

KENTUCKY STATE UNIVERSITY
(A Component Unit of the Commonwealth of Kentucky)

FINANCIAL STATEMENTS

June 30, 2018

KENTUCKY STATE UNIVERSITY

FINANCIAL STATEMENTS

June 30, 2018

CONTENTS

INDEPENDENT AUDITOR'S REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	3
FINANCIAL STATEMENTS	
KENTUCKY STATE UNIVERSITY STATEMENT OF NET POSITION	15
KENTUCKY STATE UNIVERSITY FOUNDATION, INC. STATEMENT OF FINANCIAL POSITION	16
KENTUCKY STATE UNIVERSITY STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION	17
KENTUCKY STATE UNIVERSITY FOUNDATION, INC. STATEMENT OF ACTIVITIES.....	18
KENTUCKY STATE UNIVERSITY STATEMENT OF CASH FLOWS	19
KENTUCKY STATE UNIVERSITY NOTES TO THE FINANCIAL STATEMENTS	21
REQUIRED SUPPLEMENTARY INFORMATION	
SCHEDULE OF THE UNIVERSITY'S (KSU) PROPORTIONATE SHARE OF THE NET PENSION LIABILITY AND SCHEDULE OF UNIVERSITY'S CONTRIBUTIONS KENTUCKY EMPLOYEES' RETIREMENT SYSTEM	60
KENTUCKY TEACHERS' RETIREMENT SYSTEM.....	62
SCHEDULE OF THE UNIVERSITY'S (KSU) PROPORTIONATE SHARE OF THE NET OPEB LIABILITY AND SCHEDULE OF UNIVERSITY'S CONTRIBUTIONS KENTUCKY EMPLOYEES' RETIREMENT SYSTEM	64
KENTUCKY TEACHERS' RETIREMENT SYSTEM.....	66
INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	67
SCHEDULE OF FINDINGS AND RESPONSES.....	69

INDEPENDENT AUDITOR'S REPORT

Members of the Board of Regents
Kentucky State University
Frankfort, Kentucky

Secretary of Finance and
Administration Cabinet of the
Commonwealth of Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities and discretely presented component unit of Kentucky State University (the University), a component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2018, and the related notes to the financial statements which collectively comprise the University's basic financial statements as listed on the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Kentucky State University Foundation, Inc. (Foundation) which represent the entire discretely presented component unit of the University. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Foundation is based solely on the reports of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audit contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

The financial statements of the Foundation were not audited in accordance with *Government Auditing Standards*.

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

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

(Continued)

Opinions

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and discretely presented component unit of the University as of June 30, 2018, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1 to the financial statements, during the year ended June 30, 2018, the University adopted new accounting guidance, GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits other than Pensions*, which resulted in a restatement of the University's beginning net position as of July 1, 2017 of \$10,377,399. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 14 and required supplementary information on pages 60 through 66 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2018 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.



Crowe LLP

Lexington, Kentucky
October 31, 2018

Introduction

Management's Discussion and Analysis of Kentucky State University's (the University) financial statements provide an overview of the financial position and activities of the University for the year ended June 30, 2018, with comparative information for the year ended June 30, 2017. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section. The financial statements and related notes and this discussion and analysis are the responsibility of management.

Kentucky State University is a Commonwealth of Kentucky coeducational institution for higher education. The University's mission is to build on its legacy of achievement as a historically black, liberal arts, and 1890 land-grant university, afford access to and prepare a diverse student population of traditional and non-traditional students to compete in a multifaceted, ever-changing global society by providing student-centered learning while integrating teaching, research, and service through high-quality undergraduate and select graduate programs. Kentucky State University is committed to keeping relevant its legacy of service by proactively engaging the community in partnerships on civic projects driven by the objective of positively impacting the quality of life of the citizens of the Commonwealth.

Basis of Presentation

The annual financial report and statements include the University and Kentucky State University Foundation, a component unit of the University. Kentucky State University Foundation, Inc. (the Foundation) is a not-for-profit Kentucky corporation which was established to receive, invest and expend funds to promote and implement educational and developmental activities at Kentucky State University (the University). The Foundation is managed by a Board of Trustees independent from that of the University. The Foundation is supported primarily through contributions from alumni.

Financial Highlights

The University's financial position at June 30, 2018, reflected total assets and deferred outflows of \$128.5 million and total liabilities and deferred inflows of \$127.4 million. Total net position was \$1.1 million.

Total assets and deferred outflows decreased by \$8.2 million or 6.0%, and primarily due to a decrease in cash and deferred outflows of resources related to pension funding. Total liabilities and deferred inflows decreased by \$10.9 million or 7.9% primarily due decreases in the net pension liability.

Unrestricted net position, which the University reserves for spending in programs and other capital-related contingencies, increased \$1.3 million. This increase was primarily due to changes in the net pension liability.

The University classifies amounts earned on endowments as spendable or non-spendable in accordance with the endowment's donor stipulations. Nonexpendable restricted net assets represent amounts, which must be maintained in perpetuity. Expendable restricted net assets include private grants and contributions restricted for specific purposes and accumulated earnings on endowment assets.

Operating revenues were \$34.4 million and operating expenditures were \$68.0 million, resulting in a loss from operations of \$33.6 million. Net non-operating revenues were \$32.8 million, including \$26.5 million in state appropriations, which, when combined with the loss from operations and capital appropriations, resulted in an overall increase in net position of \$2.7 million.

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

Using the Financial Statements

The University's Financial Statements consist of three financial statements: a Statement of Net Position (Balance Sheet); a Statement of Revenues, Expenses and Changes in Net Position (Income Statement); and a Statement of Cash Flows, along with the accompanying Notes to the Financial Statements. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 35, Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities.

Kentucky State University is a component unit of the Commonwealth of Kentucky.

Statement of Net Position

The Statement of Net Position presents the financial position of the University at the end of the fiscal year and includes all assets, deferred outflows of resources, liabilities, and deferred inflows of resources. Net position, the difference between total assets and deferred outflows and total liabilities and deferred inflows, is an important indicator of the current financial condition, while the change in net position is an indicator of whether the overall financial position has improved or worsened during the year.

Condensed Statement of Net Position

	<u>2018</u>	<u>2017</u> (as restated)
ASSETS		
Current assets	\$ 19,076,951	\$ 22,883,930
Noncurrent assets	<u>94,887,552</u>	<u>94,780,968</u>
Total assets	<u>113,964,503</u>	<u>117,664,898</u>
DEFERRED OUTFLOWS OF RESOURCES	14,488,964	18,972,787
LIABILITIES		
Current liabilities	7,107,307	7,470,378
Non-current liabilities	<u>89,475,083</u>	<u>114,065,254</u>
Total liabilities	<u>96,582,390</u>	<u>121,535,632</u>
DEFERRED INFLOWS OF RESOURCES	30,793,555	16,778,028
NET POSITION		
Invested in capital assets, net of related debt	72,660,076	72,727,684
Restricted		
Nonexpendable	3,562,238	3,562,238
Expendable	5,388,621	3,846,394
Unrestricted	<u>(80,533,413)</u>	<u>(81,812,291)</u>
Total net position	<u>\$ 1,077,522</u>	<u>\$ (1,675,975)</u>

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

Assets and Deferred Outflows: As of June 30, 2018, total assets and deferred outflows amounted to \$128.5 million. Of this amount, investment in capital assets (net of depreciation) of \$76.9 million, or 59.8% of total assets, represented the largest asset class. Investments amounted to \$17.7 million or 13.8% of total assets. During the year, total assets and deferred outflows decreased by \$8.2 million, primarily due to decreases in cash and deferred outflows of resources related to pension funding.

Liabilities and Deferred Inflows: As of June 30, 2018, total liabilities and deferred inflows amounted to \$127.4 million. Net pension and OPEB liabilities amounted to \$85.5 million. The University's proportion of the net pension liability and net OPEB liability of the Kentucky Employees Retirement System and the Kentucky Teachers' Retirement System was based on a projection of the University's long-term share of contributions to the pension and OPEB plans relative to the projected contributions of all participating universities, actuarially determined. Long-term debt includes bonds payable for the housing and dining system and energy-related equipment and technology equipment purchased under a Master Lease Agreement. During the year, total liabilities and deferred inflows decreased by \$10.9 million, primarily due to the decrease in the net pension liability related to KTRS offset with adoption of new accounting guidance requiring the recording of the net OPEB liabilities related to KTRS and KERS.

Net Position: Net position of the University was \$1.1 million at June 30, 2018 and was reported in three net position categories: invested in capital assets, net of related debt \$72.7 million, restricted nonexpendable \$3.6 million, expendable \$5.3 million, and unrestricted \$(80.5) million.

Statement of Revenues, Expenses and Changes in Net Position

The Statement of Revenues, Expenses and Changes in Net Position is prepared on 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. All items that increase or decrease net position must appear on the Statement of Revenues, Expenses and Changes in Net Position as revenues, expenses, gains or losses.

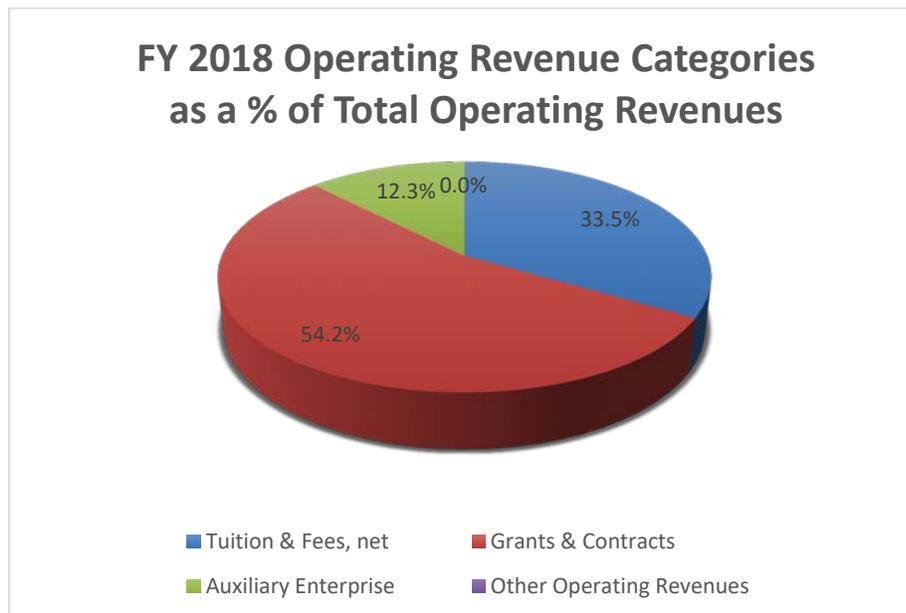
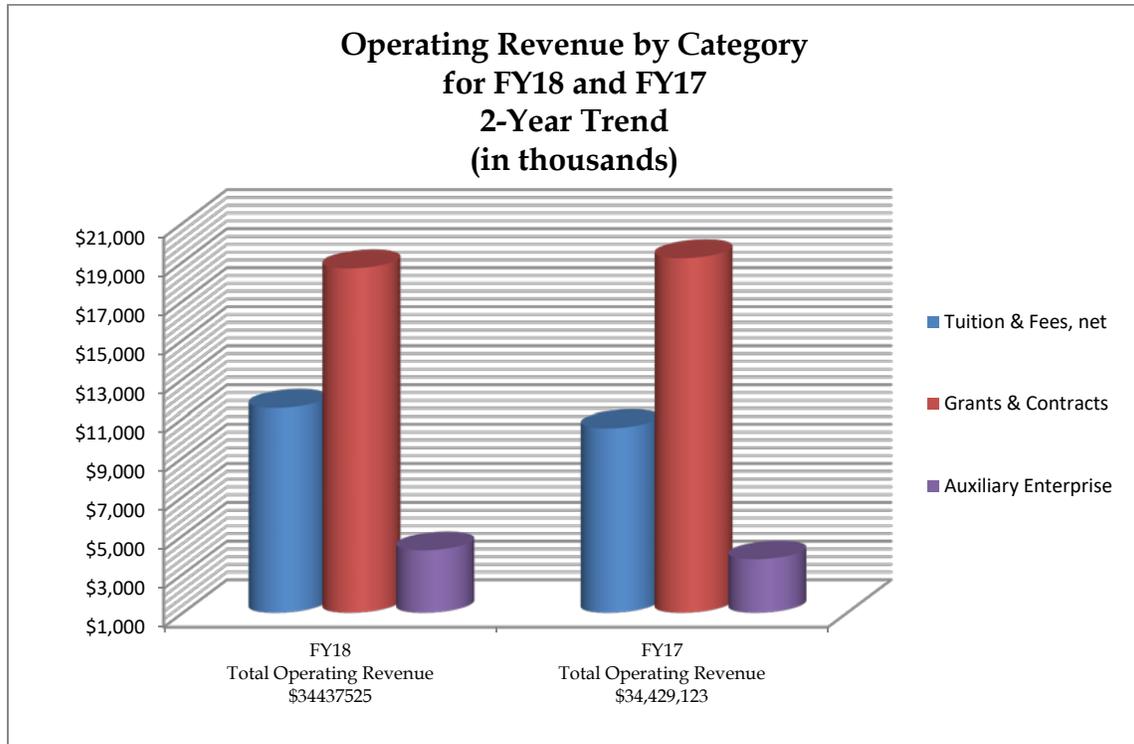
Financial activities are reported as either operating or non-operating. GASB Statement No. 35 requires state appropriations, gifts, investment income and endowment income to be classified as non-operating revenues. Accordingly, the University reports an operating loss prior to the addition of non-operating revenues. The utilization of long-lived capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life. Tuition revenue is reduced by gift scholarships and institutional aid, and is reported net of scholarship allowances in the financial statements. A summarized comparison of the University's revenues, expenses and changes in net position for the years ended June 30, 2018 and 2017 is as follows.

