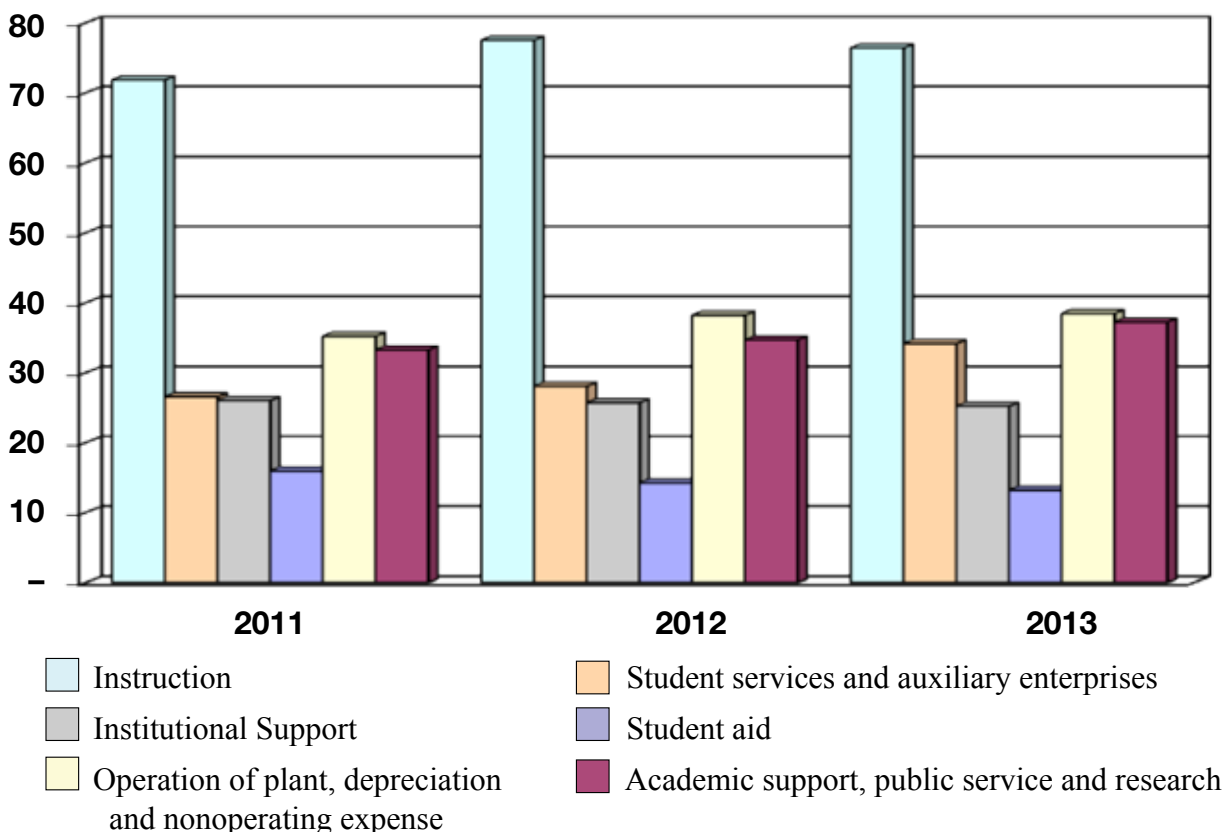
Operating revenues increased by \$5.0 million for the year with increases in net tuition and fees revenues (\$4.4 million), operating grants and contracts (\$0.5 million), auxiliary enterprises (\$0.4 million) and sales and services of educational activities (\$0.3 million). These increases were partially offset by a decrease in other operating revenues (\$0.6 million).

Nonoperating revenues declined by \$2.0 million for the year. The University's state appropriations decreased by \$2.9 million, as a result of a \$0.7 million decrease in debt service appropriations and a \$2.2 million decrease in general appropriations. The University's federal nonoperating grant revenues decreased by \$0.5 million for the year due to a decline in federal financial aid program revenues, including a \$0.3 million decrease in the Pell program. Increased endowment investment earnings resulted in a \$1.3 million increase in investment income for the year.

A \$13.9 million, or 10.6 percent, increase in operating revenues was fueled by a \$12.0 million growth in net tuition since 2011. The growth in net tuition resulted from average tuition rate increases of 4.6 percent for fiscal year 2013 and 5.0 percent for fiscal year 2012. The University's nonoperating revenues have declined by \$11.7 million since June 30, 2011 primarily due to a \$7.4 million decline in state appropriations and a \$4.3 million decline in other nonoperating revenues. The decline in state appropriations, in part, resulted from the elimination of \$3 million in federal stimulus funding that the University had received in fiscal year 2011. The decline in other nonoperating revenues is primarily attributable to a \$1.2 million decline in Pell program revenues and a \$1.2 million combined decrease resulting from the elimination of the federal SMART and academic competitiveness grant programs.

Operating and Nonoperating Expenses

The following chart illustrates the University's expenses by function (both operating and nonoperating) for fiscal years 2011, 2012 and 2013 (presented in millions).



Operating and nonoperating expenses increased by \$6.2 million, or 2.9 percent, to a total of \$224.7 million for the year ended June 30, 2013. As depicted in the chart above, the majority of the University's funds are expended directly for the primary mission of the University – instruction \$76.4 million (34.0 percent), and academic support, libraries, public service and research \$37.2 million (16.6 percent).

Instruction expenses decreased by \$1.1 million, or 1.4%, for the year ended June 30, 2013 due to a decline in nonrecurring instructional information technology expenses as compared to the prior year which included nonrecurring technology expenses related to the opening of Griffin Hall. This decline was partially offset by an increase in faculty and staff salaries and benefits. Increases in public service expenses funded by grants and revenue supplemented operations, such as the Center for Applied Informatics and The Bank of Kentucky Center, contributed to a \$0.9 million growth in public service expenses. A significant investment in student advising services and academic support technology resulted in a \$1.4 million increase in academic support expenses. Noncapital expenses related to the Student Success Center project and increased student recruitment expenses contributed to a \$5.3 million increase in student services expenses for the year. Student financial aid expenses decreased by \$1.0 million for fiscal year 2013 due, in part, to a decline in federal aid programs, including a \$0.3 million decrease in Pell grants. An increase in parking services expenses, primarily related to a garage maintenance and repair project, contributed to a net \$0.9 million increase in auxiliary enterprises expenses for the year.

Instruction, research, public service and academic support expenses grew by \$8.6 million, or 8.1%, since 2011 while institutional support, operation and maintenance of plant and interest expense on capital asset-related debt increased by only \$0.6 million, or 1.4%, since 2011. The significant increase in primary mission expenses was achieved by investing new resources and reallocating savings from cost containment efforts. The modest increase in institutional support and operation and maintenance of plant expenses reflects the University's continued effort to contain costs. Energy management initiatives have resulted in no increase in total utility costs even though new facilities, such as Griffin Hall, have opened since 2011.

Statement of Cash Flows

Another important factor to consider when evaluating financial viability is the University's ability to meet financial obligations as they become due. The statement of cash flows presents information related to cash inflows and outflows, summarized by operating, noncapital financing, capital and related financing, and investing activities.

Condensed Statements of Cash Flows (in thousands)

	2013	2012	2011
Net cash provided (used) by:			
Operating activities	\$ (58,849)	\$ (55,372)	\$ (52,238)
Noncapital financing activities	73,642	89,895	85,477
Capital and related financing activities	(21,841)	(5,371)	(19,610)
Investing activities	474	1,113	2,325
Net increase (decrease) in cash	(6,574)	30,265	15,954
Cash and cash equivalents, beginning of year	117,431	87,166	71,212
Cash and cash equivalents, end of year	<u>\$ 110,857</u>	<u>\$ 117,431</u>	<u>\$ 87,166</u>

The University's cash and cash equivalents decreased \$6.6 million in 2013 and increased \$30.3 million in 2012. The net cash provided by operating and noncapital financing activities totaled \$14.8 million for 2013, a decrease of \$19.7 million from 2012. A \$13.4 million decrease in cash deposits received by the Research Foundation on behalf of a federal agency and a \$2.9 million decline in cash provided by state appropriations resulted in a net decrease of \$16.3 million in net cash provided by noncapital financing activities. Cash used by capital and related financing activities totaled \$21.8 million for 2013 and \$5.4 million in 2012. Purchases of capital assets totaled \$13.0 million in 2013 and \$12.8 million in 2012 were primarily funded by capital lease and debt proceeds and by capital grants and gifts.

Major sources of funds included in operating activities are student tuition and fees (\$108.3 million), grants and contracts (\$9.4 million) and auxiliary enterprises (\$12.8 million). The largest cash payments for operating activities were made to employees (\$142.3 million) and to vendors and contractors (\$58.6 million). Payments to suppliers increased by \$0.2 million, or 0.4 percent, and payments for salaries and benefits increased by \$7.9 million, or 5.9 percent, for the year.

The University's cash receipts from operating activities increased by \$12.9 million, or 9.9 percent, from 2011 to 2013 while cash disbursements for operating activities increased by \$19.5 million, or 10.7 percent, for the period.

Capital Asset and Debt Administration

Capital Assets

Capital assets, net of accumulated depreciation, decreased by \$7.8 million for the year ended June 30, 2013. Additions to capital assets, net of disposals, during the year totaled \$13.0 million, including administrative software systems, technology related equipment, and renovations to the University Center, including the new Student Success Center. Depreciation expenses totaled \$20.8 million for the year. As of June 30, 2013, net capital assets totaled \$319.1 million, or 69.7 percent of total assets.

The University's net capital assets decreased by \$15.8 million from June 30, 2011 to June 30, 2013. This decline is the net result of a \$25.7 million increase in capitalized construction project costs, land improvements, equipment and other capital assets, less \$41.5 million in depreciation. Prior to June 30, 2011, the University's main campus underwent a dramatic transformation with the addition of Griffin Hall, The Bank of Kentucky Center, the James C. and Rachel M. Votruba Student Union, a soccer complex, parking facilities and numerous campus beautification projects. These projects have significantly enhanced the University's capacity to serve its students and the community.