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

Condensed Statement of Revenues, Expenses and Changes in Net Position

	<u>2018</u>	<u>2017</u>
REVENUES		
Student tuition and fees, net	\$ 11,525,935	\$ 10,497,944
Grants and contracts	18,672,021	19,192,283
Auxiliary enterprises	4,239,569	3,774,500
Other operating revenue	-	964,396
Total operating revenues	<u>34,437,525</u>	<u>34,429,123</u>
EXPENSES		
Educational and general	62,301,199	64,882,362
Auxiliary enterprises	<u>5,694,800</u>	<u>5,712,000</u>
Total operating expenses	<u>67,995,999</u>	<u>70,594,362</u>
Operating loss	<u>(33,558,474)</u>	<u>(36,165,239)</u>
NONOPERATING REVENUES (EXPENSES)		
State appropriations	26,462,300	26,729,600
Federal grants and contracts	4,391,839	3,776,772
Investment income	1,174,232	1,407,599
Interest on capital asset – related debt	(236,690)	(226,835)
Other	<u>971,372</u>	<u>(88,964)</u>
Total non-operating revenues	<u>32,763,053</u>	<u>31,598,172</u>
Loss before capital appropriations	(795,421)	(4,567,067)
Capital appropriations	<u>3,548,918</u>	<u>4,906,223</u>
Change in net position	2,753,497	339,156
NET POSITION		
Net position, beginning of year, as restated in 2018	(1,675,975)	8,362,208
Cumulative effect of GASB 75 implementation	<u>-</u>	<u>(10,377,339)</u>
Net position, end of year, as restated in 2017	<u>\$ 1,077,522</u>	<u>\$ (1,675,975)</u>

Figure 1



Operating Revenue

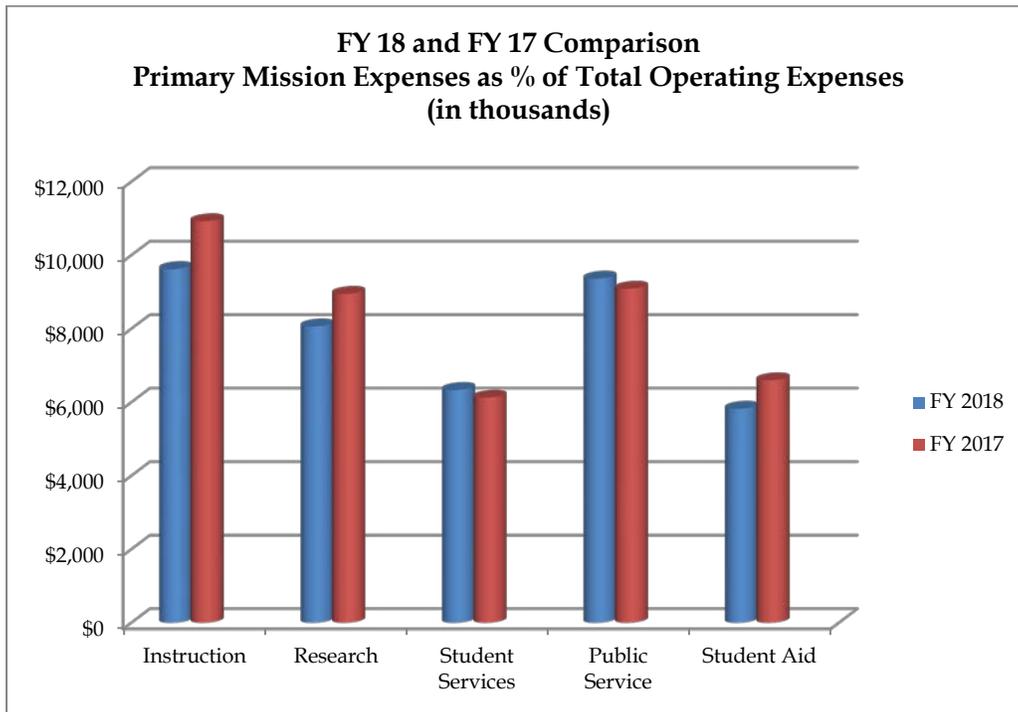
Total operating revenues were \$34.4 million for the year ended June 30, 2018, which was consistent with FY17. The primary components of operating revenue were federal, state and local grants and contracts of \$18.7 million (54.2%), student tuition and fees, net, of \$11.5 million (33.5%) and auxiliary services and other revenues of \$4.2 million (12.3%). FY18 net student tuition and fees revenue increased \$1.0 million compared to FY17. FY18 grants and contracts revenue decreased \$0.5 million compared to FY17 due to decreased awards and spending. FY18 auxiliary services and other revenue increased \$0.5 million compared to FY17. Refer to **Figure 1** for the two-year trend of the operating revenues as a percent to total operating revenues and revenue by category.

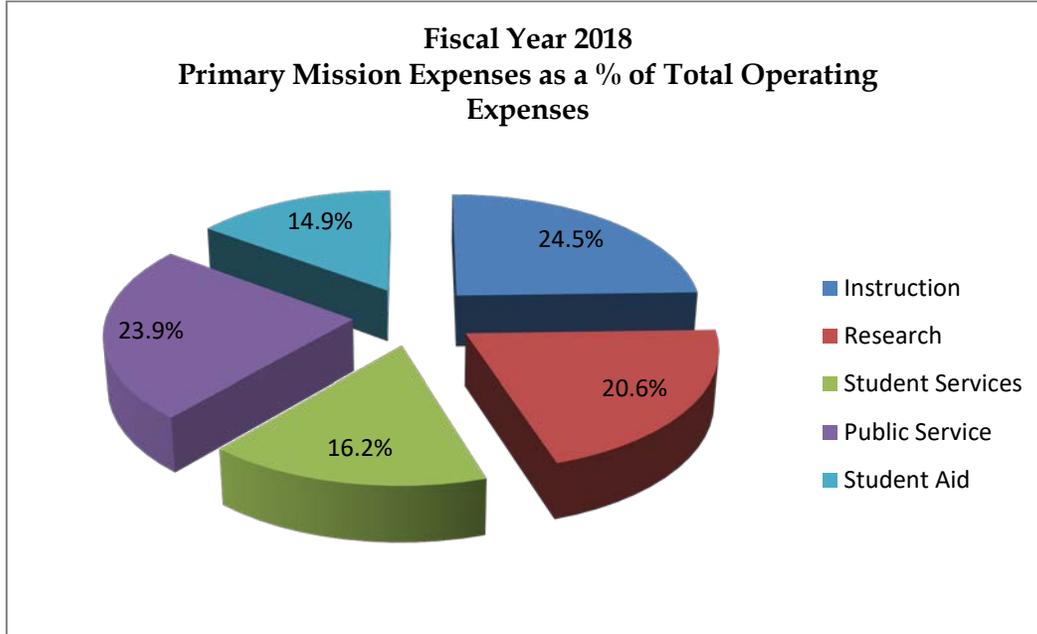
Operating Expenses

Operating expenses totaled \$68.0 million, a decrease of \$2.6 million from last year. Of this amount, \$39.2 million (57.7%) was expended directly for the primary mission of the University – instruction (14.1%), research (11.9%), student services (9.3%), student aid (8.6%), and public service (13.8%). Instruction is the main component of Primary Mission expenses amounting to \$9.6 million in fiscal year 2018 or 14.1%. Refer to **Figure 2** for the operating expenses categorized into the Primary Mission of the University.

(Percentages below do not include depreciation or operations/maintenance allocations.)

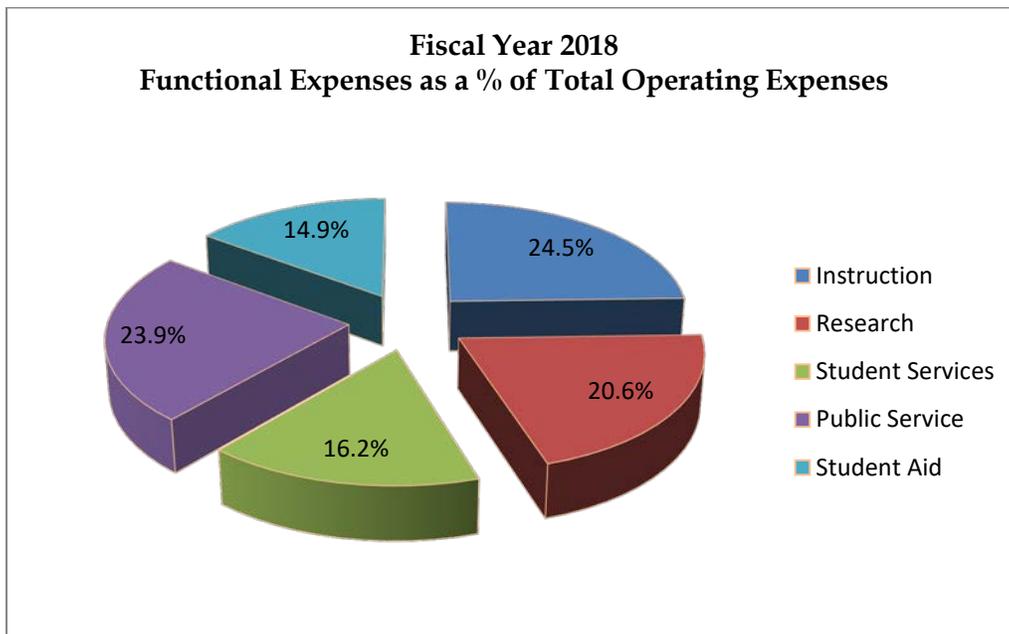
Figure 2





In addition to the Primary Mission expenses of the University, there are expenses from depreciation and operations & maintenance that are allocated to the various functional classifications (See Note 13 – Schedule of Expenses by Program). See below for the operating expenses categorized into the Functional Expenses of the University.

(Percentages below include depreciation and operations/maintenance allocations.)



KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

The University continued to invest in student aid and support services to provide students with opportunities to be successful in fiscal year 2018. For the year ended June 30, 2018, student aid expenses totaled \$5.8 million and scholarship allowances totaled \$5.1 million.

The University had an overall decrease in institutional support of \$0.1 million, which was consistent with the overall expenditure decrease University wide. The large expenditures in the primary areas of instruction, research and student services, in conjunction with minimal increases to fixed cost areas, confirms the University resource allocations are clearly aligned with the University's strategic priorities to support academic and student excellence.

The net loss from operations for the year amounted to \$33.6 million. Non-operating revenues, net of expenses, amounted to \$32.8 million, resulting in a loss before capital appropriations of \$0.8 million for the year. With capital appropriations of \$3.5 million, net position increased by \$2.7 million. Non-operating revenues include state appropriations of \$26.5 million and non-operating federal grants and contracts of \$4.4 million.

Statement of Cash Flows

The Statement of Cash Flows presents information related to the University's cash inflows and outflows summarized by operating activities, noncapital financing activities, capital financing activities and investing activities. The primary purpose of the Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the University during the year, to allow financial statement readers to assess the University's ability to generate future net cash flows, its ability to meet obligations as they become due and its possible need for external financing.

Condensed Statement of Cash Flows

	<u>2018</u>	<u>2017</u>
Cash (used) provided by:		
Operating activities	\$ (34,470,187)	\$ (29,095,167)
Non-capital financing activities	31,825,511	30,417,408
Capital and related financing activities	(2,026,596)	(2,831,576)
Investing activities	<u>-</u>	<u>220,901</u>
Change in cash	(4,671,272)	(1,288,434)
Cash and cash equivalents, beginning year	<u>18,660,458</u>	<u>19,948,892</u>
Cash and cash equivalents, end of year	<u>\$ 13,989,186</u>	<u>\$ 18,660,458</u>

Cash and Investments

Major sources of cash received from operating activities are student tuition and fees of \$10.6 million and grants and contracts of \$18.5 million. Major uses of cash for operating activities were payments to employees for salaries and benefits of \$39.2 million and to vendors and contractors of \$23.0 million.

Noncapital financing activities included state appropriations from the Commonwealth of Kentucky of \$26.5 million.

Capital and related financing activities include purchases and payments of \$5.6 million expended for construction and acquisition of capital assets and for principal and interest payments on the retirement of the University's bonds and other capital related debt.

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

State Appropriations

State appropriations represent approximately 40.0% of all operating and non-operating revenues. The level of state support is a key factor influencing the University's overall financial condition. State appropriation is unrestricted revenue and is included as non-operating revenue. State appropriations are used to support payroll and benefits for University employees.

The following details the net Commonwealth appropriations received by the University for fiscal years ending June 30, 2018 and 2017.

	<u>2018</u>	<u>2017</u>
Commonwealth appropriations	\$ 26,462,300	\$ 26,729,600

Capital Appropriations for the Commonwealth

The University faces financial challenges to maintain and upgrade its capital assets including its infrastructure, buildings and grounds. A combination of revenue sources funds the University's investment in capital improvements, including appropriations provided by the Commonwealth of Kentucky. In fiscal year 2018, the Commonwealth provided capital appropriations of \$3.5 million to the University. State capital appropriations plus federal sources play an important role in the University's efforts to address deferred maintenance projects.

Grant and Contract Revenue

The following table details the University's grant and contract revenue for fiscal years ended June 30, 2018 and 2017.

	<u>2018</u>	<u>2017</u>
Federal grants and contracts, operating	\$ 15,982,090	\$ 16,408,586
Federal grants and contracts, non-operating	4,391,839	3,776,772
State grants and contracts	<u>2,689,931</u>	<u>2,783,697</u>
Total grants and contracts	<u>\$ 23,063,860</u>	<u>\$ 22,969,055</u>

Capital Plan

The University continues to face financial challenges to maintain and upgrade its capital assets including its infrastructure, buildings and grounds. A combination of revenue sources fund the University's investment in capital improvements. Those include appropriations provided by the Commonwealth of Kentucky. In fiscal year 2016-17, the Commonwealth funded one capital project, appropriating state bond funds toward Repair Boilers and Aging Distribution Lines. As of June 30, 2018, \$8.8 million has been expended on this project. State capital appropriations for deferred maintenance were not appropriated. Federal funds are the primary source for the University's College of Agriculture and Land Grant departments.

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

Designated and Non-designated Spending

In the tables below, expenses have been categorized into designated or non-designated spending categories. The designated spending category includes funds expended by function from contracts and grants, land grant, auxiliary and depreciation. These funds must be expended for the purposes for which the funds were received or budgeted. This category also includes funds for student aid. All other spending is categorized as non-designated spending. Total spending for all functions in 2018 in the non-designated category is consistent with 2017.

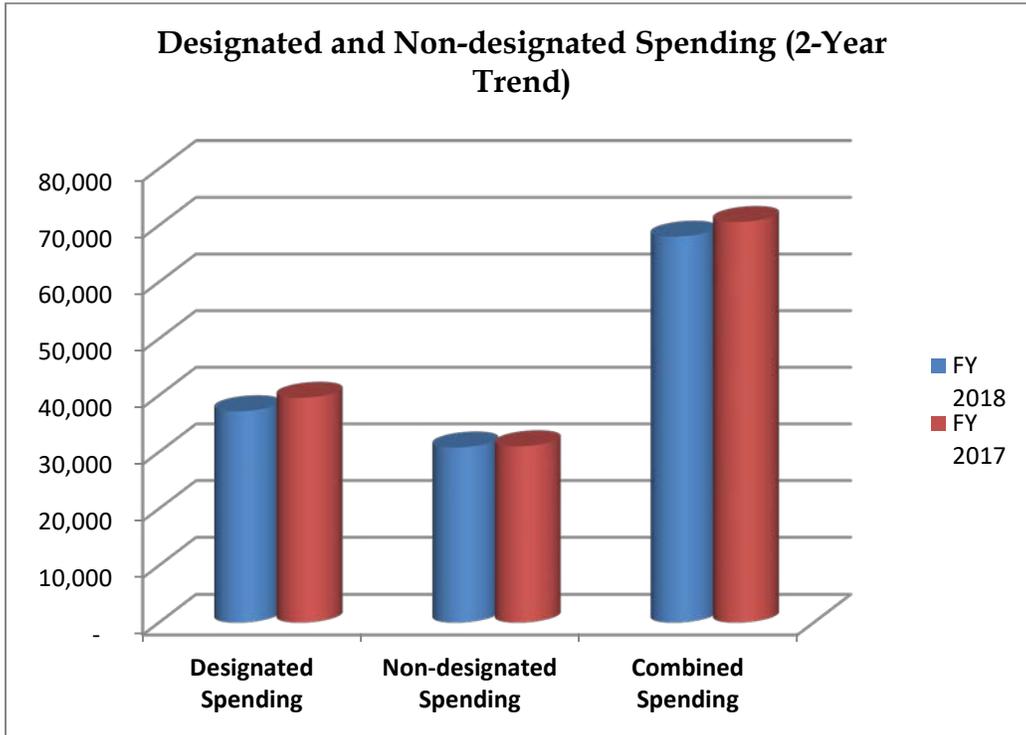
	2018		
	Designated Spending	Non-designated Spending	Combined Spending
Instruction	\$ 679,679	\$ 8,941,956	\$ 9,621,635
Research	8,343,569	(282,310)	8,061,259
Public service	9,595,485	(233,718)	9,361,767
Academic support	277,999	1,143,756	1,421,755
Student services	677,085	5,654,520	6,331,605
Institutional support	1,369,645	10,525,724	11,895,369
Operation and maintenance of plant	-	4,743,469	4,743,469
Student aid	5,518,176	303,450	5,821,626
Auxiliary	5,292,967	-	5,292,967
Depreciation	5,444,547	-	5,444,547
Total	<u>\$ 37,199,152</u>	<u>\$ 30,796,847</u>	<u>\$ 67,995,999</u>

	2017		
	Designated Spending	Non-designated Spending	Combined Spending
Instruction	\$ 1,835,073	\$ 9,088,169	\$ 10,923,242
Research	8,687,330	260,911	8,948,241
Public service	9,071,607	16,696	9,088,303
Academic support	1,745,712	1,113,267	2,858,979
Student services	1,233,403	4,892,776	6,126,179
Institutional support	1,663,318	10,302,408	11,965,726
Operation and maintenance of plant	-	4,632,516	4,632,516
Student aid	5,882,648	713,060	6,595,708
Auxiliary	5,407,271	-	5,407,271
Depreciation	4,048,197	-	4,048,197
Total	<u>\$ 39,574,559</u>	<u>\$ 31,019,803</u>	<u>\$ 70,594,362</u>

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

The graph in **Figure 3** shows a two-year trend of designated, non-designated, and combined spending. Designated spending decreased \$2.4 million in 2018. Non-designated spending decreased \$0.2 million in 2018. Combined spending decreased \$2.6 million in 2018.

Figure 3



Capital Asset and Debt Administration

Capital Assets

Capital assets, net of accumulated depreciation, totaled \$76.9 million at June 30, 2018, a decrease of \$0.9 million. Capital assets as of June 30, 2018 and significant changes in capital assets during the year are as follows (in millions):

	June 30, 2018	Net Additions (Reductions) FY 17-18	June 30, 2017
Land and land improvements	\$ 6.3	\$ -	\$ 6.3
Buildings, fixed equipment and infrastructure	155.2	0.5	154.7
Equipment, vehicles and capitalized software	31.3	1.0	30.3
Library materials and art	10.6	0.1	10.5
Construction in progress	9.6	3.0	6.6
Accumulated depreciation	(136.1)	(5.5)	(130.6)
Total	\$ 76.9	\$ (0.9)	\$ 77.8

KENTUCKY STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2018

Long-Term Debt

At June 30, 2018, bonds and lease payable amounted to \$4.3 million, as summarized below:

	<u>2018</u>	<u>2017</u>
Lease obligations	\$ 1,719,037	\$ 2,245,098
Note payable to City of Frankfort	50,000	150,000
General receipts bonds	2,525,000	2,755,000
Bond discount	<u>(36,345)</u>	<u>(38,307)</u>
Total	<u>\$ 4,257,692</u>	<u>\$ 5,111,791</u>

Economic Factors Impacting Future Periods

University management continues its strategic mission to uniquely position Kentucky State University as Kentucky's small public liberal arts institution of excellence for the citizens of the Commonwealth and for advancing higher education in Kentucky by inspiring innovation, growing leaders and advancing Kentucky. Executive management continues to work with the Council on Postsecondary Education to address the needs of the Commonwealth and believes it is positioning the University to become a strong, financially viable and efficient institution of higher learning.

Future economic factors impacting Kentucky State University include the following known facts:

- Tuition and costs of attendance—Kentucky State University continues to weigh its costs of attendance with the funding provided by the General Assembly to successfully deliver its programs and remain one of the most affordable public institutions in the Commonwealth. Funding levels and methodologies used for institutions of higher education in the Commonwealth are developed and approved by the Council on Postsecondary Education.
- Enrollment growth and student retention—Kentucky State University recruits a diverse student body of traditional, nontraditional and transfer students seeking baccalaureate and advanced degrees. Enrollment stabilization is a priority of University management and specifically, an increased strategy for recruiting in-state students.
- Program expansion—the University is well positioned to meet the needs of Kentuckians through its programs and educational activities. The University offers the following programs: Bachelors in Mass Communications and Journalism, a Masters of Arts in Special Education, and a Masters in Business Administration, a Masters in Public Administration, a Masters in Computer Science, a Masters in Environmental Studies, a Masters of Science in Interdisciplinary Behavioral Studies and a Doctorate in Nursing Practice.
- Regional Stewardship—Kentucky State University continues to meet the economic and community needs of its area of geographic responsibility through collaborative initiatives with businesses, community-based organizations, schools and other educational agencies, citizens and local and state officials.
- Land Grant – Kentucky State University continues to fulfill its mission as a land grant institution providing innovative research opportunities on its research vessel, the Kentucky River Thorobred and community based extension through the Rosenwald Center for Families and Children

The overall financial position of the University was stable during fiscal year 2018. Revenue streams were stressed. As the University adapts to present economic environments, new opportunities for funding will be explored to complement state support. Executive management's goal is to deliver exceptional programs and services to students and constituents while maintaining financial stability. Management believes Kentucky State University is able to sustain its financial position and solidify its standing as a regional university of excellence.

KENTUCKY STATE UNIVERSITY
STATEMENT OF NET POSITION
June 30, 2018

ASSETS

Current assets

Cash and cash equivalents	\$ 13,989,186
Accounts, grants and loans receivable, net	<u>5,087,765</u>
Total current assets	<u>19,076,951</u>

Noncurrent assets

Accounts, grants and loans receivable, net	235,240
Investments	17,734,544
Capital assets, net	<u>76,917,768</u>
Total noncurrent assets	<u>94,887,552</u>

DEFERRED OUTFLOWS OF RESOURCES

Deferred outflows – pension	12,978,170
Deferred outflows – other postemployment benefits	<u>1,510,794</u>
Total deferred outflows	<u>14,488,964</u>

Total assets and deferred outflows of resources 128,453,467

LIABILITIES

Current liabilities

Accounts payable and accrued liabilities	4,352,329
Accrued compensated absences	1,638,427
Unearned revenue	161,199
Deposits and other current liabilities	120,966
Long-term debt, current portion	<u>834,386</u>
Total current liabilities	<u>7,107,307</u>

Non-current liabilities

Net pension liability	73,393,612
Net OPEB liability	12,061,267
Long-term debt, non-current portion	3,423,306
Federal grants refundable	<u>596,898</u>
Total noncurrent liabilities	<u>89,475,083</u>

DEFERRED INFLOWS OF RESOURCES

Deferred inflows – pension	30,589,458
Deferred inflows – other postemployment benefits	<u>204,097</u>
Total deferred inflows	<u>30,793,555</u>

Total liabilities and deferred inflows of resources 127,375,945

NET POSITION

Invested in capital assets, net of related debt	72,660,076
Restricted	
Nonexpendable - endowment	3,562,238
Expendable	5,388,621
Unrestricted	<u>(80,533,413)</u>
Total net position	<u>\$ 1,077,522</u>

See accompanying notes to financial statements.

KENTUCKY STATE UNIVERSITY FOUNDATION, INC.
STATEMENT OF FINANCIAL POSITION
June 30, 2018

ASSETS

Current assets	
Cash and cash equivalents	\$ 1,510,660
Total current assets	<u>1,510,660</u>
Investments, at fair value	9,385,316
Property and equipment	
Equipment	140,400
Buildings and improvements	<u>65,526</u>
	205,926
Accumulated depreciation	<u>(183,884)</u>
Property and equipment, net	22,042
Other assets	<u>34,099</u>
Total assets	<u>\$ 10,952,117</u>

LIABILITIES AND NET ASSETS

Current liabilities	
Accounts payable	\$ 844
Accrued liabilities	<u>3,727</u>
Total liabilities	4,571
Net assets	
Unrestricted	242,591
Temporarily restricted	6,910,849
Permanently restricted	<u>3,794,106</u>
Total net assets	<u>10,947,546</u>
Total liabilities and net assets	<u>\$ 10,952,117</u>

See accompanying notes to financial statements.

KENTUCKY STATE UNIVERSITY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
Year ended June 30, 2018

REVENUES

Operating revenues	
Student tuition and fees (net of scholarship allowances of \$5,069,418)	\$ 11,525,935
Federal grants and contracts	15,982,090
State and local grants and contracts	2,689,931
Auxiliary enterprises:	
Residence halls	2,179,609
Dining	1,913,732
Bookstore	119,680
Other auxiliaries	26,548
Total operating revenues	<u>34,437,525</u>

EXPENSES

Operating expenses	
Educational and general	
Instruction	9,621,635
Research	8,061,259
Public service	9,361,767
Academic support	1,421,755
Student services	6,331,605
Institutional support	11,895,369
Operation and maintenance of plant	4,743,469
Student aid	5,821,626
Depreciation	5,042,714
Auxiliary enterprises	
Residence halls	1,124,604
Dining	2,339,189
Other auxiliaries	816,209
Bookstore	1,012,965
Depreciation	401,833
Total operating expenses	<u>67,995,999</u>

Operating loss (33,558,474)

NONOPERATING REVENUES (EXPENSES)

State appropriations	26,462,300
Federal grants and contracts	4,391,839
Investment income (net of investment expense)	1,174,232
Interest on capital asset-related debt	(236,690)
Other	971,372
Net non-operating revenues	<u>32,763,053</u>

Loss before capital appropriations (795,421)

Capital appropriations 3,548,918

Change in net position 2,753,497

NET POSITION

Net position, beginning of year, as originally stated	8,701,364
Cumulative effect of GASB 75 implementation	<u>(10,377,339)</u>
Net position, beginning of year, as restated	<u>(1,675,975)</u>
Net position, end of year	<u>\$ 1,077,522</u>

See accompanying notes to financial statements.

KENTUCKY STATE UNIVERSITY FOUNDATION, INC.
STATEMENT OF ACTIVITIES
Year ended June 30, 2018

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenues, gains and other support				
Contributions	\$ 6,328	\$ 730,102	\$ 78,882	\$ 815,312
Investment income:				
Interest and dividends	2,623	223,769	-	226,392
Realized and unrealized gains	<u>5,859</u>	<u>357,649</u>	<u>-</u>	<u>363,508</u>
Total investment income	8,482	581,418	-	589,900
Releases from restrictions	<u>1,172,159</u>	<u>(1,172,159)</u>	<u>-</u>	<u>-</u>
Total revenues, gains and other support	1,186,969	139,361	78,882	1,405,212
Expenses				
Scholarships	298,107	-	-	298,107
Operating expenses	161,035	-	-	161,035
Personal services	118,414	-	-	118,414
University support	435,343	-	-	435,343
Student support	130,447	-	-	130,447
Travel and promotion	<u>61,017</u>	<u>-</u>	<u>-</u>	<u>61,017</u>
Total expenses	<u>1,204,363</u>	<u>-</u>	<u>-</u>	<u>1,204,363</u>
Change in net assets, before reclassification	(17,394)	139,361	78,882	200,849
Reclassification	<u>6,662</u>	<u>(10,162)</u>	<u>3,500</u>	<u>-</u>
Change in net assets	(10,732)	129,199	82,382	200,849
Net assets, beginning of year	<u>253,323</u>	<u>6,781,650</u>	<u>3,711,724</u>	<u>10,746,697</u>
Net assets, end of year	<u>\$ 242,591</u>	<u>\$ 6,910,849</u>	<u>\$ 3,794,106</u>	<u>\$ 10,947,546</u>

See accompanying notes to financial statements.