At June 30, 2013, the University had several major projects in progress, including the design of a student campus recreation facility, the construction of new recreation fields and the reconstruction of the north plaza. In addition, numerous facility renovations were underway, including food service facility upgrades, roof repair and replacements, and instructional space upgrades.

Debt

The following is a summary of the University's outstanding debt summarized by revenue pledge as of June 30, 2013, 2012 and 2011 (in thousands):

	2013	2012	2011
General Receipts Bonds, net of discounts, premium and loss on refunding	\$ 85,723	\$ 83,155	\$ 77,609
Consolidated Educational Buildings Revenue Bonds, net of discounts	-	7,028	9,568
Housing and Dining System Revenue Bonds	1,475	1,635	1,790
Capital Lease - Residential Suites	-	500	980
Notes Payable and municipal lease obligations	6,218	7,137	3,002
	<u>\$ 93,416</u>	<u>\$ 99,455</u>	<u>\$ 92,949</u>

The University issued \$5.1 million, net of the premium and deferred loss on the refunding, of General Receipts Bonds in 2013 to refund \$5.7 million in outstanding Consolidated Educational Building Revenue Bonds resulting in a \$0.8 million present value savings. Notes payable and capital lease obligations totaling \$0.6 million were issued in 2013 to finance the acquisition of computer equipment and the renovation of a food service facility. The issuance of debt was offset by principal payments, retirements and amortization adjustments totaling \$11.7 million resulting in a \$6.0 million net decrease in outstanding debt for the year. This decrease was offset by a \$6.5 million increase in debt in fiscal year 2012, yielding a \$0.5 million net increase in outstanding debt since June 30, 2011.

A strong debt rating is an important indicator of the University's financial health. The University's current bond ratings assigned by Moody's Investors Service (A1) and Standard and Poor's (A) to the University's General Receipts and Consolidated Educational Building Revenue bonds reflect the University's solid financial position.

FACTORS IMPACTING FUTURE PERIODS

In November of 2012, the University launched into a new strategic planning process to develop a strategic plan for 2013-18. This plan is scheduled to be presented to the Board of Regents for approval in November 2013. This new strategic plan will guide us towards our 50th anniversary and lay the foundation for the next 50 years for the University.

The University's Board of Regents approved a 2.7 percent increase in undergraduate resident tuition rates for fiscal year 2014. In addition to this modest increase in tuition, student fees that will support the debt service and operating expenses related to the renovation and expansion of the A. D. Albright Health Center are scheduled to increase by \$4 per credit hour in fiscal year 2014. The University's Board of Regents has authorized the issuance of approximately \$53.2 million in General Receipts Bonds to finance this project and the acquisition and renovation of a student housing facility that will be supported by student fees. The University will be requesting the necessary approvals from the State Property and Buildings Commission and the Capital Projects and Bond Oversight Committee this fall.

Although the economy continues to show signs of improvement, the Commonwealth and the University still face budget challenges, including federal program funding reductions, and budgetary pressures related to the Medicaid program and the state pension systems. The 2012-14 biennial budget passed by the General Assembly reflects a \$48.6 million general state appropriation for the University for fiscal year 2013-14. University management does not anticipate a reduction in state appropriations for 2013-14. In addition, it is anticipated that our state appropriation will most likely remain flat for 2014-16 excluding any funding provided to cover increases in the Kentucky employer retirement system increases.

The General Assembly passed comprehensive pension reform as part of the 2012-13 legislation session, including the creation of a new defined contribution plan for all new state employees. As part of this reform measure, the legislature committed to funding the full actuarial required contribution rate in the 2014-16 biennial budget. Accompanying pension reform legislation were tax law changes intended to fund a portion of the full actuarial required contribution rate. It is not known whether additional state funds will be provided to the University to cover the cost of a significant increase in the employer contribution rate. It is projected that the total annual increase would be roughly \$5 million.

Beginning in fiscal year 2014-15, GASB Statement No. 68 requires governmental employers participating in a cost-sharing defined benefit pension plan to recognize their long-term obligation for pension benefits as a liability for the first time. As a participating employer in the Kentucky Employees Retirement System (KERS), the University will be required to report a net pension liability, pension expense and pension-related assets and liabilities based on its proportionate share of the collective amounts for all governmental entities in the KERS plan.

Although the Commonwealth and the University will continue to face economic uncertainties and other challenges, management believes the University is well positioned to achieve its strategic priorities in partnership with the Commonwealth, the Council on Postsecondary Education and the region. The University is continuing its efforts to diversify revenue sources, contain costs and redirect resources to core mission priorities. The University has made great strides in its effort to develop the capacity to fully support the region. The region's economic growth depends heavily on the University's capacity to support that growth in a variety of ways.

Northern Kentucky University and Affiliate
A Component Unit of the Commonwealth of Kentucky
Consolidated Statements of Net Position
June 30, 2013 and 2012
(in thousands)

	<u>2013</u>	<u>2012</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 82,910	\$ 86,789
Notes, loans and accounts receivable, net	10,386	9,094
Other current assets	2,357	2,304
Total current assets	<u>95,653</u>	<u>98,187</u>
Noncurrent Assets		
Cash and cash equivalents	27,947	30,642
Investments	13,277	12,209
Notes, loans and accounts receivable, net	1,660	2,102
Capital assets, net	319,115	326,938
Other noncurrent assets	329	267
Total noncurrent assets	<u>362,328</u>	<u>372,158</u>
Total assets	<u>457,981</u>	<u>470,345</u>
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	17,310	19,475
Unearned revenue	6,742	5,905
Long-term liabilities-current portion	5,884	6,110
Total current liabilities	<u>29,936</u>	<u>31,490</u>
Noncurrent Liabilities		
Deposits	17,549	18,291
Unearned revenue	471	573
Long-term liabilities	90,742	96,649
Total noncurrent liabilities	<u>108,762</u>	<u>115,513</u>
Total liabilities	<u>138,698</u>	<u>147,003</u>
DEFERRED INFLOWS OF RESOURCES		
Service concession arrangement revenue applicable to future years	<u>1,785</u>	<u>2,049</u>
NET POSITION		
Invested in capital assets, net of related debt	224,099	230,200
Restricted		
Nonexpendable	7,616	7,616
Expendable	5,175	8,661
Unrestricted	80,608	74,816
Total net position	<u>\$ 317,498</u>	<u>\$ 321,293</u>

See accompanying notes to the financial statements

Northern Kentucky University Foundation, Inc.
Consolidated Statements of Financial Position
As of June 30, 2013 and 2012
(in thousands)

	2013	2012
ASSETS		
Cash and cash equivalents	\$ 7,480	\$ 9,128
Loans, interest and accounts receivable, net	149	116
Accrued interest receivable	21	33
Contributions receivable, net	4,642	4,489
Prepaid expenses and deferred charges	42	36
Investments	84,005	73,563
Land and land improvements	548	548
Accumulated depreciation	(208)	(203)
Total assets	<u>96,679</u>	<u>87,710</u>
LIABILITIES AND NET ASSETS		
Accounts payable	250	258
Accrued interest payable	64	95
Annuities payable	191	242
Deferred income	26	26
Funds held in trust for Northern Kentucky University	11,277	10,209
Notes payable	<u>1,609</u>	<u>2,363</u>
Total liabilities	13,417	13,193
NET ASSETS		
Unrestricted		
For current operations	694	562
Contributions receivable	3	1
Amounts functioning as endowment funds	1,939	1,755
Invested in property, plant and equipment	<u>340</u>	<u>345</u>
Total unrestricted	<u>2,976</u>	<u>2,663</u>
Temporarily restricted		
Unexpended funds received for restricted purposes	6,005	4,922
Contributions receivable	4,409	4,175
Loan funds	136	138
Endowment funds	<u>28,911</u>	<u>22,139</u>
Total temporarily restricted	<u>39,461</u>	<u>31,374</u>
Permanently restricted		
Contributions receivable	230	313
Endowment funds	<u>40,595</u>	<u>40,167</u>
Total permanently restricted	<u>40,825</u>	<u>40,480</u>
Total net assets	<u>83,262</u>	<u>74,517</u>
Total liabilities and net assets	<u>\$ 96,679</u>	<u>\$ 87,710</u>

Northern Kentucky University and Affiliate
A Component Unit of the Commonwealth of Kentucky
Consolidated Statements of Revenues, Expenses and Changes in Net Position
For the Years Ended June 30, 2013 and 2012
(in thousands)

	<u>2013</u>	<u>2012</u>
OPERATING REVENUES		
Student tuition and fees (net of scholarship allowances of \$28,137 in 2013 and \$26,741 in 2012)	\$ 109,562	\$ 105,171
Federal grants and contracts	3,281	3,528
State and local grants and contracts	4,251	3,560
Nongovernmental grants and contracts	2,436	2,409
Sales and services of educational departments	4,751	4,407
Auxiliary enterprises		
Housing operations (net of scholarship allowances of \$740 in 2013 and \$576 in 2012)	8,646	8,574
Other auxiliaries	4,769	4,461
Other operating revenues	7,173	7,783
Total operating revenues	<u>144,869</u>	<u>139,893</u>
OPERATING EXPENSES		
Educational and general		
Instruction	76,420	77,538
Research	1,453	1,660
Public service	13,076	12,130
Libraries	4,950	4,475
Academic support	17,758	16,404
Student services	25,084	19,771
Institutional support	25,210	25,718
Operation and maintenance of plant	16,626	16,240
Depreciation	17,954	17,963
Student aid	13,195	14,240
Auxiliary enterprises		
Housing operations	4,215	4,309
Other auxiliaries	1,979	1,118
Auxiliary depreciation	2,828	2,804
Other expenses	44	64
Total operating expenses	<u>220,792</u>	<u>214,434</u>
Net loss from operations	<u>(75,923)</u>	<u>(74,541)</u>
NONOPERATING REVENUES (EXPENSES)		
State appropriations	46,835	49,744
Federal grants and contracts	19,423	19,936
State and local grants and contracts	7,663	7,599
Private gifts and grants	64	32
Investment income (loss)	1,542	226
Interest on capital asset-related debt	(3,769)	(3,988)
Other nonoperating revenues (expenses)	(108)	(16)
Net nonoperating revenues	<u>71,650</u>	<u>73,533</u>
Income (loss) before other revenues, expenses, gains or losses	<u>(4,273)</u>	<u>(1,008)</u>
Capital appropriations	(80)	-
Capital grants and gifts	558	3,862
Total other revenues	<u>478</u>	<u>3,862</u>
Increase (decrease) in net position	<u>(3,795)</u>	<u>2,854</u>
NET POSITION		
Net position-beginning of year	321,293	318,439
Net position-end of year	<u>\$ 317,498</u>	<u>\$ 321,293</u>