KENTUCKY STATE UNIVERSITY
STATEMENT OF CASH FLOWS
Year ended June 30, 2018

Cash flows from operating activities	
Tuition and fees	\$ 10,585,839
Grants and contracts	18,494,647
Payments to suppliers	(23,036,507)
Payments to employees	(39,227,212)
Payments to students	(5,555,850)
Collection of loans issued to students	11,144
Auxiliary enterprises:	
Residence halls and dining	4,111,668
Bookstore	119,680
Other auxiliaries	26,548
Other payments	(144)
Net cash from operating activities	<u>(34,470,187)</u>
Cash flows from non-capital financing activities	
State appropriations	26,462,300
Federal grants and contracts	4,391,839
Other	<u>971,372</u>
Net cash from non-capital financing activities	31,825,511
Cash flows from capital financing activities	
Purchases of capital assets	(4,522,840)
Principal paid on capital debt	(854,099)
Interest paid on capital debt	(198,575)
Capital appropriations	<u>3,548,918</u>
Net cash from capital financing activities	(2,026,596)
Cash flows from investing activities	
Investment income	1,174,232
Proceeds from sale of investments	7,195,829
Purchases of investments	<u>(8,370,061)</u>
Net cash from investing activities	<u>-</u>
Net change in cash and cash equivalents	(4,671,272)
Cash and cash equivalents at beginning of year	<u>18,660,458</u>
Cash and cash equivalents at end of year	<u><u>\$ 13,989,186</u></u>

(Continued)

KENTUCKY STATE UNIVERSITY
STATEMENT OF CASH FLOWS
Year ended June 30, 2018

**Reconciliation of net operating loss to net cash
from operating activities**

Operating loss	\$ (33,558,474)
Adjustments to reconcile operating loss to net cash from operating activities:	
Depreciation expense	5,444,547
Changes in assets and liabilities:	
Receivables, net	(864,293)
Collection of loans issued to students	11,144
Accounts payable and accrued liabilities	(149,002)
Unearned revenue	(253,321)
Deposits	18,327
Deferred outflows – pension and OPEB	4,483,823
Deferred inflows – pension and OPEB	14,015,527
Net pension liability	(24,678,942)
Net OPEB liability	<u>1,060,477</u>
Net cash from operating activities	<u>\$ (34,470,187)</u>

See accompanying notes to financial statements.

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity: Kentucky State University (the University) is a component unit of the Commonwealth of Kentucky (the Commonwealth) and is included in the general-purpose financial statements of the Commonwealth. The Kentucky State 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 or income thereon that the Foundation holds and invests is restricted by the donors to the activities of the University. 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 financial statements.

Basis of Presentation: The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB), including Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments, and Statement No. 35, Basic Financial Statements and Management's Discussion and Analysis of Public College and Universities, issued in June and November, 1999, respectively. The University reports as a Business Type Activity (BTA), as defined by GASB Statement No. 35. BTA's are those activities that are financed in whole or in part by fees charged to external parties for goods and services. The University, as a BTA, has adopted GASB Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements. Therefore, the University follows GASB pronouncements and all Financial Accounting Standards Board pronouncements except those that conflict with or contradict GASB pronouncements.

Basis of Accounting: 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.

GASB Statement No. 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 asset 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. Such positions include the University's permanent endowment funds.
 - 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.
- **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.

(Continued)

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The financial statement presentation required by GASB Statement No. 35 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.

Cash Equivalents: For the Statement of Cash Flows, the University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Accounts, Grants, and Loans Receivable, net: Accounts receivables consist of tuition and fee charges, loans to students and amounts due from federal and state governments, non-governmental sources, in connection with reimbursements of allowable expenses made pursuant to grants and contracts. Accounts receivables are recorded net of allowance for doubtful accounts.

Allowance for Doubtful Accounts: The allowance for doubtful accounts is established through a provision for doubtful accounts charged to expense. The allowance represents an amount, which, in management's judgment, will be adequate to absorb probable losses on existing accounts that may become uncollectible.

Inventories: Inventories are stated at the lower of cost (first-in, first-out method) or market and consist of physical plant items. Inventories consist of physical plant, postage and printing supplies.

Endowment Funds: Kentucky State University recognizes its fiduciary duty not only to invest the University's endowment holdings in formal compliance with the Uniform Prudent Management of Institutional Funds Act (UPMIFA) but also to manage those funds in continued recognition of the basic long-term nature of the University. The University interprets this to mean, in addition to the adopted spending guidelines and restrictions described below, that the assets of the University shall be actively managed, that is, investment decisions regarding the particular securities to be purchased or sold shall be the result of the conscious exercise of discretion. The University recognizes that, commensurate with its overall objective of maximizing long-range return while maintaining a high standard of portfolio quality and consistency of return, it is necessary that proper diversification of assets be maintained both among and within the classes of securities held. Within this context of active management and the necessity of adherence to proper diversification, the University relies upon appropriate professional advice.

The University recognizes that long-term objectives are most important, but it is also necessary that shorter-term benchmarks be used to assess the periodic performance of the investment program. The University anticipates annual spending of five percent (5%) of the average market value for the past three years, the amount of which shall be determined in January of each year.

The University believes that it is prudent to diversify endowment investments so as to minimize the risks of large losses and has established asset allocation ranges based upon the University's participation demographics, anticipated cash flow requirements and the expected returns of the capital markets.

Investments: Investments are valued at fair value based on quoted market prices.

Capital Assets: Capital assets are stated at cost at date of acquisition or, in the case of gifts, at fair value at date of gift. Equipment with a unit cost of \$2,000 or more and having an estimated useful life of greater than one year is capitalized. Renovations to buildings and 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.

(Continued)

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Depreciation of capital assets is computed on a straight-line basis over the estimated useful lives of the respective assets. The University capitalizes, but does not depreciate, works of art and historical treasures that are held for exhibition, education, research and public service. Estimated lives used for depreciation purposes are as follows:

Classification	Estimated Life
Improvements	20 years
Buildings	40 years
Transportation equipment	5-15 years
Equipment	5-20 years
Enterprise Resource Software	7 years
Library holdings	10 years

Compensated Absences: The liability and expense incurred for employee vacation and sick pay are recorded as accrued compensated absences in the statement of net position and as a component of compensation and benefit expense in the statement of revenues, expenses and changes in net position.

Unearned Revenue: Unearned revenue includes amounts received for tuition and fees prior to the end of the fiscal year but related to the subsequent reporting period. Unearned revenues also include amounts received from grant and contract sponsors and state deferred maintenance funds that have not yet been earned.

Pensions and Other Postemployment Benefits (OPEB): For purposes of measuring the net pension liability, net OPEB liability, deferred outflows of resources and deferred inflows of resources, and related expense, information about the fiduciary net position of the Kentucky Employees Retirement System (KERS) and Kentucky Teachers' Retirement System (KTRS) and additions to/deductions from KERS's and KTRS's fiduciary net position have been determined on the same basis as they are reported by KERS and KTRS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

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 Foundation has received a determination from the Internal Revenue Service granting exemption from federal income taxation pursuant to the provisions of the Internal Revenue Code section 501(c)(3).

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.

Operating Activities: The University defines operating activities, as reported on the statement 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 and certain federal appropriations, gifts and investment income, are recorded as non-operating revenues, in accordance with GASB Statement No. 35.

(Continued)

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Scholarship Discounts and Allowances: Financial aid to students is reported in the financial statements under the alternative method as prescribed by the National Association of College and University Business Officers (NACUBO). Certain aid, such as loans and funds provided to students awarded by third parties, is accounted for as third party payments (credited to the student's account as if the student made the payment). All other aid is reflected in the financial statements as operating expenses, or scholarship allowances, which reduce revenues. The amount reported as operating expenses represents the portion of aid that was provided to the student in the form of cash. Scholarship allowances represent the portion of aid provided to the student in the form of reduced tuition. Under the alternative method, these amounts are computed by allocating the cash payments to students, excluding payments for services, on the ratio of total aid to the aid not considered to be third party aid.

Federal Grants and Contracts: Per GASB Statement No. 24, pass-through grants should be reported as revenues and expenses in the financial statements if that entity has any administrative or direct financial involvement in the program. An entity has administrative involvement if it determines eligible secondary recipients or projects, even if using grantor-established criteria. Therefore, Pell Grants are considered non-exchange transactions and are recorded as non-operating revenues in the accompanying financial statements.

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 disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Component Unit Disclosure: The accompanying 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 FASB. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features.

During the year ended June 30, 2018, the Foundation made distributions of approximately \$435,343 on behalf of the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the Kentucky State University Foundation, Inc. at P.O. Box 4210, Frankfort, KY 40604.

Recent Accounting Pronouncements Adopted/Implemented: As of June 30, 2018, the GASB has issued the following statements which were implemented by the University.

- GASB Statement No. 75, *Account and Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB). It also improves information provided by state and local governmental employers about financial support for OPEB that is provided by other entities. The University adopted the Statement during the year ended June 30, 2018 and the adoption resulted in a decrease in net position at July 1, 2017 of \$10,377,339 to reflect the beginning of year net OPEB liability and deferred outflow of resources.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- GASB Statement No. 85, *Omnibus*. The objective of this Statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. This Statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits [OPEB]). The adoption of this standard had no effect on the University's net position or changes therein.
- GASB Statement No. 86, *Certain Debt Extinguishment Issues*. The primary objective of this Statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources—resources other than the proceeds of refunding debt—are placed in an irrevocable trust for the sole purpose of extinguishing debt. The adoption of this standard had no effect on the University's net position or changes therein.

NOTE 2 - CASH, CASH EQUIVALENTS, AND INVESTMENTS

The statement of net position classification "cash and cash equivalents" includes all readily available sources of cash such as petty cash and demand deposits.

At June 30, 2018, the University had petty cash funds totaling zero, and deposits as reflected by bank balances as follows:

	<u>2018</u>
Insured, commercial banks	\$ 250,000
Uninsured, commercial banks; collateral held by pledging institution's agent in the University's name	371,211
Uninsured and uncollateralized, commercial banks	170,958
Maintained by Commonwealth of Kentucky, collateral held by the Commonwealth in the Commonwealth's name	<u>14,311,402</u>
	<u>\$ 15,103,571</u>

The difference in the cash carrying amount per the statement of net position and the above balances represented items in transit. At June 30, 2018, the University had no cash and cash equivalents that are restricted for capital expenditures.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 2 - CASH, CASH EQUIVALENTS, AND INVESTMENTS (Continued)

As of June 30, 2018, the University had the following investments and maturities:

Investment Maturities (in years)

<u>Investment Type</u>	<u>Fair Value</u>	<u>< 1</u>	<u>1-5</u>	<u>6-10</u>	<u>11-20</u>
Money market funds	\$ 907,305	\$ 907,305	\$ -	\$ -	\$ -
Equities and equity funds	10,143,085	10,143,085	-	-	-
Alternative strategies funds	635,723	635,723	-	-	-
Real assets funds	1,324,938	1,324,938	-	-	-
Corporate bonds	974,624	202,916	404,602	367,106	-
Government bonds	1,214,667	249,077	422,029	543,561	-
Other bond funds	<u>2,534,202</u>	<u>2,534,202</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 17,734,544</u>	<u>\$15,997,246</u>	<u>\$ 826,631</u>	<u>\$ 910,667</u>	<u>\$ -</u>

The University has an investment management agreement with Fifth Third Bank (Fifth Third). Fifth Third serves individual and institutional clients.

The University has the following recurring fair value measurements as of June 30, 2018:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Money market funds	\$ 907,305	\$ 907,305	\$ -	\$ -
Equities and equity funds	10,143,085	10,143,085	-	-
Alternative strategies funds	635,723	635,723	-	-
Real assets funds	1,324,938	1,324,938	-	-
Corporate bonds	974,624	974,624	-	-
Government bonds	1,214,667	1,214,667	-	-
Other bond funds	<u>2,534,202</u>	<u>2,534,202</u>	<u>-</u>	<u>-</u>
	<u>\$ 17,734,544</u>	<u>\$ 17,734,544</u>	<u>\$ -</u>	<u>\$ -</u>

All securities classified in level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities.

Credit Risk: The University's average credit quality rating according to Moody's is Aa3.

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The University does not have a formal policy to specifically limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University does not have a formal policy for concentration of credit risk.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The University does not have a formal policy for custodial credit risk.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 3 - ACCOUNTS, GRANTS AND LOAN RECEIVABLE

Accounts, grants and loans receivable consist of the following as of June 30, 2018:

Student tuition and fees	\$ 2,421,086
Student loans	1,262,458
Grants and contracts	3,629,310
Other	17,350
	<u>7,330,204</u>
Less: allowance for doubtful accounts	<u>(2,007,199)</u>
	5,323,005
Less: non-current portion	<u>(235,240)</u>
Current portion	<u>\$ 5,087,765</u>

NOTE 4 - CAPITAL ASSETS, NET

Capital assets as of June 30, 2018, are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions/ Transfers</u>	<u>Ending Balance</u>
<u>Cost</u>				
Land and improvements	\$ 6,275,031	\$ -	\$ -	\$ 6,275,031
Buildings	154,741,818	446,243	-	155,188,061
Equipment	24,594,798	746,054	-	25,340,852
Computer software	1,611,447	8,923	-	1,620,370
Library holdings	10,488,366	159,705	-	10,648,071
Transportation equipment	4,160,577	203,484	-	4,364,061
Construction in progress	<u>6,651,604</u>	<u>3,396,753</u>	<u>446,243</u>	<u>9,602,114</u>
	208,523,641	4,961,162	446,243	213,038,560
<u>Accumulated depreciation</u>				
Buildings	99,521,389	2,310,432	-	101,831,821
Equipment	17,264,642	2,757,422	-	20,022,064
Library holdings	10,334,171	11,304	-	10,345,475
Transportation equipment	<u>3,563,964</u>	<u>357,468</u>	-	<u>3,921,432</u>
	<u>130,684,166</u>	<u>5,436,626</u>	-	<u>136,120,792</u>
Capital assets, net	<u>\$ 77,839,475</u>	<u>\$ (475,464)</u>	<u>\$ 446,243</u>	<u>\$ 76,917,768</u>

Construction in progress consists primarily of a project to repair and replace boilers and distribution lines. It is estimated that it will cost an additional \$1.4 million to complete and will be completed in fiscal year 2019.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 5 - UNEARNED REVENUE

Unearned revenue consists of the following as of June 30, 2018:

Unearned summer school tuition and fees	\$ 155,144
Unearned grants and contracts	<u>6,055</u>
	<u>\$ 161,199</u>

NOTE 6 - LONG-TERM LIABILITIES

Long-term liabilities as of June 30, 2018, are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>	<u>Non-current Portion</u>
General receipts bonds	\$ 2,755,000	\$ -	\$ 230,000	\$ 2,525,000	\$ 240,000	\$ 2,285,000
Note payable – City of Frankfort	150,000	-	100,000	50,000	50,000	-
Capital lease obligations - energy savings	2,245,098	-	526,061	1,719,037	548,870	1,170,167
Bond discount	<u>(38,307)</u>	-	<u>(1,962)</u>	<u>(36,345)</u>	<u>(4,484)</u>	<u>(31,861)</u>
Total bonds payable and capital lease obligations	5,111,791	-	854,099	4,257,692	834,386	3,423,306
Federal grants refundable	<u>731,695</u>	-	<u>134,797</u>	<u>596,898</u>	-	<u>596,898</u>
Total long-term liabilities	<u>\$ 5,843,486</u>	<u>\$ -</u>	<u>\$ 988,896</u>	<u>\$ 4,854,590</u>	<u>\$ 834,386</u>	<u>\$ 4,020,204</u>

The outstanding General Receipts Bonds Series A Bonds have interest rates from 3.625% - 3.875%. The bonds mature through 2027. The reserve requirements for these issues have been fully funded as of June 30, 2018.

All bonds are collateralized by University property and the pledge of certain revenues, tuition and fees.

The net book value of assets acquired through the capital leases included in the above schedule was approximately \$2,618,566 as of June 30, 2018.

In 2009, the University signed a 10-year promissory note with the City of Frankfort, for the purchase of real property. The following is a schedule of future minimum payments required for the note payable at June 30, 2018:

<u>Year ending June 30,</u> 2019	<u>\$ 50,000</u>
	<u>\$ 50,000</u>

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 6 - LONG-TERM LIABILITIES (Continued)

The principal and interest repayment requirements relating to the outstanding bonds payable at June 30, 2017, are as follows:

<u>Year ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2019	\$ 240,000	\$ 97,291	\$ 337,291
2020	250,000	88,291	338,291
2021	260,000	78,791	338,791
2022	270,000	68,781	338,781
2023	280,000	58,319	338,319
2024-2027	<u>1,225,000</u>	<u>120,900</u>	<u>1,345,900</u>
Total	<u>\$ 2,525,000</u>	<u>\$ 512,373</u>	<u>\$ 3,037,373</u>

During 2005, the University entered into a capital lease for an energy management project. The lease obligation has an interest rate of 4.29% and requires annual payments of principal and interest through 2021. The lease obligation will be paid with guaranteed energy savings.

The following is a schedule of future minimum payments required for the capital lease obligations at June 30, 2018:

<u>Year ending June 30,</u>	
2019	\$ 616,792
2020	616,792
2021	<u>616,791</u>
Total minimum lease payments	1,850,375
Less: amounts representing interest	<u>(131,337)</u>
Present value of minimum lease payment	<u>\$ 1,719,038</u>

NOTE 7 - OPERATING LEASES

The University leases certain assets under operating lease agreements. The operating leases expire in various years through 2022. These leases do not transfer assets at the end of the lease term. Periods on these leases range from one to five years and requires the University to pay all executor costs (maintenance, insurance, taxes).

Future minimum lease payments at June 30, 2018, are as follows:

<u>Year ending June 30,</u>	
2019	\$ 145,538
2020	52,303
2021	46,303
2022	<u>17,034</u>
	\$261,178

Lease expense was \$222,509 for the year ended June 30, 2018.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS

Kentucky Employees' Retirement System - Defined Benefit Plan

Plan Description – The University contributes to 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. 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, required supplementary information, and detailed information about the pension plan's fiduciary net position. 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.

Benefits Provided

Non-Hazardous

	Tier 1 Participation Prior to <u>September 1, 2008</u>	Tier 2 Participation September 1, 2008 through <u>December 31, 2013</u>	Tier 3 Participation <u>January 1, 2014</u>
Benefit Formula	Final Compensation x Benefit Factor x Years of Service		Cash Balance Plan
Final Compensation	Average of the highest 5 fiscal years (must contain at least 48 months). Includes lump-sum compensation payments (before and at retirement).	5 complete fiscal years immediately preceding retirement; each year must contain 12 months. Lump-sum compensation payments (before and at retirement) are not to be included in creditable compensation.	No Final Compensation
Benefit Factor	1.97% or 2.0% for those retiring with service for all months between 1/1998 and 1/1999.	10 years or less = 1.10%. Greater than 10 years, but no more than 20 years = 1.30%. Greater than 20 years, but no more than 26 years = 1.50%. Greater than 26 years, but no more than 30 years = 1.75%. Additional years above 30 – 2.00% (2.00% benefit factor only applies to service earned in excess of 30 years).	No benefit factor. A life annuity can be calculated in accordance with actuarial assumptions and methods adopted by the board based on member's accumulated account balance.
Cost of Living Adjustment (COLA)	No COLA unless authorized by the Legislature. If authorized, the COLA is limited to 1.5%. This impacts all retirees regardless of Tier.		
Unreduced Retirement Benefit	Any age with 27 years of service. Age 65 with 48 months of service. Money purchase for age 65 with less than 48 months based on contributions and interest.	Rule of 87: Member must be at least age 57 and age plus earned service must equal 87 years at retirement to retire under this provision. Age 65 with 5 years of earned service. No month purchased calculations.	

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

	Tier 1 Participation Prior to <u>September 1, 2008</u>	Tier 2 Participation September 1, 2008 through <u>December 31, 2013</u>	Tier 3 Participation <u>January 1, 2014</u>
Reduced Retirement Benefit	Any age with 25 years of service. Age 55 with 5 years of service.	Age 60 with 10 years of service. Excludes purchased service (exception: refunds, omitted, free military).	No reduced retirement benefit.

Hazardous

	Tier 1 Participation Prior to <u>September 1, 2008</u>	Tier 2 Participation September 1, 2008 through <u>December 31, 2013</u>	Tier 3 Participation <u>January 1, 2014</u>
Benefit Formula	Final Compensation X Benefit Factor X Years of Service	Cash Balance Plan	
Final Compensation	Highest 3 fiscal years (must contain at least 24 months). Includes lump-sum compensation payments (before and at retirement).	3 highest salaries; each year must contain 12 months. Lump-sum compensation payments (before and at retirement) are not to be included in creditable compensation.	No Final Compensation
Benefit Factor	2.49%	10 years or less = 1.30%. Greater than 10 years, but no more than 20 years = 1.50%. Greater than 20 years, but no more than 26 years = 2.25%. Greater than 25 years = 2.50%.	No benefit factor. A life annuity can be calculated in accordance with actuarial assumptions and methods adopted by the board based on member's accumulated account balance.
Cost of Living Adjustment (COLA)	No COLA unless authorized by the Legislature. If authorized, the COLA is limited to 1.5%. This impacts all retirees regardless of Tier.		
Unreduced Retirement Benefit	Any age with 20 years of service. Age 55 with 60 months of service.	Any age with 25 years of service. Age 60 with 60 months of service.	Any age with 25 years of service. Age 60 with 60 months of service.
Reduced Retirement Benefit	Age 50 with 15 years of service.	Age 50 with 15 years of service.	No reduced retirement benefit.

Contributions - Benefit and contribution rates are established by state statute. Per Kentucky Revised Statute 61.565(3) contribution requirements of the active employees and the participating organizations are established and may be amended by the KRS Board. For the fiscal year ended June 30, 2018, University non-hazardous and hazardous employees were required to contribute 5 percent of their annual covered salary for retirement benefits for the year ended June 30, 2018. Non-hazardous and hazardous

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

employees with a participation date after September 1, 2008 were required to contribute an additional 1 percent of their covered salary for retiree healthcare benefits. The University was contractually required to contribute 41.06 percent of annual covered payroll for non-hazardous pay and 21.44 percent for hazardous pay to the pension plan for the year ended June 30, 2018. Actuarially determined as an amount that, when combined with employee contributions, is expected to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The University's total contributions to KERS for the year ended June 30, 2018 was \$1,531,999, equal to the required contributions for the year.

Pension liabilities, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions - At June 30, 2018, the University reported a liability of \$32,618,138 for its proportionate share of the non-hazardous net pension liability and \$237,122 for hazardous. The net pension liability was measured as of June 30, 2017 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The University's proportion of the net pension liability was based on actual contributions to the pension plan during the measurement period. At June 30, 2018, the University's proportion was 0.24 percent for non-hazardous and 0.05 percent for hazardous, respectively.

For the year ended June 30, 2018, the University's actuarially calculated pension expense was \$2,754,949 for non-hazardous and \$92,166 for hazardous. At June 30, 2018, the University reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

<u>2018</u>	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Non-hazardous:		
Difference between expected and actual experience	\$ 5,802	\$ 210,046
Net difference between projected and actual earnings on investments	157,733	-
Changes of assumptions	4,138,399	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	-	2,567,605
University contributions subsequent to measurement date	<u>1,471,207</u>	<u>-</u>
	<u>\$ 5,773,141</u>	<u>\$ 2,777,651</u>
Hazardous:		
Difference between expected and actual experience	\$ 8,966	\$ -
Net difference between projected and actual earnings on investments	2,630	-
Changes of assumptions	43,572	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	106,497	-
University contributions subsequent to measurement date	<u>60,792</u>	<u>-</u>
	<u>\$ 222,457</u>	<u>\$ -</u>

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

At June 30, 2018, the University reported \$1,531,999 as deferred outflows of resources related to pensions resulting from University contributions subsequent to the measurement date that will be recognized as a reduction of the net pension liability in the following fiscal year. Deferred outflows and deferred inflows of resources at June 30, 2018, related to pensions will be recognized in pension expense as follows:

	<u>Non-hazardous</u>	<u>Hazardous</u>
2018	\$ 857,284	\$ 76,546
2019	667,676	78,197
2020	44,244	9,910
2021	<u>(44,920)</u>	<u>(2,984)</u>
	<u>\$ 1,524,284</u>	<u>\$ 161,665</u>

Actuarial assumptions - The total pension liability at the measurement date of June 30, 2017 was determined by actuarial valuations as of June 30, 2017, using the following actuarial assumptions, applied to all periods included in the measurement.

	<u>2017</u>
Inflation	2.30%
Salary increases, average including inflation	3.05
Investment rate of return, non-hazardous	5.25
Investment rate of return, hazardous	6.25

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set back 1 year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back 4 years for males) is used for the period after disability retirement.

The actuarial assumptions used in the June 30, 2017 valuation were based on the results of an actuarial experience study for the period July 1, 2008 - June 30, 2013.

The long-term expected return on plan assets is reviewed as part of the regular experience studies prepared every five years for KERS. The most recent analysis is outlined in a report dated December 5, 2015. Several factors are considered in evaluating the long-term rate of return assumption including long-term historical data, estimates inherent in current market data, and a log - normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected return, net of investment expense and inflation) were developed by the investment consultant for each major asset class. These ranges were combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and then adding expected Inflation. The assumption is intended to be a long-term assumption and is not expected to change absent a significant change in the asset allocation, a change in the inflation assumption, or a fundamental change in the market that alters expected returns in future years.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

The target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Non-hazardous</u>	
	<u>Target Allocation</u>	<u>Long-Term Nominal Rate of Return</u>
<u>2018</u>		
U.S. Equity	17.50%	5.75%
International Equity	17.50	7.38
Global Bonds	10.00	2.63
Global Credit	17.00	3.63
Real Estate	5.00	6.63
Absolute Return	10.00	5.63
Real Return	10.00	5.13
Private Equity	10.00	8.25
Cash Equivalents	<u>3.00</u>	1.88
Total	<u>100%</u>	

<u>Asset Class</u>	<u>Hazardous</u>	
	<u>Target Allocation</u>	<u>Long-Term Nominal Rate of Return</u>
<u>2018</u>		
U.S. Equity	17.50%	5.75%
International Equity	17.50	7.38
Global Bonds	4.00	2.63
Global Credit	2.00	3.63
High Yield	7.00	5.75
Emerging Market Debt	5.00	5.50
Private Credit	10.00	8.75
Real Estate	5.00	7.63
Absolute Return	10.00	5.63
Real Return	10.00	6.13
Private Equity	10.00	8.25
Cash Equivalents	<u>2.00</u>	1.88
Total	<u>100%</u>	

Changes in Assumptions and Benefit Terms Since Prior Measurement Date - Since the prior measurement date, the demographic and economic assumptions that affect the measurement of the total pension liability have been updated as follows:

- The assumed investment rate of return was decreased from 6.75% to 5.25% (Non-hazardous) and 7.50% to 6.25% (Hazardous).
- The assumed rate of inflation was reduced from 3.25% to 2.30%.
- Payroll growth assumption was reduced from 4.00% to 3.05%.