See accompanying notes to the financial statements

Northern Kentucky University Foundation, Inc.
Consolidated Statement of Activities
For the year ended June 30, 2013
(in thousands)

	<u>Unrestricted Net Assets</u>	<u>Temporarily Restricted Net Assets</u>	<u>Permanently Restricted Net Assets</u>	<u>Total</u>
CHANGES IN NET ASSETS:				
Revenues and Gains				
Gifts, grants and bequests	\$ 12	\$ 4,378	\$ 331	\$ 4,721
Rental income	119	-	-	119
Investment income	57	1,502	-	1,559
Net gain on investments	155	6,850	-	7,005
Other revenue	206	286	2	494
Total revenues and gains	549	13,016	333	13,898
Net assets released from restrictions	4,642	(4,642)	-	-
Total revenues and gains and other support	5,191	8,374	333	13,898
Program Expenses				
Instruction	619	-	-	619
Research	21	-	-	21
Public service	700	-	-	700
Libraries	15	-	-	15
Academic support	541	-	-	541
Student services	528	-	-	528
Institutional support	566	-	-	566
University facilities and equipment acquisition	210	-	-	210
Student financial aid	1,323	-	-	1,323
Total program expenses	4,523	-	-	4,523
Support Expenses				
Management and general	509	-	-	509
Fundraising support	114	-	-	114
Rental property	7	-	-	7
Total support expenses	630	-	-	630
Total expenses	5,153	-	-	5,153
Net transfers in (out)	275	(287)	12	-
Increase (decrease) in net assets	313	8,087	345	8,745
Net assets - beginning of year	2,663	31,374	40,480	74,517
Net assets - end of year	<u>\$ 2,976</u>	<u>\$ 39,461</u>	<u>\$ 40,825</u>	<u>\$ 83,262</u>

See accompanying notes to the financial statements

Northern Kentucky University Foundation, Inc.
Consolidated Statement of Activities
For the year ended June 30, 2012
(in thousands)

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total
CHANGES IN NET ASSETS:				
Revenues and Gains				
Gifts, grants and bequests	\$ 21	\$ 3,665	\$ 1,098	\$ 4,784
Rental income	118	-	-	118
Investment income	57	1,042	-	1,099
Net gains (losses) on investments	(40)	(1,246)	-	(1,286)
Other revenue	35	377	-	412
Total revenues and gains	191	3,838	1,098	5,127
Net assets released from restrictions	4,484	(4,484)	-	-
Total revenues and gains and other support	4,675	(646)	1,098	5,127
Program Expenses				
Instruction	590	-	-	590
Research	15	-	-	15
Public service	881	-	-	881
Libraries	31	-	-	31
Academic support	519	-	-	519
Student services	341	-	-	341
Institutional support	398	-	-	398
University facilities and equipment acquisition	446	-	-	446
Student financial aid	1,132	-	-	1,132
Total program expenses	4,353	-	-	4,353
Support Expenses				
Management and general	474	-	-	474
Fundraising support	98	-	-	98
Rental property	8	-	-	8
Total support expenses	580	-	-	580
Total expenses	4,933	-	-	4,933
Net transfers in (out)	181	(280)	99	-
Increase (decrease) in net assets	(77)	(926)	1,197	194
Net assets - beginning of year	2,740	32,300	39,283	74,323
Net assets - end of year	<u>\$ 2,663</u>	<u>\$ 31,374</u>	<u>\$ 40,480</u>	<u>\$ 74,517</u>

See accompanying notes to the financial statements

Northern Kentucky University and Affiliate
A Component Unit of the Commonwealth of Kentucky
Consolidated Statements of Cash Flows
For the Years Ended June 30, 2013 and 2012
(in thousands)

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	\$ 108,344	\$ 102,365
Grants and contracts	9,454	9,953
Payments to suppliers	(58,583)	(58,352)
Payments for salaries and benefits	(142,282)	(134,374)
Loans issued to students	(350)	(458)
Collection of loans to students	409	472
Auxiliary enterprise receipts:		
Housing operations	8,323	8,569
Other auxiliaries	4,485	4,198
Sales and service of educational departments	4,581	4,799
Other receipts (payments)	6,770	7,456
Net cash used by operating activities	<u>(58,849)</u>	<u>(55,372)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	46,835	49,744
Gifts and grants for other than capital purposes	27,430	27,279
Agency and loan program receipts	93,572	106,723
Agency and loan program disbursements	(94,087)	(93,835)
Other nonoperating receipts (payments)	(108)	(16)
Net cash provided by noncapital financing activities	<u>73,642</u>	<u>89,895</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt and leases	5,811	14,290
Capital appropriations	(80)	-
Capital grants, gifts, and advances received	984	5,030
Purchases of capital assets	(12,959)	(12,840)
Principal paid on capital debt and leases	(11,879)	(8,045)
Interest paid on capital debt and leases	(3,718)	(3,806)
Net cash used by capital and related financing activities	<u>(21,841)</u>	<u>(5,371)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	294	2,500
Purchase of investments	-	(2,000)
Interest on investments	180	613
Net cash provided (used) by investing activities	<u>474</u>	<u>1,113</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	<u>(6,574)</u>	<u>30,265</u>
Cash and cash equivalents-beginning of year	117,431	87,166
Cash and cash equivalents-end of year	<u><u>\$ 110,857</u></u>	<u><u>\$ 117,431</u></u>
RECONCILIATION OF NET OPERATING REVENUES (EXPENSES) TO NET CASH USED BY OPERATING ACTIVITIES:		
Net loss from operations	\$ (75,923)	\$ (74,541)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Depreciation expense	20,782	20,767
Changes in assets and liabilities:		
Receivables, net	(1,535)	(117)
Other assets	(87)	(248)
Accounts payable	(2,327)	(489)
Unearned revenue	739	(520)
Long-term liabilities	(234)	40
Deferred inflows of resources	(264)	(264)
Net cash used by operating activities	<u><u>\$ (58,849)</u></u>	<u><u>\$ (55,372)</u></u>

See accompanying notes to the financial statements

Northern Kentucky University and Affiliate
A Component Unit of the Commonwealth of Kentucky
Notes to the Consolidated Financial Statements
For the Years Ended June 30, 2013 and 2012

Note 1 – Organization and Summary of Significant Accounting Policies

a. Reporting Entity

Northern Kentucky University (the University) is a component unit of the Commonwealth of Kentucky and is included in the general-purpose financial statements of the Commonwealth. The consolidated financial statements of the University include the operations of the Northern Kentucky University Research Foundation; an affiliated non-profit corporation. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 61, condensed financial information for the Northern Kentucky University Research Foundation is provided in note 12.

The Northern Kentucky University Foundation, Inc. (the Foundation) is a legally separate, tax-exempt organization supporting the University. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The Foundation's Board of Directors is self-perpetuating and consists of graduates and friends of the University. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources the Foundation holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by the Foundation can only be used by, or for the benefit of, the University, the Foundation is considered a component unit of the University and is discretely presented in the University's consolidated financial statements. The accompanying consolidated financial statements do not include the financial position or operation results of the Chase College Foundation, Inc. This foundation is a separately incorporated not-for-profit entity organized for the purpose of promoting the educational mission of the University's Salmon P. Chase College of Law. Although this entity benefits the University's Salmon P. Chase College of Law, it is governed by an independent Board of Directors and is not controlled by the University.

b. Basis of Presentation

The accompanying consolidated financial statements of the University have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the GASB. During the year ended June 30, 2013, the University adopted GASB No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989, FASB and AICPA Pronouncements, which supersedes GASB Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, thereby eliminating the election provided in paragraph 7 of that statement for business-type activities to apply post-November 30, 1989, FASB statements and interpretations that do not conflict with or contradict GASB pronouncements. GASB No. 62 has been applied retrospectively and had no impact on the University's net position, changes in net position or financial reporting disclosures.

In accordance with GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities* (GASB 35) and subsequent standards issued by GASB, the University has elected to report as an entity engaged in business-type activities (BTA). BTAs are those activities that are financed in whole or part by fees charged to external parties for goods and services. GASB 35 establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following net position categories:

- **Invested in capital assets, net of related debt:** Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- **Restricted:**
 - Nonexpendable* – Net position subject to externally imposed stipulations that they be maintained permanently by the University.
 - Expendable* – Net position whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time. Expendable net position consists primarily of amounts for specified capital construction projects.
- **Unrestricted:** Net position whose use by the University is not subject to externally imposed stipulations. Unrestricted net position may be designated for specific purposes by action of management or the Board of Regents or may otherwise be limited by contractual agreements with outside parties.

The financial statement presentation required by GASB is intended to provide a comprehensive, entity-wide perspective of the University's assets, liabilities, net position, revenues, expenses, changes in net position and cash flows.

c. Accrual Basis

The financial statements have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation has been incurred.

d. Notes, Loans and Accounts Receivable

This classification consists of tuition and fee charges to students, charges for auxiliary enterprise services provided to students, faculty and staff, loans to students and amounts due from sponsors for reimbursement of expenses made pursuant to contracts and grants. Accounts receivable are recorded net of estimated uncollectible amounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

e. Capital Assets

Capital assets are stated at cost at date of acquisition or, in the case of gifts, at fair market value at date of gift. Equipment with a unit cost of \$5,000 or more and having an estimated useful life of greater than one year is capitalized. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred.