Changes Since Measurement Date - There were no changes between the measurement date of the collective net pension liability and the employer's reporting date.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

Discount rate - The discount rate used to measure the total pension liability was 5.25% (Non-hazardous) and 6.25% (Hazardous), which was reduced from the 6.75% (Non-hazardous) and 7.50% (Hazardous) discount rates used in the prior year. The projection of cash flows used to determine the discount rate assumed that local employers would contribute the actuarially determined contribution rate of projected compensation over the remaining 26-year amortization period of the unfunded actuarial accrued liability. The actuarial determined contribution rate is adjusted to reflect the phase in of anticipated gains on actuarial value of assets over the first four years of the projection period. Projected inflows from investment earnings were calculated using the long-term assumed investment return of 5.25% for Non-Hazardous and 6.75% for Hazardous for the June 30, 2017 actuarial valuation. The long-term assumed investment rate of return was applied to all periods of projected of benefit payments to determine the total pension liability.

Sensitivity of the University's proportionate share of the net pension liability to changes in the discount rate - The University's proportionate share of the net pension liability has been calculated using a discount rate of 5.25% (Non-hazardous) for the June 30, 2017 actuarial valuation. The following presents the University's proportionate share of the net pension liability calculated using a discount rate 1% higher and 1% lower than the current rate as of June 30, 2018:

	1% Decrease <u>(4.25%)</u>	Current Discount Rate <u>(5.25%)</u>	1% Increase <u>(6.25%)</u>
<u>Non-Hazardous</u>			
Proportionate share of the Collective Net Pension Liability	\$ 37,242,518	\$ 32,618,138	\$ 28,773,195
	1% Decrease <u>(5.25%)</u>	Current Discount Rate <u>(6.25%)</u>	1% Increase <u>(7.25%)</u>
<u>Hazardous</u>			
Proportionate share of the Collective Net Pension Liability	\$ 301,620	\$ 237,122	\$ 183,602

Kentucky Teachers' Retirement System - Defined Benefit Plan

Plan Description –The Kentucky Teachers' Retirement System (KTRS), a cost sharing - multiple employer public employee retirement system. KTRS is a defined benefit plan providing for retirement, disability, death benefits and health insurance. Participants have a fully vested interest after the completion of 60 months of service, 12 of which are current service. KTRS issues a publicly available financial report that includes financial statements, required supplementary information, and detailed information about the pension plan's fiduciary net position. That report may be obtained by writing to Kentucky Teachers' Retirement System, 479 Versailles Road, Frankfort, Kentucky, 40601 or by calling (502) 573-3266.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

Benefits Provided

	Tier 1 Participation Prior to <u>July 1, 2008</u>	Tier 2 Participation on or After <u>July 1, 2008</u>
Covered Employees:	University faculty and professional staff that do not choose the Optional Retirement Plan (Deferred Contribution)	University faculty and professional staff that do not choose the Optional Retirement Plan (Deferred Contribution)
Benefit Formula:	Final Compensation X Benefit Factor X Years of Service	
Final Compensation:	Average of the highest 5 annual salaries reduced 5% per year from the earlier of age 60 or the date 27 years of service would have been completed. Average of the highest 3 annual salaries if age 55 with 27 or more years of service. The minimum annual service allowance for all members is \$440 multiplied by credited service.	Average of the highest 5 annual salaries reduced 6% per year from the earlier of age 60 or the date 27 years of service would have been completed. Average of the highest 3 annual salaries if age 55 with 27 or more years of service. The minimum annual service allowance for all members is \$440 multiplied by credited service.
	Tier 1 Participation Prior to <u>July 1, 2008</u>	Tier 2 Participation on or After <u>July 1, 2008</u>
Benefit Factor:	Non-University members: 2.00% for service prior to 7/1/1983; 2.50% for service after 7/1/1983; 2.00% if participation after 7/1/2002 and less than 10 years; 2.50% if participation after 7/1/2002 and more than 10 years; 3.00% if retire after 7/1/2004 with more than 30 years. University members: 2.0% for each year of service.	Non-University members: 1.70% if less than 10 years; 2.00% if greater than 10 years, but no more than 20 years; 2.30% if greater than 20 years, but no more than 26 years; 2.50% if greater than 26 years, but no more than 30 years; 3.00% for service greater than 30 years. University members: 1.50% if less than 10 years; 1.70% if greater than 10 years, but less than 20 years; 1.85% if greater than 20 years, but less than 27 years; 2.00% if greater than 27 years.
Cost of Living Adjustment (COLA):	1.5% annually additional ad hoc increases must be authorized by the General Assembly.	

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

Unreduced Retirement Benefit:	Any age with 27 years of Kentucky service. Age 55 with 5 years of Kentucky service.	Any age with 27 years of Kentucky service. Age 60 with 5 years of Kentucky service. Age 55 with 10 years of Kentucky service.
Reduced Retirement Benefit:	Must be retired for service or disability to be eligible. Retired members are given a supplement based upon a contribution supplement table approved by the KTRS Board of Trustees. The retired member pays premiums in excess of the monthly supplement.	

Contributions - Benefit and contribution rates are established by state statute. Per Kentucky Revised Statutes 161.540, 161.550 and 161.565, contribution requirements of the active employees and the participating organizations are established and may be amended by the KTRS Board. For the fiscal year ended June 30, 2018, University employees were required to contribute 7.625 percent of their annual covered salary for retirement benefits. The University was contractually required to contribute 15.865 percent of covered payroll for the year ended June 30, 2018. The actuarially determined amount, when combined with employee contributions, is expected to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The University's total contributions to KTRS for the year ending June 30, 2018 was \$1,729,748 and were equal to the required contributions for the year. In addition, the Commonwealth of Kentucky contributes ad hoc annual cost of living adjustments provided by the General Assembly for KTRS retirees at a contribution rate of 3.25% for the year ending June 30, 2018.

Pension liabilities, pension expense, and deferred outflows of resources and deferred inflows of resources related to pensions - At June 30, 2018, the University reported a liability for its proportionate share of the net pension liability that reflected a reduction for pension support provided to the University by the Commonwealth of Kentucky. The amount recognized by the University as its proportionate share of the net pension liability, the related State support, and the total portion of the net pension liability that was associated with the University were as follows:

	<u>2018</u>
University's proportionate share of the net pension liability	\$ 40,538,352
Commonwealth of Kentucky's proportionate share of the net pension liability associated with the University	<u>32,308,289</u>
	<u>\$ 72,846,641</u>

The net pension liability was measured as of June 30, 2017 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2016 and update procedures were used to roll forward the total pension liability to the measurement date. The University's proportion of the net pension liability was based on actual contributions to the pension plan during the measurement period. At June 30, 2018, the University's proportion was 0.14 percent.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

For the year ended June 30, 2018, the University's actuarially calculated pension expense was \$(2,992,100). The University also recognized revenue of \$2,061,409 for support provided by the Commonwealth. At June 30, 2018, the University reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
<u>2018</u>		
Net difference between projected and actual earnings on investments	\$ -	\$ 313,654
Change in assumptions	5,019,090	2,814,238
Differences between expected and actual experience	233,734	857,357
Changes in proportion and differences between employer contributions and proportionate share of contributions	-	23,826,558
Contributions subsequent to the measurement date	<u>1,729,748</u>	<u>-</u>
	<u>\$ 6,982,572</u>	<u>\$ 27,811,807</u>

At June 30, 2018, the University reported \$1,729,748 as deferred outflows of resources related to pensions resulting from University contributions subsequent to the measurement date that will be recognized as a reduction of the net pension liability in the following fiscal year. Net deferred outflow (inflows) of resources at June 30, 2018, related to pensions will be recognized in pension expense as follows:

2019	\$ (7,369,801)
2020	(6,851,873)
2021	(6,059,024)
2022	<u>(2,278,285)</u>
	<u>\$ (22,558,983)</u>

Actuarial assumptions - The total pension liability was determined by actuarial valuations as of June 30, 2016 and update procedures were used to roll forward the total pension liability to the measurement date, using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.00%	
Salary Increases	3.50 – 7.30%, including inflation	
Investment Rate of Return	7.50%, net of pension plan investment expense, including inflation	

The rates of mortality for the period after service retirement are according to the RP-2000 Combined Mortality Table for Males and Females, as appropriate, with adjustments for mortality improvements based on a projection of Scale BB to 2025 with a set forward of 2 years for males and 1 year for females.

The actuarial assumptions used in the June 30, 2016 valuation were based on the results of an actuarial experience study for the period July 1, 2010 - June 30, 2015 adopted by the Board on November 19, 2016.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

The long-term expected return on plan was determined using a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The June 30, 2018 target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Nominal Rate of Return</u>
U.S. Equity	42.0%	4.4%
Non-U.S. Equity	20.0	5.3
Fixed Income	16.0	1.5
Additional Categories (Incl. Hedge Funds, High Yield And Non-U.S. Developed Bonds)	9.0	3.6
Real Estate	5.0	4.4
Private Equity	6.0	6.7
Cash	<u>2.0</u>	0.8
Total	<u>100%</u>	

Changes in Assumptions and Benefit Terms Since Prior Measurement Date - The total pension liability as of June 30, 2017 reflects that the assumed municipal bond index rate increased from 3.01% to 3.56%, resulting in a change in the Single Equivalent Interest Rate (SEIR) from 4.20% to 4.49%.

Changes Since Measurement Date - There were no changes between the measurement date of the collective net pension liability and the University reporting date that are expected to have a significant effect on the University's proportionate share of the collective net pension liability.

Discount rate - The discount rate used to measure the total pension liability at June 30, 2017 was 4.49%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rates and the Employer contributions will be made at statutorily required rates, and the additional amount appropriated for fiscal year 2018. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members until the 2038 plan year. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments through 2037 and a municipal bond index rate of 3.56% was applied to all periods of projected benefit payments after 2037. The SEIR that discounts the entire projected benefit stream to the same amount as the sum of the present values of the two separate benefit payments streams was used to determine the total pension liability.

The total pension liability as of June 30, 2017 reflects that the assumed municipal bond index rate increased from 3.01% to 3.56%, resulting in a change in the SEIR from 4.20% to 4.49%. The impact of this change in the discount rate is a change in assumptions that is added to the expected total pension liability to determine the final total pension liability as of June 30, 2017.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 8 – DEFINED BENEFIT PENSION PLANS (Continued)

Sensitivity of the University's proportionate share of the net pension liability to changes in the discount rate -
The following table presents the net pension liability of the University as of June 30, 2018, calculated using the discount rate of 4.49%, as well as what the University's net pension liability (in thousands) would be if it were calculated using a discount rate that is 1-percentage-point lower (3.49%) or 1-percentage-point higher (5.49%) than the current rate:

	1% Decrease <u>(3.49%)</u>	Current Discount Rate <u>(4.49%)</u>	1% Increase <u>(5.49%)</u>
Proportionate share of the Collective Net Pension Liability	\$ 50,250,685	\$ 40,538,352	\$ 32,567,126

Summary Pension Plan Information:

	KERS Hazardous/ <u>Non-hazardous</u>	<u>KTRS</u>	<u>Total</u>
<u>June 30, 2018</u>			
Net pension liability	\$ 32,855,260	\$ 40,538,352	\$ 73,393,612
Deferred outflows of resources	5,995,598	6,982,572	12,978,170
Deferred inflows of resources	2,777,651	27,811,807	30,589,458
Actuarially determined pension expense	2,847,115	(2,992,100)	(144,985)

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB)

In addition to the pension plans disclosed in Note 8, the University's employees participate in either the Kentucky Teachers Retirement System (KTRS) OPEB Plan or the Kentucky Employees Retirement System (KERS) OPEB Plan depending on the retirement plan in which they participate. Each OPEB plan is described in detail below.

Kentucky Employees Retirement System (KERS) OPEB Plan

OPEB Benefits Provided: The information below summarizes the major other postemployment retirement benefit provisions of KERS Non-Hazardous and Hazardous plans. It is not intended to be, nor should it be interpreted as, a complete statement of all benefit provisions:

Insurance Tier 1: Participation began before 7/1/2003

Benefit Eligibility: Recipient of a retirement allowance

Benefit: The percentage of member premiums paid by the retirement system are dependent on the number of years of service. Benefits also include duty disability retirements, duty death in service, non-duty death in service and surviving spouse of a retiree.

(Continued)

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Insurance Tier 2: Participation began on or after 7/1/2003, but before 9/1/2008

Benefit Eligibility: Recipient of a retirement allowance with at least 120 months of service at retirement

Benefit: The system provides a monthly contribution subsidy of \$10 (Non-hazardous) and \$15 (Hazardous) for each year of earned service. The monthly contribution is increased by 1.5% each July 1. Benefits also include duty disability retirements, duty death in service and non-duty death in service.

Insurance Tier 3: Participation began on or after 9/1/2008

Benefit Eligibility: Recipient of a retirement allowance with at least 180 months of service at retirement

Benefit: Tier 3 insurance benefits are identical to Tier 2, except Tier 3 members are required to have at least 180 months of service in order to be eligible.

Contributions: The University was required to contribute at an actuarially determined rate determined by Statute. Per Kentucky Revised Statute Section 78.545(33) normal contribution and past service contribution rates shall be determined by the KRS Board on the basis of an annual valuation last preceding July 1 of a new biennium. The KRS Board may amend contribution rates as of the first day of July of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial bases adopted by the KRS Board.

For the fiscal year ended June 30, 2018, participating employers in the non-hazardous plan contributed 49.47% (41.06% allocated to pension and 8.41% allocated to OPEB) as set by KRS of each non-hazardous employee's creditable compensation. For the fiscal year ended June 30, 2018, participating employers in the Hazardous plan contributed 23.70% (21.44% allocated to pension and 2.26% allocated to OPEB) as set by KRS of each Hazardous employee's creditable compensation. These percentages are inclusive of both pension and insurance payments for employers. Administrative costs of KRS are financed through employer contributions and investment earnings.