Depreciation of capital assets is computed on a straight-line basis over the estimated useful lives of the respective assets, generally 40 years for land improvements, 10 – 40 years for buildings and fixed equipment, 10 years for library books and 3 – 10 years for equipment. The University capitalizes, but does not depreciate, works of art and historical treasures that are held for exhibition, education, research and public service or intangible assets with an indefinite life. Indefinite life intangible assets are reviewed annually for impairment. If the fair value of the asset is less than the carrying amount, an impairment loss is recognized for the difference.

f. Inventories

Inventories are stated at cost (first-in, first-out or average cost).

g. Investments

Investments are stated at fair value.

h. Unearned Revenue

Unearned revenue includes amounts received for tuition and fees prior to the end of the fiscal year but related to the subsequent accounting period. Unearned revenue also includes amounts received from grants and contracts sponsors that have not yet been earned.

i. Deferred Inflow of Resources

A deferred inflow of resources resulted from a concession service agreement between the University and a food service provider. Significant consideration was received through up-front payments that are being amortized over the life of the contract. Deferred inflows are \$1,785,000 and \$2,049,000 as of June 30, 2013 and 2012, respectively.

j. Scholarship Allowances

Student tuition and fee revenues and other student related revenues are reported net of scholarship allowances in the consolidated statements of revenues, expenses and changes in net position. Scholarship allowances are the differences between the stated charge for services provided by the University, and the amounts that are paid by the students or third parties making payments on a student's behalf. To the extent that revenues from such programs are used to satisfy tuition and fees, and other student charges, the University has recorded a scholarship allowance.

k. Income Taxes

The University is an agency and instrumentality of the Commonwealth of Kentucky, pursuant to Kentucky Revised Statutes sections 164.290 through 164.475. Accordingly, the University is generally exempt from federal income taxes as an organization described in Section 115 of the Internal Revenue Code of 1986, as amended. The University's affiliated non-profit organization has received a determination from the Internal Revenue Service granting exemption from federal income taxation pursuant to the provisions of Internal Revenue Code section 501(c)(3).

l. Restricted Asset Spending Policy

The University's policy is that restrictions on assets cannot be fulfilled by the expenditure of unrestricted funds for similar purposes. The determination on whether restricted or unrestricted funds are expended for a particular purpose is made on a case-by-case basis. Restricted funds remain restricted until spent for the intended purpose.

m. Operating Activities

The University defines operating activities, as reported on the consolidated statements of revenues, expenses and changes in net position, as those that generally result from exchange transactions, such as payments received for providing goods and services and payments made for services and goods received. Nearly all of the University's expenses are from exchange transactions. Certain significant revenues relied upon for operations, such as state appropriations, gifts, and investment income, are recorded as nonoperating revenues, in accordance with GASB 35. In accordance with GASB Statement No. 24, *Accounting and Financial Reporting for Certain Grants and Other Financial Assistance* and related GASB implementation guidance, Pell Grants, College Access Program (CAP) Grants and Kentucky Educational Excellence Scholarship (KEES) are considered nonexchange transactions and are recorded as nonoperating revenues in the accompanying financial statements.

n. Use of Estimates

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

o. Component Unit Disclosure

The accompanying consolidated financial statements of the Foundation have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Financial Accounting Standards Board. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features.

During the years ended June 30, 2013, and 2012, the Foundation made payments on behalf of the University of \$2,490,000 and \$2,562,000, respectively. In addition, the Foundation transferred to the University \$2,033,000 in 2013 and \$1,791,000 in 2012 for restricted purposes. Complete financial statements for the Foundation can be obtained from the Northern Kentucky University Foundation, Inc. at Founder's Hall Room 120, Nunn Drive, Highland Heights, KY 41099.

p. Reclassifications

Certain items have been reclassified for the year ended June 30, 2012, in order to conform to classifications used for the year ended June 30, 2013. These reclassifications had no effect on total net position and the change in net position.

q. Recent Accounting Pronouncements

In June 2012, the GASB approved Statement No. 68, *Accounting and Financial Reporting for Pensions*. This Statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and Statement No. 50, *Pension Disclosures*, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits.

Governmental employers participating in a cost-sharing plan will also be required to report a net pension liability, pension expense and pension-related assets and liabilities based on their proportionate share of the collective amounts for all governments in the plan. All governments participating in the defined benefit pension plan would also have the following in their note disclosures:

- Descriptions of the plan and benefits provided
- Significant assumptions employed in the measurement of the net pension liability
- Descriptions of benefit changes and changes in assumptions
- Assumptions related to the discount rate and impact on the total pension liability of a 1 percentage point increase and decrease in the discount rate
- Net pension assets and liabilities

The provisions of this Statement are effective for fiscal years beginning after June 15, 2014. The University is currently evaluating the effects of this statement on its financial statements.

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. This statement also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term deferred in financial statement presentations. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. The University is currently evaluating the effects of this statement on its financial statements.

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this statement is to improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on net position. It alleviates uncertainty about reporting those financial statement elements by providing guidance where none previously existed. The requirements of this statement were implemented as of June 30, 2013. The implementation of this statement affected the financial statement titles and required the University to reclassify certain previously reported amounts to deferred inflows of resources. In addition, net assets were renamed to be net position.

Note 2 – Cash, Cash Equivalents and Investments

Cash and cash equivalents include all readily available sources of cash such as petty cash, demand deposits, certificates of deposit and temporary investments in marketable debt securities with original maturities less than three months. At June 30, 2013, petty cash funds totaled \$30,000 and the carrying amount of the deposits was \$110,827,000 with a corresponding total bank balance of \$113,838,000. Of the bank balance, \$25,913,000 was covered by federal depository insurance, or collateralized with securities held by the pledging bank, or bank's agents, in the University's name and \$87,926,000 was held and invested by the Commonwealth of Kentucky. These deposits were covered by federal depository insurance or by collateral held by the Commonwealth in the Commonwealth's name.

Investments

The investments which the University may purchase are limited by the Commonwealth's law and the University's bond resolutions to the following (1) securities or obligations which are fully guaranteed by the U.S. Government or agencies of the U.S. Government as to principal and interest; (2) certificates of deposit or time deposits of banks, trust companies or national banking associations which are insured by the Federal Deposit Insurance Corporation; and (3) mutual funds investing solely in U.S. securities.

The following schedule reports the fair values of the University's investments at June 30, 2013 and 2012 (in thousands):

	2013	2012
Certificates of deposit	\$ 2,000	\$ 2,000
Restricted assets held by the Foundation	11,277	10,209
Total Investments	<u>\$ 13,277</u>	<u>\$ 12,209</u>

University investments held by the Northern Kentucky University Foundation, Inc. are comprised of Regional University Excellence Trust Fund endowments. Assets held by the Foundation are invested in an investment pool managed by the Foundation. University assets in the Foundation investment pool at June 30, 2013 and 2012 are invested as follows:

	2013	2012
Type of Investment:		
Fixed income funds	14%	18%
Equity funds and common stock	55%	51%
Hedge funds	12%	12%
Alternative investments	17%	15%
Other	2%	4%
Total Investments	<u>100%</u>	<u>100%</u>

Occasionally, the fair value of assets associated with endowments fall below the level that is required for the Foundation to retain as a fund of perpetual duration. Deficiencies of this nature are \$5,000 and \$19,000 as of June 30, 2013 and 2012 respectively.

See note 13 for further details of the Foundation's investment pool.

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. As stated in the University's investment policy, the bond resolution governs the investment of bond reserves. The bond resolution limits the investment maturities by the lesser of the remaining life of the bond issue or ten years. Certificates of deposit can have a maturity of not more than two years from the date of issue.

Credit Risk: Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The University's investment policy requires investments to be in compliance with state statute. University investments that are managed by the Foundation are governed by the Foundation's investment policy. This policy contains several provisions which are intended to limit credit risk, including a requirement that fixed income portfolios maintain a weighted average credit rating of at least AA (Standard and Poor's) and have no more than 10 percent of the portfolio in below investment grade bonds.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single user. The University debt service reserves are invested by the bond trustees in accordance with the governing bond resolutions. There are no specific limits on the maximum amount of investment securities held in bond debt service reserve funds that may be invested in one issuer. However, such investments are limited to bonds or interest bearing notes of the U.S. government.

Note 3 – Notes, Loans and Accounts Receivable

Notes, loans and accounts receivable as of June 30, 2013 and 2012 are as follows (in thousands):

2013			
	Gross Receivable	Allowance	Net Receivable
Student loans	\$ 1,382	\$ (596)	\$ 786
Student account receivables	10,399	(4,187)	6,212
Reimbursement receivable grants and contracts	1,531	-	1,531
Other	4,424	(907)	3,517
Total	<u>\$ 17,736</u>	<u>\$ (5,690)</u>	<u>\$ 12,046</u>
Current portion			10,386
Noncurrent portion			1,660
Total			<u>\$ 12,046</u>
2012			
	Gross Receivable	Allowance	Net Receivable
Student loans	\$ 1,751	\$ (556)	\$ 1,195
Student account receivables	9,095	(4,001)	5,094
Reimbursement receivable grants and contracts	1,545	-	1,545
Other	4,199	(837)	3,362
Total	<u>\$ 16,590</u>	<u>\$ (5,394)</u>	<u>\$ 11,196</u>
Current portion			9,094
Noncurrent portion			2,102
Total			<u>\$ 11,196</u>

Note 4 – Capital Assets, net

Capital assets for the years ended June 30, 2013 and 2012 are summarized as follows (in thousands):

	July 1, 2012	Additions	Reductions	June 30, 2013
Cost:				
Indefinite life intangible assets	\$ 4,622	\$ -	\$ -	\$ 4,622
Land	9,045	232	-	9,277
Land improvements	28,459	1,061	-	29,520
Buildings	385,387	7,580	487	392,480
Equipment	65,351	1,869	473	66,747
Library books	36,687	1,516	216	37,987
Construction in process	2,418	834	-	3,252
	<u>531,969</u>	<u>13,092</u>	<u>1,176</u>	<u>543,885</u>
Accumulated Depreciation:				
Land improvements	4,870	768	-	5,638
Buildings	134,591	12,633	408	146,816
Equipment	38,748	5,746	418	44,076
Library books	26,822	1,635	217	28,240
	<u>205,031</u>	<u>20,782</u>	<u>1,043</u>	<u>224,770</u>
Capital assets, net	<u>\$ 326,938</u>	<u>\$ (7,690)</u>	<u>\$ 133</u>	<u>\$ 319,115</u>

	<u>July 1, 2011</u>	<u>Additions</u>	<u>Reductions</u>	<u>June 30, 2012</u>
Cost:				
Indefinite life intangible assets	\$ 4,622	\$ -	\$ -	\$ 4,622
Land	8,919	126	-	9,045
Land Improvements	26,416	2,043	-	28,459
Buildings	381,877	3,901	391	385,387
Equipment	60,755	4,901	305	65,351
Library books	35,028	1,990	331	36,687
Construction in process	2,457	-	39	2,418
	<u>520,074</u>	<u>12,961</u>	<u>1,066</u>	<u>531,969</u>
Accumulated Depreciation:				
Land Improvements	4,114	756	-	4,870
Buildings	122,498	12,436	343	134,591
Equipment	33,044	5,974	270	38,748
Library books	25,552	1,601	331	26,822
	<u>185,208</u>	<u>20,767</u>	<u>944</u>	<u>205,031</u>
Capital assets, net	<u>\$ 334,866</u>	<u>\$ (7,806)</u>	<u>\$ 122</u>	<u>\$ 326,938</u>

As of June 30, 2013 and 2012, the net book value of land, buildings and equipment acquired through capital leases included in the above schedules totaled \$14,252,000 and \$12,423,000 respectively, including buildings of \$13,904,000 and \$12,240,000, respectively.

Note 5 – Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities as of June 30, 2013 and 2012 are as follows (in thousands):

	<u>2013</u>	<u>2012</u>
Payable to vendors and contractors	\$ 8,007	\$ 10,425
Accrued expenses, primarily payroll and vacation leave	6,307	6,391
Employee withholdings and deposits payable to third parties	2,996	2,659
	<u>\$ 17,310</u>	<u>\$ 19,475</u>

Note 6 – Unearned Revenue

Unearned revenue as of June 30, 2013 and 2012 are as follows (in thousands):

	<u>2013</u>	<u>2012</u>
Unearned summer school revenue	\$ 5,144	\$ 3,846
Unearned grants and contracts revenue	743	954
Unearned auxiliary revenue	828	900
Other	498	778
Total	<u>\$ 7,213</u>	<u>\$ 6,478</u>
Current	6,742	5,905
Noncurrent	471	573
Total	<u>\$ 7,213</u>	<u>\$ 6,478</u>

Note 7 – Long-term Liabilities

The changes in long-term liabilities for the years ended June 30, 2013 and 2012 are summarized as follows (in thousands):

	Balance July 1, 2012	Additions	Reductions	Balance June 30, 2013	Current Portion	Noncurrent Portion
Consolidated Educational Buildings Revenue						
Bonds (net of discounts)	\$ 7,028	\$ -	\$ 7,028	\$ -	\$ -	\$ -
Housing and Dining Revenue Bonds	1,635	-	160	1,475	165	1,310
General Receipts Bonds (net of discounts, premiums, and deferred losses on refunding)	83,155	5,069	2,501	85,723	3,973	81,750
Total bonds	91,818	5,069	9,689	87,198	4,138	83,060
Municipal lease obligations	7,010	445	1,500	5,955	1,553	4,402
Capital leases	500	-	500	-	-	-
Notes payable	127	200	64	263	42	221
Total notes and capital leases	7,637	645	2,064	6,218	1,595	4,623
Deferred compensation	542	-	20	522	84	438
Federal portion of loan programs	2,087	-	69	2,018	-	2,018
KERS-sick leave	675	3	8	670	67	603
Total other liabilities	3,304	3	97	3,210	151	3,059
Total long-term liabilities	<u>\$ 102,759</u>	<u>\$ 5,717</u>	<u>\$ 11,850</u>	<u>\$ 96,626</u>	<u>\$ 5,884</u>	<u>\$ 90,742</u>

	Balance July 1, 2011	Additions	Reductions	Balance June 30, 2012	Current Portion	Noncurrent Portion
Consolidated Educational Buildings Revenue						
Bonds (net of discounts)	\$ 9,568	\$ -	\$ 2,540	\$ 7,028	\$ 1,406	\$ 5,622
Housing and Dining Revenue Bonds	1,790	-	155	1,635	160	1,475
General Receipts Bonds (net of discounts, premiums, and deferred losses on refunding)	77,609	9,400	3,854	83,155	2,501	80,654
Total bonds	88,967	9,400	6,549	91,818	4,067	87,751
Municipal lease obligations	2,856	5,000	846	7,010	1,445	5,565
Capital leases	980	-	480	500	500	-
Notes payable	146	-	19	127	20	107
Total notes and capital leases	3,982	5,000	1,345	7,637	1,965	5,672
Deferred compensation	639	-	97	542	11	531
Federal portion of loan programs	2,172	-	85	2,087	-	2,087
KERS-sick leave	600	81	6	675	67	608
Total other liabilities	3,411	81	188	3,304	78	3,226
Total long-term liabilities	<u>\$ 96,360</u>	<u>\$ 14,481</u>	<u>\$ 8,082</u>	<u>\$ 102,759</u>	<u>\$ 6,110</u>	<u>\$ 96,649</u>

a. Bonds

The gross revenues of the Housing and Dining system operations are pledged for the retirement of the Housing and Dining System Revenue Bond. The \$210,000 reserve requirement for the Housing and Dining issue has been fully funded as of June 30, 2013. The \$348,000 required housing repair and replacement fund was fully funded as of June 30, 2013.

The outstanding obligation as of June 30, 2013 for the Northern Kentucky University General Receipts Bonds are reported net of discounts totaling \$911,000, premiums of \$371,000 and a \$1,167,000 deferred loss on bond refunding's. General Receipts Bonds are collateralized by the operating and nonoperating income of the University excluding income which as a condition of the receipt is not available for payment of debt service charges.

On February 26, 2013 Northern Kentucky University General Receipts Bonds were issued in the amount of \$4,995,000 at a net interest cost of 1.40 percent. The proceeds refunded the Consolidated Educational Buildings Revenue Bonds Series L maturities on or after May 1, 2014. The refunding reduced the University's total debt service payments over the term by \$980,000, representing an economic gain of \$832,000. Economic gain is determined by calculating the difference between the present value of the debt service payments on the old and new debt.

On August 4, 2011, Northern Kentucky University General Receipts Bonds were issued in the amount of \$9,290,000 at a net interest cost of 3.64 percent. The proceeds were used to (i) finance the acquisition of two radio licenses and equipment (ii) acquire property in accordance with the land acquisition plan approved by the Board of Regents.

The total bonds payable as of June 30 are as follows (in thousands):

	2013	2012
Consolidated Educational Building Revenue bonds payable		
Series B, dated November 1, 1973, with interest rates from 4.00% to 5.90%. Final principal payment date May 1, 2013.	\$ -	\$ 955
Series L, dated January 1, 2004, with interest rates from 3.25% to 4.25%. Refunded in 2013.	-	6,170
Total Consolidated Educational Building Revenue bonds payable	-	7,125
Housing and Dining System Revenue bonds payable		
Series B, dated November 1, 1980, with an interest rate of 3.00%. Final principal payment date November 1, 2021.	1,475	1,635
Total Housing and Dining System Revenue bonds payable	1,475	1,635
General Receipts bonds payable		
Series A 2007, dated May 23, 2007, with interest rates from 4.00% to 4.30%. Final principal payment date September 1, 2027.	39,825	41,735
Series A 2008, dated June 18, 2008, with interest rates from 3.00% to 4.38%. Final principal payment date September 1, 2028.	18,655	18,865
Series A 2010, dated June 29, 2010, with interest rates from 2.00% to 3.50%. Final principal payment date September 1, 2020.	2,990	3,375
Series B 2010, dated October 21, 2010, with interest rates from 2.00% to 3.75%. Final principal payment date September 1, 2027.	11,675	11,800
Series A 2011, dated August 4, 2011, with interest rates from 2.00% to 4.00%. Final principal payment date September 1, 2030.	9,290	9,290
Series A 2013, dated February 26, 2013, with an interest rate of 2.00%. Final principal payment date September 1, 2022.	4,995	-
Total General Receipts bonds payable	87,430	85,065
Less: Net discounts, premiums and losses on refundings	(1,707)	(2,007)
Total bonds payable	\$ 87,198	\$ 91,818

Principal maturities and interest on bonds and notes payable for the next five years and in subsequent five-year periods are as follows (in thousands):

Fiscal Year	Principal	Interest	Total
2014	\$ 4,302	\$ 3,249	\$ 7,551
2015	4,638	3,113	7,751
2016	4,770	2,971	7,741
2017	4,904	2,821	7,725
2018	5,075	2,660	7,735
2019-2023	28,894	10,311	39,205
2024-2028	32,455	4,395	36,850
2029-2033	4,130	169	4,299
Subtotal	89,168	29,689	118,857
Less: Net discounts and premiums	(540)	-	(540)
Loss on refundings	(1,167)	-	(1,167)
Total	\$ 87,461	\$ 29,689	\$ 117,150

b. Capital and Municipal Leases

On December 3, 2012, the University entered into a new municipal lease obligation through a local bank, in the amount of \$445,000, with an interest rate of 1.41percent. The proceeds from this obligation will be used to fund computer hardware equipment.