The University has met 100% of the contribution funding requirement for the fiscal years ended June 30, 2018. Total current year contributions recognized by the Plan were \$1,845,787 (\$1,531,999 related to pension and \$313,788 related to OPEB) for the year ended June 30, 2018. The OPEB contributions amount does not include the implicit subsidy reported in the amount of \$48,179.

Members whose participation began before 9/1/2008:

Nonhazardous contributions equal 5% and Hazardous contributions equal 8% of all creditable compensation. Interest paid on the members' accounts is currently 2.5%; and per statute shall not be less than 2.0%. Member entitled to a full refund of contributions with interest.

Members whose participation began on or after 9/1/2008:

Nonhazardous contributions equal to 6% and Hazardous contributions equal 9% of all creditable compensation, with 5% (Non-hazardous) and 8% (Hazardous) being credited to the member's account and 1% deposited to the KRS 401(h) Account. Interest paid on the members' accounts will be set at 2.5%. Member is entitled to a full refund of contributions and interest in their individual account, however, the 1% contributed to the insurance fund is non-refundable.

(Continued)

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Members whose participation on or after 1/1/2014:

Nonhazardous contributions equal to 6% and Hazardous contributions equal 9% of all creditable compensation, with 5% (Non-hazardous) and 8% (Hazardous) being credited to the member's account and 1% deposited to the KRS 401(h) Account. Interest paid on the members' accounts will be set at 2.5%. Member is entitled to a full refund of contributions and interest in their individual account, however, the 1% contributed to the insurance fund is non-refundable.

Nonhazardous contributions equal to 6% and Hazardous contributions equal 9% of all creditable compensation, with 5% (Non-hazardous) and 8% (Hazardous) being credited to the member's account and 1% deposited to the KRS 401(h) Account. Interest paid on the members' accounts will be set at 2.5%. Member is entitled to a full refund of contributions and interest in their individual account, however, the 1% contributed to the insurance fund is non-refundable.

Total OPEB Liability: The total other postemployment benefits plan ("OPEB") was determined by an actuarial valuation as of June 30, 2017, using the following actuarial assumptions, applied to all periods included in the measurement:

Price inflation	2.30 percent
Payroll growth rate	0.0 percent for KERS non-hazardous
Salary increases	3.05 percent, average
Investment rate of return	6.25 percent
Healthcare trend rates	
Pre-65	Initial trend starting at 7.25 percent at January 1, 2019 and gradually decreasing to an ultimate trend rate of 4.05 percent over a period of 13 years.
Post-65	Initial trend starting at 5.10 percent at January 1, 2019 and gradually decreasing to an ultimate trend rate of 4.05 percent over a period of 11 years.

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiplied by 50% for males and 30% for females). For healthy retired members and beneficiaries, the mortality table used is the RP-2000 Combined Mortality Table projected with Scale BB to 2013 (set back 1 year for females). For disabled members, the RP-2000 Combined Disabled Mortality Table projected with Scale BB to 2013 (set back 4 years for males) is used for the period after disability retirement. There is some margin in the current mortality tables for possible future improvement in mortality rates and that margin will be reviewed again when the next experience investigation is conducted. The actuarial assumptions used in the June 30, 2017 valuation were based on the results of an actuarial experience study for the period July 1, 2008 – June 30, 2013.

Discount rate assumptions:

- (a) **Discount Rate:** The discount rate used to measure the total Non-hazardous OPEB liability was 5.83%, which was reduced from the 6.90% discount rate used in the prior year. The discount rate used to measure the total Hazardous OPEB liability was 5.87%, which was reduced from the 7.20% discount rate used in the prior year.

(Continued)

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

- (b) **Projected Cash Flows:** The projection of cash flows used to determine the discount rate assumed the local employers and plan members would contribute the actuarially determined contribution rate of projected compensation over the remaining 26-year amortization period of the unfunded actuarial accrued liability.
- (c) **Long-Term Rate of Return:** The long-term expected return on plan assets is reviewed as part of the regular experience studies prepared every five years for the System. The most recent analysis, performed for the period covering fiscal years 2008 through 2013 is outlined in a report dated April 30, 2014. However, the Board of KRS has the authority to review the assumptions on a more frequent basis and adopt new assumptions prior to the next scheduled experience study. The long-term expected rate of return was determined by using a building-block method in which best-estimate ranges of expected future real rate of returns are developed for each asset class. The ranges are combined by weighting the expected future real rate of return by the target asset allocation percentage.
- (d) **Municipal Bond Rate:** The discount rate determination used a municipal bond rate of 3.56% as reported in Fidelity Index's "20 – Year Municipal GO AA Index" as of June 30, 2017.
- (e) **Period of Projected Benefit Payments:** Current assets, future contributions, and investment earnings are projected to be sufficient to pay the projected benefit payments from the retirement system. However, the cost associated with the implicit employer subsidy is not currently being included in the calculation of the system's actuarial determined contributions, and it is the actuary's understanding that any cost associated with the implicit subsidy will not be paid out of the system's trust. Therefore, the municipal bond rate was applied to future expected benefit payments associated with the implicit subsidy.
- (f) **Assumed Asset Allocations:** The target asset allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
US Equity	17.50%	5.97%
International Equity	17.50%	7.85%
Global Bonds	4.00%	2.63%
Global Credit	2.00%	3.63%
High Yield	7.00%	5.75%
Emerging Market Debt	5.00%	5.50%
Private Credit	10.00%	8.75%
Real Estate	5.00%	7.63%
Absolute Return	10.00%	5.63%
Real Return	10.00%	6.13%
Private Equity	10.00%	8.25%
Cash	<u>2.00%</u>	<u>1.88%</u>
Total	<u>100.00%</u>	<u>6.56%</u>

The long-term expected rate of return on pension plan assets was established by the KRS Board of Trustees at 6.25% based on a blending of the factors described above.

(Continued)

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

- (g) **Sensitivity Analysis:** This paragraph requires disclosure of the sensitivity of the net OPEB liability to changes in the discount rate and changes in the healthcare cost trend rate.

Non-hazardous

The following presents the University's allocated portion of the Non-hazardous net OPEB liability of the System, calculated using the discount rate of 5.83% percent, as well as what the University's allocated portion of the System's net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (4.83 percent) or 1-percentage-point higher (6.83 percent) than the current rate for Non-hazardous:

	<u>1% Decrease</u> <u>(4.83%)</u>	<u>Current</u> <u>Discount Rate</u> <u>(5.83%)</u>	<u>1% Increase</u> <u>(6.83%)</u>
The University's Net OPEB liability – Non-hazardous	\$ 7,223,284	\$ 6,178,390	\$ 5,310,018

The following presents the University's allocated portion of the Non-hazardous net OPEB liability of the System, calculated using the healthcare cost trend rate of percent, as well as what the University's allocated portion of the System's net OPEB liability would be if it were calculated using a healthcare cost trend rate that is 1-percentage-point lower or 1-percentage-point higher than the current rate for Non-hazardous:

	<u>1% Decrease</u>	<u>Current Healthcare</u> <u>Cost Trend Rate</u>	<u>1% Increase</u>
The University's Net OPEB liability – Non-hazardous	\$ 5,249,63	\$ 6,178,390	\$7,344,612

Hazardous

The following presents The University's allocated portion of the Hazardous net OPEB liability of the System, calculated using the discount rate of 5.87% percent, as well as what the University's allocated portion of the System's net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (4.87 percent) or 1-percentage-point higher (6.87 percent) than the current rate for Hazardous:

	<u>1% Decrease</u> <u>(4.87%)</u>	<u>Current</u> <u>Discount Rate</u> <u>(5.87%)</u>	<u>1% Increase</u> <u>(6.87%)</u>
The University's Net OPEB liability – Hazardous	\$ 35,037	\$ 2,877	\$ (23,473)

The following presents the University's allocated portion of the Hazardous net OPEB liability of the System, calculated using the healthcare cost trend rate of percent, as well as what the University's allocated portion of the System's net OPEB liability would be if it were calculated using a healthcare cost trend rate that is 1-percentage-point lower or 1-percentage-point higher than the current rate for Hazardous:

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

	<u>1% Decrease</u>	<u>Current Healthcare Cost Trend Rate</u>	<u>1% Increase</u>
The University's Net OPEB liability – Hazardous	\$ (23,721)	\$ 2,877	\$ 35,894

Employer's Portion of the Collective OPEB Liability: The University's proportionate share of the Non-hazardous net OPEB liability, as indicated in the prior table, is \$6,178,390, or approximately 0.243631%. The University's proportionate share of the Hazardous net OPEB liability, as indicated in the prior table, is \$2,877, or approximately 0.047701%. The net pension liabilities were distributed based on 2017 actual employer contributions to the plan.

Measurement Date: June 30, 2017 is the actuarial valuation date and measurement date upon which the total pension liability is based.

Changes in Assumptions and Benefit Terms: Since the prior measurement date, the demographic and economic assumptions that affect the measurement of the total OPEB liability have been updated as follows:

- The assumed investment rate of return was decreased from 6.75% to 5.25% (Non-hazardous) and 7.50% to 6.25% (Hazardous).
- The assumed rate of inflation was reduced from 3.25% to 2.30%.
- Payroll growth assumption was reduced from 4.00% to 3.05%.

Changes Since Measurement Date: There were no changes between the measurement date of the collective net OPEB liability and the employer's reporting date.

OPEB Expense: The University was allocated pension expense of \$612,902 related to the KERS Non-Hazardous and \$5,128 related to the KERS Hazardous for the year ending June 30, 2018.

Deferred Outflows and Deferred Inflows: Since certain expense items are amortized over closed periods each year, the deferred portions of these items must be tracked annually. If the amounts serve to reduce OPEB expense they are labeled as deferred inflows. If they will increase OPEB expense they are labeled deferred outflows. The amortization of these amounts is accomplished on a level dollar basis, with no interest included in the deferred amounts. Experience gains/losses and the impact of changes in actuarial assumptions, if any, are amortized over the average remaining service life of the active and inactive System members at the beginning of the fiscal year. Investment gains and losses are amortized over a fixed five-year period. Deferred inflows and outflows as of the Measurement Date include:

Non-hazardous	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference between expected and actual experience	\$ -	\$ 7,646
Change of assumptions	808,938	-
Changes in proportion and differences between employer contributions and proportionate shares of contributions	-	45,341
Differences between expected and actual investment earning on plan investments	-	79,967
	808,938	132,954
Contributions subsequent to the measurement date	349,447	-
Total	\$ 1,158,385	\$ 132,954

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Deferred outflows of resources resulting from employer contributions subsequent to the measurement date of \$301,336, which include the implicit subsidy reported of \$48,111, will be recognized as a reduction of net OPEB liability in the year ending June 30, 2019. The remainder of the deferred outflows and deferred inflows of resources are amortized over three to five years with remaining amortization as follows:

Year ending June 30:	
2018	\$ 168,525
2019	168,525
2020	168,525
2021	168,525
2022	1,885

Hazardous

	Deferred Outflows <u>of Resources</u>	Deferred Inflows <u>of Resources</u>
Difference between expected and actual experience	\$ -	\$ 413
Change of assumptions	35,865	-
Changes in proportion and differences between employer contributions and proportionate share of plan contributions	-	428
Differences between expected and actual investment earning on plan investments	-	10,302
	<u>35,865</u>	<u>11,143</u>
Contributions subsequent to the measurement date	12,520	-
Total	<u>\$ 48,385</u>	<u>\$ 11,143</u>

Deferred outflows of resources resulting from employer contributions subsequent to the measurement date of \$12,452, which include the implicit subsidy reported of \$68, will be recognized as a reduction of net OPEB liability in the year ending June 30, 2019. The remainder of the deferred outflows and deferred inflows of resources are amortized over three to five years with remaining amortization as follows:

Year ending June 30:	
2018	\$ 4,045
2019	4,045
2020	4,045
2021	4,045
2022	6,621
Thereafter	1,921

OPEB Plan Fiduciary Net Position: Detailed information about the KERS OPEB plans' fiduciary net position is available in the separately issued OPEB plan financial reports.

(Continued)

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Kentucky Teachers' Retirement System

Medical Insurance Plan

Plan Description - In addition to the pension benefits previously described, Kentucky Revised Statute 161.675 requires KTRS to provide post-employment healthcare benefits to eligible members and dependents. The KTRS Medical Insurance benefit is a cost-sharing multiple employer defined benefit plan. Changes made to the medical plan may be made by the KTRS Board of Trustees, the Kentucky Department of Employee Insurance and the General Assembly.

Benefits Provided - To be eligible for medical benefits, the member must have retired either for service or disability. The KTRS Medical Insurance Fund offers coverage to members under the age of 65 through the Kentucky Employees Health Plan administered by the Kentucky Department of Employee Insurance. KTRS retired members are given a supplement to be used for payment of their health insurance premium. The amount of the member's supplement is based on a contribution supplement table approved by the KTRS Board of Trustees. The retired member pays premiums in excess of the monthly supplement. Once retired members and eligible spouses attain age 65 and are Medicare eligible, coverage is obtained through the KTRS Medicare Eligible Health Plan.

Contributions - In order to fund the post-retirement healthcare benefit, seven and one-half percent (7.50%) of the gross annual payroll of members is contributed. Three percent (3.75%) is paid by member contributions and three quarters percent (0.75%) from state appropriation and three percent (3.00%) from the employer. The state contributes the net cost of health insurance premiums for members who retired on or after July 1, 2010 who are in the non-Medicare eligible group. Also, the premiums collected from retirees as described in the plan description and investment interest help meet the medical expenses of the plan.