On June 26, 2012, the University entered into a new municipal lease obligation through a local bank, in the amount of \$5,000,000, with an interest rate of 1.58 percent. The proceeds from this obligation will be used to fund the Student Success Center renovation project.

Capital and municipal lease obligations as of June 30 are as follows (in thousands):

	<u>2013</u>	<u>2012</u>
Municipal leases payable		
Energy Management lease, dated October 22, 2004, with an interest rate of 3.76%. Final payment date September 22, 2016.	\$ 1,523	\$ 1,956
Equipment leases, dating from June 30, 2006 - October 1, 2009, with interest rates ranging from 1.46-4.65%. Final payment dates from June 30, 2014 to December 3, 2016.	401	20
Facility improvement leases, dating from June 30, 2006 - June 26, 2012, with interest rates ranging from 1.58-4.65%. Final payment dates from July 22, 2013 to June 26, 2017.	4,031	5,034
Total Municipal leases payable	<u>5,955</u>	<u>7,010</u>
Capital leases payable		
University Suites lease, dated August 1, 2002, with an interest rate of 4.00%. Final payment date December 1, 2012.	-	500
Total Capital leases payable	<u>-</u>	<u>500</u>
Total leases payable	<u><u>\$ 5,955</u></u>	<u><u>\$ 7,510</u></u>

Capital and municipal future minimum lease payments by year as of June 30 are as follows (in thousands):

<u>Fiscal Year</u>	<u>Present Value of Future Minimum Lease Payments</u>	<u>Interest Portion</u>	<u>Total</u>
2014	\$ 1,553	\$ 111	\$ 1,664
2015	1,577	77	1,654
2016	1,612	41	1,653
2017	1,213	10	1,223
Total	<u><u>\$ 5,955</u></u>	<u><u>\$ 239</u></u>	<u><u>\$ 6,194</u></u>

Note 8 – Pension Plans and Accrued Compensated Absences

Employees of the University are covered by one of two pension plans:

a. Defined Contribution Plan

A Teachers Insurance and Annuity Association - College Retirement Equities Fund (TIAA CREF) sponsored plan, adopted by the Board of Regents in July 1970, is available upon completion of ninety days of service, to all regular full-time members of the faculty, administrative officers and others who have educational related duties. The TIAA CREF retirement plan is a defined contribution, money purchase retirement plan. The employees contribute 5 percent of their base salary to the plan, and the University contributes 10 percent. All payments are vested immediately and the contracts with the providers are owned by the individual employees. The employee is entitled to various payment options upon retirement. Benefit payments at retirement depend on the total contributions with interest deposited into the employee's account. Retirement benefits can begin upon retirement or termination of employment with the University. Covered payroll totaled \$44,190,000 and \$43,790,000 for the years ended June 30, 2013 and 2012, respectively. Expenditures for the University's portion amounted to \$4,419,000 and \$4,379,000 for the years ended June 30, 2013 and 2012, respectively.

b. Defined Benefit Plan

Plan Description - All regular employees not participating in the above plan are required to participate in the Kentucky Employees Retirement System (KERS), a cost sharing - multiple employer public employee retirement system. KERS is a defined benefit plan providing for retirement, disability, death benefits and health insurance. Each employee covered by KERS is entitled to a monthly benefit based upon their months of service multiplied by the average of 5 full fiscal years of salary (highest 5 or last 5 based on date of participation) upon attainment of KERS specified age (or age and service combinations). Participants have a fully vested interest after the completion of 60 months of service, 12 of which are current service. KERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Retirement Systems, Perimeter Park West, 1260 Louisville Road, Frankfort, Kentucky, 40601-6124 or by calling (502) 696-8800.

Funding Policy - Benefit and contribution rates are established by state statute. For the fiscal year ended June 30, 2013, University employees were required to contribute 5 percent of their annual covered salary for retirement benefits and anyone with a participation date after 9/1/2008 are required to contribute an additional 1 percent of their covered salary for retiree healthcare benefits. The University was required to contribute 23.61 percent of covered payroll for non-hazardous pay and 29.79 percent for hazardous pay. The University's contributions to KERS for the years ending June 30, 2013, 2012 and 2011 were \$10,322,000, \$8,201,000, and \$6,608,000, respectively, equal to the required contributions for each year.

Effective July 1, 2010 KRS 61.546 states "the value of any accumulated sick leave that is added to the member's service credit in the Kentucky Employees Retirement System on or after July 1, 2010, shall be paid to the retirement system by the last participating Kentucky Employees Retirement System employer based upon a formula adapted by the Board." The KERS sick leave liability as of June 30, 2013 and 2012 was \$670,000 and \$675,000, respectively.

c. Deferred Compensation Plans

The University, through participation in the Commonwealth of Kentucky plan, offers its employees two deferred compensation plans created in accordance with Internal Revenue Code Sections 457 and 401(k). The plans, available to all Commonwealth employees, permit them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death or unforeseeable emergency.

All compensation deferred under Section 457, all property and rights purchased with that compensation and all income attributable to that compensation, property or rights belong solely to the Commonwealth and the University until paid to the employee or beneficiary, subject only to the claims of the Commonwealth's and University's general creditors. Participants' rights under the plan are equal to those of general creditors of the Commonwealth and the University in an amount equal to the fair market value of the deferred account for each participant. The market value of the University's share of the Section 457 plan assets, as of June 30, 2013 and 2012, was \$3,042,000 and \$2,850,000, respectively. All compensation deferred under Section 401(k) and resultant assets belong to the plan participants.

d. Compensated Absences

University employees begin to accumulate annual vacation allowance from the initial date of employment; however, no vacation is granted until three months of continuous employment have been completed. The maximum accumulation of vacation leave is limited to the number of days that can be accumulated in twelve months, based upon length of service and employment classification. Eligible employees are paid their accumulated vacation upon termination, subject to certain limitations. At June 30, 2013 and 2012, the University had recognized an accrued vacation liability of \$3,188,000 and \$3,144,000, respectively.

Note 9 – Operating Expenses By Natural Classification

The University's operating expenses by natural classification are as follows for the years ended June 30, 2013 and 2012 (in thousands):

	2013	2012
Salaries and wages	\$ 108,494	\$ 103,985
Employee benefits	36,318	32,571
Utilities	5,581	5,574
Supplies and other services	36,084	36,998
Depreciation	20,782	20,767
Student scholarships and financial aid	13,533	14,539
Total	<u>\$ 220,792</u>	<u>\$ 214,434</u>

Note 10 – Risk Management

The University is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by (1) the State Fire and Tornado Insurance Fund (the Fund), (2) Sovereign Immunity and the State Board of Claims, or (3) in the case of risks not covered by the Fund and Sovereign Immunity, commercial insurance, participation in insurance risk retention groups or self-insurance.

The Fund covers losses to property from fire, wind, earthquake, flood and most other causes of loss between \$500 and \$500,000 per occurrence. Losses in excess of \$500,000 are insured by commercial carriers up to \$500 million per occurrence with buildings insured at replacement cost and contents on an actual cash value basis. As a state agency, the University is vested with Sovereign Immunity and is subject to the provisions of the Board of Claims Act, under which the University's liability for certain negligence claims is limited to \$200,000 for any one person or \$350,000 for all persons damaged by a single act of negligence. Claims against educators' errors and omissions and wrongful acts are insured through a reciprocal risk retention group. There have been no significant reductions in insurance coverage from 2012 to 2013. Settlements have not exceeded insurance coverage during the past three years.

The University also self-insures certain employee benefits, including health insurance, worker's compensation and unemployment claims to the extent not covered by insurance. The University has recorded an estimate for asserted claims at June 30, 2013.

Note 11 – Contingencies and Commitments

The University is a party to various litigation and other claims in the ordinary course of business. University officials are of the opinion, based upon the advice of legal counsel, that the ultimate resolution of these matters will not have a material effect on the financial position of the University. The estimated cost to complete construction under contract at June 30, 2013 was approximately \$5,421,000.

Note 12 – Blended Entity Condensed Financial Information

Condensed financial information for Northern Kentucky University Research Foundation (NKURF) is provided below for the years ended June 30, 2013 and 2012 (in thousands):

NKURF Condensed Statement of Net Position

	2013	2012
ASSETS		
Current Assets	\$ 3,008	\$ 4,760
Noncurrent Assets	17,282	15,857
Due from the University	-	179
Total Assets	<u>20,290</u>	<u>20,796</u>
LIABILITIES		
Current Liabilities	971	1,316
Noncurrent Liabilities	17,282	17,857
Due to the University	460	-
Total Liabilities	<u>18,713</u>	<u>19,173</u>
NET POSITION		
Restricted expendable	81	60
Unrestricted	1,496	1,563
Total Net Position	<u>\$ 1,577</u>	<u>\$ 1,623</u>

NKURF Condensed Statements of Revenues, Expenses, and Changes in New Position

	2013	2012
OPERATING REVENUES		
Grants and contracts	\$ 5,836	\$ 4,661
Recoveries of facilities and administrative costs	414	1,041
Other operating revenues	8	97
Total operating revenues	<u>6,258</u>	<u>5,799</u>
OPERATING EXPENSES		
Operating expenses	<u>5,984</u>	<u>5,638</u>
Operating income (loss)	<u>274</u>	<u>161</u>
NONOPERATING REVENUES (EXPENSES)		
Non-capital transfers (to)/from the University	(385)	(306)
Gifts and grants	61	57
Net nonoperating revenues (expenses)	<u>(324)</u>	<u>(249)</u>
Income (loss) before other revenues, expenses, gains or losses	<u>(50)</u>	<u>(88)</u>
Capital transfers (to)/from the University	-	(1,379)
Capital grants and gifts	4	2,203
Total other revenues	<u>4</u>	<u>824</u>
Increase (decrease) in net position	<u>(46)</u>	<u>736</u>
NET POSITION		
Net position-beginning of year	1,623	887
Net position-end of year	<u>\$ 1,577</u>	<u>\$ 1,623</u>

NKURF Condensed Statement of Cash Flows

	2013	2012
Net cash provided (used) by operating activities	\$ (603)	\$ 839
Net cash provided (used) by noncapital financing activities	(277)	12,136
Net cash provided by (used in) capital and related financing activities	324	534
Net cash provided by (used in) investing activities	-	500
Net increase (decrease) in cash and cash equivalents	(556)	14,009
Cash and cash equivalents-beginning of year	17,495	3,486
Cash and cash equivalents-end of year	<u>\$ 16,939</u>	<u>\$ 17,495</u>

Note 13 – Northern Kentucky University Foundation, Inc. Notes to Financial Statements

a. Summary of Significant Accounting Policies

1. Scope of Statements

The consolidated financial statements of the Northern Kentucky Foundation, Inc. include the operations of the Foundation and several single member limited liability companies. NKU Foundation Properties Inc, included in the statements for 2012 was dissolved effective December 31, 2011 and its net assets were transferred to NKUF Properties 6, LLC. All material intercompany transactions and balances have been eliminated for the years ended June 30, 2013 and 2012.

2. Basis of Presentation

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) which require management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates. The following is a summary of the significant accounting policies consistently followed by the Foundation in preparation of its financial statements.

These statements are presented on the accrual basis of accounting, and have been prepared to focus on the Foundation as a whole and to present transactions according to the existence or absence of donor-imposed restrictions. This has been accomplished by classification of fund balances and transactions into three classes of net position - permanently restricted, temporarily restricted and unrestricted net assets.

Net assets and changes therein are classified as follows:

- ***Permanently restricted net assets*** - Net assets subject to donor-imposed stipulations that they be maintained permanently by the Foundation. Generally, the donors of these assets permit the Foundation to use the returns on the related investments over time for general or specific purposes.
- ***Temporarily restricted net assets*** - Net assets subject to donor-imposed stipulations that may or will be met by actions of the Foundation and/or the passage of time. Temporarily restricted net assets are generally established in support of colleges or departments of the University, often for specific purposes such as faculty support, scholarships and fellowships, library acquisitions, equipment or building projects and other specific purposes.
- ***Unrestricted net assets*** - Net assets not subject to donor-imposed stipulations.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as reclassifications between the applicable classes of net assets.

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions receivable are discounted at an appropriate rate commensurate with the risks involved. Amortization of discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions on the contributions. An allowance for uncollectible contributions receivable is provided based upon management's judgment of such factors as prior collection history, type of contribution and nature of the fund-raising activity.

Income and realized net gains on long-term investments are reported as follows:

- As increases in permanently restricted net assets – if the terms of the gift require that they be added to the principal of a permanent endowment fund.

- As increases in temporarily restricted net assets – if the terms of the gift impose restrictions on the use of the income.
- As increases in unrestricted net assets – in all other cases.

3. Cash and Cash Equivalents

Cash and cash equivalents includes all readily available sources of cash such as petty cash, demand deposits and temporary investments in marketable securities with maturities of less than three months. Cash and cash equivalents representing investments purchased with endowment net assets are reported as investments.

At various times throughout the year, the Foundation has cash in certain financial institutions in excess of insured limits. Included in the Foundation's deposits at June 30, 2013 and 2012, are short term government obligation shares of \$323,000. Additionally, at June 30, 2013 and 2012, \$2,546,000 and \$3,224,000, respectively, was collateralized with securities held by the financial institution's trust department or agent, but not in the Foundation's name. At June 30, 2013 and 2012, balances of \$2,095,000 and \$3,069,000, respectively, were neither insured nor collateralized.

4. Loans and Accounts Receivable

Loans receivable consists primarily of loans made to students under privately funded loan programs. The advances are evidenced by signed promissory notes, bearing interest at varying stated interest rates, with varying due dates. Loans, accounts and other receivables are stated at the amount management expects to collect from outstanding balances. Management provides for a probable uncollectible allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. The allowance for doubtful accounts at June 30, 2013 and 2012 was \$116,000 and \$115,000, respectively.

5. Investments

Investments in equity securities with readily determinable fair value and all debt securities are reported at their fair value. The estimated fair value of investments is based on quoted market prices, except for investments for which quoted market prices are not available. The alternative investments, which are not readily marketable, are carried at estimated fair values as provided by the investment managers. The estimated fair value of certain alternative investments, such as private equity interests, is based on valuations provided by the external investment managers adjusted for cash receipts, cash disbursements and distributions. The Foundation believes the carrying amount of these financial instruments is a reasonable estimate of fair value. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investments existed. Such difference could be material.

The Foundation invests its endowment investment portfolio and allocates the related earnings for expenditure in accordance with the total return concept. A distribution of endowment return that is independent of the cash yield and appreciation (depreciation) of investments earned during the year is provided for program support.

The Foundation has significant exposure to a number of risks including interest rate, market and credit risks for both marketable and non-marketable securities. Due to the level of risk exposure, it is possible that near-term valuation changes for investment securities may occur to an extent that could materially affect the amounts reported in the Foundation's financial statements.

All true endowment investments and long-term net assets functioning as endowment are managed in a pool, unless special considerations or donor stipulations require that they be held separately.

6. Land and Land Improvements

At June 30, 2013 and 2012, land and land improvements consisted of:

	<u>2013</u>	<u>2012</u>
Type of Asset:		
Land	\$ 340	\$ 340
Land improvements	208	208
Total Fixed Assets	<u>\$ 548</u>	<u>\$ 548</u>

Assets acquired for Foundation use with a useful life greater than one year and a value of \$5,000 or more are capitalized. Annual depreciation for land improvements is calculated on a straight-line basis, beginning in the month of acquisition based on a useful life of 30 years. Depreciation expense for the years ended June 30, 2013 and 2012 was approximately \$5,000 and \$7,000, respectively, and is reported as support expenses under rental property in the statement of activities.

Assets purchased or constructed through the Foundation for use by Northern Kentucky University are recorded by the Foundation as a program expense.

7. Net assets Released from Restrictions

Reclassification of net assets is based upon the satisfaction of the purpose for which the net assets were restricted or the completion of a time stipulation. Restricted contributions and net investment returns earned are reported as temporarily restricted support and reclassified as unrestricted when any donor-imposed restrictions are satisfied.

b. Notes Payable

The Foundation borrowed \$4.425 million on a promissory note collateralized by certain pledges receivable restricted by the donor to partially fund construction of The Bank of Kentucky Center, a multi-purpose athletic and special event facility, with equal annual payments of \$857,000 including principal and interest at a rate of 4.31 percent due from August 1, 2009 through August 1, 2014. Loan principal (in thousands) to be paid over the term of the loan are as follows:

<u>Year Ended</u>	<u>Principal</u>
June 30, 2014	\$ 787
June 30, 2015	822
	<u>\$ 1,609</u>

Costs of \$33,700 associated with obtaining the loan are being amortized over the 73-month term of the note. Amortization expense for the years ended June 30, 2013 and 2012 was \$5,540 and is reported as management and general expense in the financial statements.

c. Unconditional and Conditional Promises to Give

Unconditional promises to give that are expected to be collected in future years are recorded at the present value of estimated future cash flows. The discounts are computed using a risk free interest rate as of fiscal year-end. Amortization of the discount is included in contribution revenue.

At June 30, 2013 and 2012, the Foundation recognized contributions based on the following unconditional promises to give (in thousands):

	<u>2013</u>	<u>2012</u>
Purpose:		
Endowment giving	\$ 236	\$ 327
Capital purposes	2,072	3,139
Operating programs	2,583	1,394
Gross unconditional promises	<u>4,891</u>	<u>4,860</u>
Less: Discount and allowance for uncollectable accounts	(249)	(371)
Net unconditional promises to give	<u>\$ 4,642</u>	<u>\$ 4,489</u>
 Amounts due in:		
Less than one year	\$ 2,584	\$ 2,052
One to five years	1,904	2,805
More than five years	403	3
Total	<u>\$ 4,891</u>	<u>\$ 4,860</u>

The discount rates used to calculate the present value of contributions receivable at June 30, 2013 and 2012 vary from 1.2 percent to 5.6 percent depending on when the promise was made.

The Foundation has pledged \$1.714 million of unconditional promises to give as collateral against a promissory note.

Conditional promises to give are not included as support until such time as the conditions are substantially met. At June 30, 2013 and 2012, the Foundation had received conditional promises to give of approximately \$1.2 million, consisting of the face value of life insurance policies, net of accumulated cash surrender value.

d. Fair Value Measurements

The three levels of the fair value hierarchy under generally accepted accounting principles are described as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities

Level 2 – Observable inputs other than Level 1 prices, such as:

- Quoted prices for similar assets or liabilities;
- Quoted prices for identical or similar assets or liabilities in inactive markets;

- Other inputs that are observable for the asset or liability;
- Other inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value:

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 investments include short term money market funds, cash and cash surrender value, certificates of deposit, fixed income funds and equity funds.

Level 2 investments are based on quoted prices of securities or other property with similar characteristics and include hedge funds of funds and a remainder interest in real property subject to a life estate.

In certain cases where level 1 or 2 inputs are not available, investments are classified within Level 3 of the hierarchy and include investments in private equity, natural resources and private real estate.

There have been no changes in the methodologies used at June 30, 2013.

The following assets were measured at fair value as of June 30, 2013 and 2012 (in thousands):

	<u>2013</u>	<u>2012</u>
Level 1		
Investments	\$ 59,742	\$ 52,648
Level 2		
Investments	\$ 10,234	\$ 9,522
Level 3		
Investments	\$ 14,029	\$ 11,393

The table below presents information about the changes in the fair value of assets based on significant unobservable inputs (Level 3):

	<u>Private Equity</u>	<u>Natural Resources</u>	<u>Private Real Estate</u>
Investments:			
Beginning balance, June 30, 2011	\$ 4,082	\$ 2,781	\$ 1,608
Additional investment	1,609	1,289	442
Capital distributions	(691)	(196)	(234)
Fees	(40)	(44)	(7)
Realized gains (losses)	34	37	(12)
Unrealized gains (losses)	272	351	112
Balance, June 30, 2012	5,266	4,218	1,909
Additional investment	1,397	1,719	348
Capital distributions	(1,100)	(649)	(93)
Fees	-	(35)	(19)
Realized gains (losses)	272	257	97
Unrealized gains	251	104	87
Ending balance, June 30, 2013	<u>\$ 6,086</u>	<u>\$ 5,614</u>	<u>\$ 2,329</u>

e. Investments

The market values (in thousands) of the Foundation's investments as of June 30, 2013 and 2012 are categorized by type below:

	2013	2012
Type of Investment:		
Short-term money market funds	\$ 2	\$ 3
Cash and cash surrender value	427	441
Certificates of deposit	700	1,950
Fixed income funds:		
Core plus	7,004	10,106
Global	2,978	2,758
High yield	1,991	-
Equity funds:		
Large/Mid Cap - broad	14,966	11,483
Large/Mid Cap - growth	3,919	6,742
Large/Mid Cap - value	7,975	6,084
Small Cap - growth	1,903	1,476
Small Cap - value	2,054	1,550
International - core	6,909	5,983
International small cap - value	1,845	316
Emerging markets - value	3,834	3,756
Emerging markets - small cap	3,235	-
Quoted prices in active market for identical assets (level 1)	59,742	52,648
Hedge funds:		
Directional	4,861	4,533
Directional fund of funds	5,049	4,600
Remainder interest in real property and other	324	389
Significant other observable inputs (level 2)	10,234	9,522
Private equity:		
Buyout	1,992	1,992
Distressed	769	926
Diversified	1,346	1,149
Mezzanine	778	562
Venture capital	619	637
Secondary	582	-
Natural resources:		
Diversified	3,255	1,929
Energy	2,359	2,289
Private real estate:		
Secondary	633	611
Value added	1,696	1,298
Significant unobservable inputs (level 3)	14,029	11,393
Total investments	\$ 84,005	\$ 73,563

Investment income and gains (in thousands) for the years ended June 30, 2013 and 2012 consist of:

	<u>2013</u>	<u>2012</u>
Interest	\$ 24	\$ 33
Dividends	1,678	1,205
Fees	(143)	(139)
Total Investment Income	<u>\$ 1,559</u>	<u>\$ 1,099</u>
Realized gains (losses)	2,968	274
Unrealized gains (losses)	4,037	(1,560)
Total Investment Income	<u>\$ 7,005</u>	<u>\$ (1,286)</u>

The Foundation records the cost of managing its endowment portfolio as a decrease in investment income within the appropriate net asset class in the Statement of Activities. Some of the Foundation's investment managers report investment transactions net of fees. The fees noted above are only those fees separately stated by the managers.

The investments of the Foundation are commingled with certain investments which the Foundation holds in trust for Northern Kentucky University. The market value of funds held in trust for the University at June 30, 2013 and 2012 were \$11,277,000 and \$10,209,000 respectively. See note 13h for further explanation of the trust funds.

At June 30, 2013 and 2012, the Foundation had committed \$24.4 and \$22.4 million, respectively, of its endowment investment resources to alternative investments, of which \$8.6 and \$10.0 million, respectively, had not yet been called by the investment managers. Alternative investments for which commitments have been made consist of private equity, natural resources and private real estate.

Alternative investments of the Foundation have limited marketability and the related investment agreements generally contain restrictive redemption provisions to the extent that the underlying investments should be considered illiquid for the duration of the investment through normal maturity. Early redemption of such investments would likely result in recovery of significantly less than the original investment amount. Foundation management believes the investment portfolio contains sufficient liquidity among other asset classes to make early redemption of alternative investments unlikely for reasons of meeting current spending needs.

f. Endowments

The Foundation's endowment consists of approximately 252 individual funds established for a variety of purposes. Its endowment includes both donor-restricted funds and funds designated by the Board of Directors to function as endowments (quasi-endowments). Net assets associated with endowment funds, including quasi-endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. The board, at their discretion, can at any time permit spending from the principal of any quasi-endowed fund, provided the expenditure complies with any donor-imposed restrictions related to the fund.

Kentucky enacted the Kentucky Uniform Prudent Management of Institutional Funds Act (KUPMIFA), the provisions of which apply to endowment funds existing on or established after enactment, with an effective date of July 15, 2010.

An interpretation of KUPMIFA provisions by the Foundation Board of Directors requires that the historical dollar amount of a donor-restricted endowment fund be preserved. As a result of this requirement, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment. In the absence of donor restrictions, the net appreciation on a donor-restricted endowment fund is spendable. The net appreciation of donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation.

Under KUPMIFA, Foundation endowment spending policy allows for prudent spending of future endowment earnings for accounts without accumulated earnings based upon consideration of the following factors, if applicable:

- Duration and preservation of the endowment fund
- Purpose of the institution and the endowment fund
- General economic conditions
- Possible effect of inflation or deflation
- Expected total return on investments
- Other resources of the institution
- Investment policy

The approved annual endowment spending rate is reduced by a proportion of 5 percent for each 1 percent the affected endowment is below the value of original and subsequent gifts to the permanent endowment (i.e. principal).

Return Objectives and Risk Parameters. The Foundation has adopted investment and spending policies, approved by the Board of Directors, for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of these endowment assets over the long-term. The Foundation's spending and investment policies work together to achieve this objective. The investment policy establishes an achievable return objective through diversification of asset classes. The current long-term return objective is to return a rate equal to the Consumer Price Index plus 5 percent, net of investment fees. Actual returns in any given year may vary from this amount.

Strategies Employed for Achieving Objectives. To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that includes fixed income investments as well as publicly traded equity-based investments and various alternative investment strategies to achieve its long-term return objectives within prudent risk parameters.

Spending Policy and How the Objectives Relate to Spending Policy. The spending policy calculates the amount of money annually distributed from the Foundation's various endowed funds, for grant making and administration. The current spending policy is to distribute an amount at least equal to 3-5 percent of a moving sixteen quarter average of the fair value of the endowment funds. Accordingly, over the long term, the Foundation expects its current spending policy to allow its endowment assets to grow at an average rate of 3 percent annually. This is consistent with the Foundation's objective to maintain the historical dollar amount of endowment assets as well as to provide additional real growth through investment return.

Endowment net asset composition by type of endowment (in thousands) as of June 30, 2013 is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Donor restricted endowment funds	\$ -	\$ 22,829	\$ 40,595	\$ 63,424
Quasi-endowment funds	1,939	6,082	-	8,021
Total endowment funds	<u>\$ 1,939</u>	<u>\$ 28,911</u>	<u>\$ 40,595</u>	<u>\$ 71,445</u>

Changes in endowment net assets (in thousands) as of June 30, 2013 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Endowment net assets, beginning of year	\$ 1,755	\$ 22,139	\$ 40,167	\$ 64,061
Contributions collected	-	22	416	438
Investment income	34	1,501	-	1,535
Net investment gain	153	6,822	-	6,975
Amounts appropriated for expenditure	(11)	(1,565)	-	(1,576)
Investment loss recovery transferred to unrestricted	8	(8)	-	-
Transfer to permanently restricted	-	-	12	12
Endowment net assets, end of year	<u>\$ 1,939</u>	<u>\$ 28,911</u>	<u>\$ 40,595</u>	<u>\$ 71,445</u>

Endowment net asset composition by type of endowment (in thousands) as of June 30, 2012 is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Donor restricted endowment funds	\$ -	\$ 16,119	\$ 40,167	\$ 56,286
Quasi-endowment funds	1,755	6,020	-	7,775
Total endowment funds	<u>\$ 1,755</u>	<u>\$ 22,139</u>	<u>\$ 40,167</u>	<u>\$ 64,061</u>

Changes in endowment net assets (in thousands) as of June 30, 2012 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Endowment net assets, beginning of year	\$ 1,775	\$ 23,786	\$ 33,771	\$ 59,332
Contributions collected	-	9	6,297	6,306
Investment income	24	1,040	-	1,064
Net investment loss	(30)	(1,249)	-	(1,279)
Amounts appropriated for expenditure	(6)	(1,356)	-	(1,362)
Investment loss transferred to unrestricted	(8)	8	-	-
Transfer to permanently restricted	-	(99)	99	-
Endowment net assets, end of year	<u>\$ 1,755</u>	<u>\$ 22,139</u>	<u>\$ 40,167</u>	<u>\$ 64,061</u>

Funds with Deficiencies. From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or KUPMIFA requires the Foundation to retain as a fund of perpetual duration. There were no such deficiencies at June 30, 2013. Deficiencies of this nature that are reported in unrestricted net assets were \$8,000 of June 30, 2012. These deficiencies resulted from unfavorable market conditions that occurred after the investment of permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Board of Directors.

g. Contingent Liabilities

Legal counsel for the Foundation have advised that they know of no pending or threatened litigation, claims or assessments involving the Foundation that could have a material adverse financial effect on the Foundation.

h. Regional University Excellence Trust Fund

The Foundation holds certain funds, consisting of endowment matching funds received by Northern Kentucky University from the Commonwealth of Kentucky's Regional University Excellence Trust Fund, which were subsequently transferred to the Foundation for management and investment. The Foundation reports these funds and accumulated earnings as assets held in trust for Northern Kentucky University. Investment earnings, gains and losses and expenditures from these funds are reported as changes in the balance held in trust rather than as revenue and expenses of the Foundation.

i. Subsequent Events

The date to which events occurring after June 30, 2013 have been evaluated for possible adjustment to the financial statements or disclosure is September 10, 2013, which is the date the financial statements were available to be issued.

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