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows

of Resources Related to OPEBs - At June 30, 2018, the University reported a liability of \$5,799,000 for its proportionate share of the collective net OPEB liability that reflected a reduction for state OPEB support provided to the University. The collective net OPEB liability was measured as of June 30, 2017, and the total OPEB liability used to calculate the collective net OPEB liability was based on a projection of the University's long-term share of contributions to the OPEB plan relative to the projected contributions of all participating employers, actuarially determined. At June 30, 2017, the University's proportion was 0.162629%.

The amount recognized by the University as its proportionate share of the OPEB liability, the related State support, and the total portion of the net OPEB liability that was associated with the University were as follows:

University's proportionate share of the net OPEB liability	\$ 5,799,000
State's proportionate share of the net OPEB liability associated with the University	<u>2,630,000</u>
Total	<u>\$ 8,429,000</u>

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

For the year ended June 30, 2018, the University recognized OPEB expense of \$377,000 and revenue of \$171,000 for support provided by the State. At June 30, 2018, the University reported deferred outflows of resources and deferred inflows of resources related to OPEBs from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Net difference between projected and actual earnings on OPEB plan investments	\$ -	\$ 60,000
University's contributions subsequent to the measurement date	<u>283,192</u>	<u>-</u>
Total	<u>\$ 283,192</u>	<u>\$ 60,000</u>

Of the total amount reported as deferred outflows of resources related to OPEB, \$283,192 resulting from University contributions subsequent to the measurement date and before the end of the fiscal year will be included as a reduction of the collective net OPEB liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in the University's OPEB expense as follows:

Year ended June 30:	
2019	\$ (15,000)
2020	(15,000)
2021	(15,000)
2022	(15,000)

Actuarial Assumptions - The total OPEB liability in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Investment rate of return	8.00%, net of OPEB plan investment expense, including inflation.
Projected salary increases	3.50 – 7.20%, including inflation
Inflation rate	3.00%
Real Wage Growth	0.50%
Wage Inflation	3.50%
Healthcare cost trend rates	
Under 65	7.75% for FY 2017 decreasing to an ultimate rate of 5.00% by FY 2023
Ages 65 and Older	5.75% for FY 2017 decreasing to an ultimate rate of 5.00% by FY 2020
Medicare Part B Premiums	1.02% for FY 2017 with an ultimate rate of 5.00% by 2029
Municipal Bond Index Rate	3.56%
Discount Rate	8.00%
Single Equivalent Interest Rate	8.00%, net of OPEB plan investment expense, including inflation.

(Continued)

KENTUCKY STATE UNIVERSITY
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Mortality rates were based on the RP-2000 Combined Mortality Table projected to 2025 with projection scale BB and set forward two years for males and one year for females is used for the period after service retirement and for dependent beneficiaries. The RP-2000 Disabled Mortality Table set forward two years for males and seven years for females is used for the period after disability retirement.

The remaining actuarial assumptions (e.g. initial per capita costs, health care cost trends, rate of plan participation, rates of plan election, etc.) used in the June 30, 2017 valuation were based on a review of recent plan experience done concurrently with the June 30, 2017 valuation.

The long-term expected rate of return on OPEB plan investments was determined using a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of OPEB plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

The target allocation and best estimates of arithmetic real rates of return for each major asset class, as provided by TRS's investment consultant, are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Nominal Rate of Return</u>
Global Equity	60.0%	5.1%
Fixed Income	9.0	1.2
Real Estate	4.5	4.0
Private Equity	5.5	6.6
High Yield	10.0	4.3
Other Additional Categories*	10.0	3.3
Cash (LIBOR)	<u>1.0</u>	0.4
Total	<u><u>100%</u></u>	

*Modeled as 50% High Yield and 50% Bank Loans.

Discount Rate - The discount rate used to measure the total OPEB liability was 8.00%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rates and the employer contributions will be made at statutorily required rates. Based on those assumptions, the OPEB plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Sensitivity of the University's proportionate share of the net OPEB liability to changes in the discount rate The following table presents the University's proportionate share of the collective net OPEB liability of the System, calculated using the discount rate of 8.00%, as well as what the University's proportionate share of the collective net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7.00%) or 1-percentage-point higher (9.00%) than the current rate:

	1% Decrease <u>(7.00%)</u>	Current Discount Rate <u>(8.00%)</u>	1% Increase <u>(9.00%)</u>
University's net OPEB liability (MI)	\$ 6,752,000	\$ 5,799,000	\$ 5,004,000

Sensitivity of the University's proportionate share of the collective net OPEB liability to changes in the healthcare cost trend rates – The following presents the University's proportionate share of the collective net OPEB liability, as well as what the University's proportionate share of the collective net OPEB liability would be if it were calculated using healthcare cost trend rates that were 1-percentage-point lower or 1-percentage-point higher than the current healthcare cost trend rates:

	1% <u>Decrease</u>	Current Trend Rate	1% <u>Increase</u>
University's net OPEB liability (MI)	\$ 4,856,000	\$ 5,799,000	\$ 6,961,000

OPEB Plan Fiduciary Net Position – Detailed information about the OPEB plan's fiduciary net position is available in the separately issued TRS financial report.

Changes of benefit terms – With the passage of House Bill 471, the eligibility for non-single subsidies (NSS) for the KEHP-participating members who retired prior to July 1, 2010 is restored, but the state will only finance, via its KEHP "Shared Responsibility" contributions, the costs of the NSS related to those KEHP-participating members who retired on or after July 1, 2010.

Methods and assumptions used in the actuarially determined contributions – The actuarially determined contribution rates, as a percentage of payroll, used to determine the actuarially determined contribution amounts in the Schedule of Employer Contributions are calculated as of the indicated valuation date. The following actuarial methods and assumptions (from the indicated actuarial valuations) were used to determine contribution rates reported in that schedule for the year ending June 30, 2018:

Valuation date	June 30, 2016
Actuarial cost method	Entry Age Normal
Amortization method	Level Percent of Payroll
Amortization period	30 years, Open
Asset valuation method	Five-year smoothed value
Inflation	3.00%
Real wage growth	0.50%
Wage inflation	3.50%
Salary increases, including wage inflation	3.50% - 7.20%
Discount rate	8.00%
Health care cost trends	
Under 65	7.75% for FY 2017 decreasing to an ultimate rate of 5.00% by FY 2023

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Ages 65 and older	5.75% for FY 2017 decreasing to an ultimate rate of 5.00% by FY 2020
Medicare Part B premiums	1.02% for FY 2017 with an ultimate rate of 5.00% by 2029
Under age 65 claims	the current premium charged by KEHP is used as the base cost and is projected forward using only the health care trend assumption (no implicit rate subsidy is recognized).

Life Insurance Plan

Plan Description – Life Insurance Plan – KTRS administers the life insurance plan as provided by Kentucky Revised Statute 161.655 to eligible active and retired members. The KTRS Life Insurance benefit is a cost-sharing multiple employer defined benefit plan. Changes made to the life insurance plan may be made by the KTRS Board of Trustees and the General Assembly.

Benefits Provided – KTRS provides a life insurance benefit of five thousand dollars payable for members who retire based on service or disability. KTRS provides a life insurance benefit of two thousand dollars payable for its active contributing members. The life insurance benefit is payable upon the death of the member to the member’s estate or to a party designated by the member.

Contributions – In order to fund the post-retirement life insurance benefit, three hundredths of one percent (0.03%) of the gross annual payroll of members is contributed by the state.

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEBs: At June 30, 2018, the University reported a liability of \$81,000 for its proportionate share of the collective net OPEB liability that reflected a reduction for state OPEB support provided to the University. The collective net OPEB liability was measured as of June 30, 2017, and the total OPEB liability used to calculate the collective net OPEB liability was based on a projection of the University’s long-term share of contributions to the OPEB plan relative to the projected contributions of all participating employers, actuarially determined. At June 30, 2017, the University’s proportion was 0.369048%.

For the year ended June 30, 2018, the University recognized OPEB expense of \$12,000. At June 30, 2018, the University reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Net difference between projected and actual earnings on OPEB plan investments	\$ 17,000	\$ -
University’s contributions subsequent to the measurement date	<u>3,832</u>	<u>-</u>
Total	<u>\$ 20,832</u>	<u>\$ -</u>

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

Of the total amount reported as deferred outflows of resources related to OPEB, \$3,832 resulting from University contributions subsequent to the measurement date and before the end of the fiscal year will be included as a reduction of the collective net OPEB liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in the University's OPEB expense as follows:

Year ended June 30:		\$	
2019			4,000
2020			4,000
2021			4,000
2022			5,000

Actuarial Assumptions – The total OPEB liability in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Investment rate of return	7.50%, net of OPEB plan investment expense, including inflation.
Projected salary increases	3.50 – 7.20%, including inflation
Inflation rate	3.00%
Real Wage Growth	0.50%
Wage Inflation	3.50%
Municipal Bond Index Rate	3.56%
Discount Rate	7.50%
Single Equivalent Interest Rate	7.50%, net of OPEB plan investment expense, including inflation.

Mortality rates were based on the RP-2000 Combined Mortality Table projected to 2025 with projection scale BB and set forward two years for males and one year for females is used for the period after service retirement and for dependent beneficiaries. The RP-2000 Disabled Mortality Table set forward two years for males and seven years for females is used for the period after disability retirement.

The remaining actuarial assumptions (e.g. initial per capita costs, rate of plan participation, rates of plan election, etc.) used in the June 30, 2017 valuation were based on a review of recent plan experience done concurrently with the June 30, 2017 valuation.

The long-term expected rate of return on OPEB plan investments was determined using a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of OPEB plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

The target allocation and best estimates of arithmetic real rates of return for each major asset class, as provided by TRS's investment consultant, are summarized in the following table:

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 9 - OTHER POSTEMPLOYMENT BENEFITS PLANS (OPEB) (Continued)

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Nominal Rate of Return</u>
U.S. Large Cap Equity	38.4%	4.3%
U.S. Small Cap Equity	2.6	4.8
Developed International Equity	15.8	5.2
Emerging Markets Equity	4.2	5.4
Fixed Income – Inv. Grade	16.0	1.2
Real Estate	6.0	4.0
Private Equity	7.0	6.6
High Yield	2.0	4.3
Other Additional Categories**	7.0	3.3
Cash (LIBOR)	<u>1.0</u>	0.5
 Total	 <u>100%</u>	

* As the LIF investment policy is to change, the above reflects the pension allocation and returns that achieve the target 7.5% long-term rate of return.

** Modeled as 50% High Yield and 50% Bank Loans.

Discount rate - The discount rate used to measure the total OPEB liability for life insurance was 7.50%. The projection of cash flows used to determine the discount rate assumed that the employer contributions will be made at statutorily required rates. Based on those assumptions, the OPEB plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on OPEB plan investments was applied to all periods of projected benefit payments to determine the total OPEB liability.

Sensitivity of the University's proportionate share of the net OPEB liability to changes in the discount rate - The following table presents the University's proportionate share of the collective net OPEB liability of the System, calculated using the discount rate of 7.50%, as well as what the University's proportionate share of the collective net OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50%) or 1-percentage-point higher (8.50%) than the current rate:

	1% Decrease <u>(6.50%)</u>	Current Discount Rate <u>(7.50%)</u>	1% Increase <u>(8.50%)</u>
University's net OPEB (LI) liability	\$ 135,000	\$ 81,000	\$ 37,000

OPEB plan fiduciary net position – Detailed information about the KTRS OPEB plans' fiduciary net position is available in the separately issued KTRS financial report.

Summary OPEB Information:

	<u>KERS</u>	<u>KTRS</u>	<u>Total</u>
June 30, 2018			
Net OPEB liability	\$ 6,181,267	\$ 5,880,000	\$ 12,061,267
Deferred outflows of resources	1,206,770	304,024	1,510,794
Deferred inflows of resources	144,097	60,000	204,097
Actuarially determined pension expense	618,030	389,000	1,007,030

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 10 - COMMITMENTS AND CONTINGENCIES

The University is a party to various lawsuits 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 statements of the University.

The University receives financial assistance from federal and state agencies in the form of grants and awards. The expenditure of funds received from these programs generally requires compliance with terms and conditions specified in the grant agreements and are subject to audit by the grantor agencies. Any disallowed claims resulting from such audit could become a liability of the applicable fund.

NOTE 11 - RISK MANAGEMENT

The University is exposed to various risks of loss from torts; theft of, damage to, destruction of assets; business interruption; employee injuries and illnesses; natural disasters; and employee health and accident benefits. Commercial insurance coverage is purchased for claims arising from these risks. Settled claims have not exceeded this commercial coverage in any of the three preceding years. As a sovereign entity of the Commonwealth of Kentucky, the Kentucky Board of Claims handles tort claims on behalf of the University.

NOTE 12 - SCHEDULE OF EXPENSES BY PROGRAM

In the Statement of Revenues, Expenses and Changes in Net Position, operating expenses are presented by functional expense purpose. Depreciation is allocated below based on functional classification as required by IPEDS for Fiscal Year 2018. Functional expense purpose is classified by natural classification as follows:

	Compensation and Benefits	Supplies and Services	Scholarships and Fellowships	Depreciation	Operations Maintenance	Total
Instruction	\$ 8,539,997	\$ 1,081,638	\$ -	\$ 838,237	\$ 937,501	\$ 11,397,373
Research	5,269,187	2,792,072	-	1,151,000	825,679	10,037,938
Public service	5,582,327	3,779,440	-	506,494	884,476	10,752,737
Academic support	1,042,013	379,742	-	192,626	144,694	1,759,075
Student services	4,107,648	2,223,957	-	588,539	620,241	7,540,385
Institutional support	6,844,384	5,050,985	-	866,779	1,143,850	13,905,998
Operation & maintenance of plant	1,225,026	3,518,443	-	849,601	(5,593,070)	-
Auxiliary enterprises	585,940	4,707,027	-	401,833	510,415	6,205,215
Student financial aid	<u>253,906</u>	<u>11,870</u>	<u>5,555,850</u>	<u>49,438</u>	<u>526,214</u>	<u>6,397,278</u>
Total operating expense	<u>\$ 33,450,428</u>	<u>\$ 23,545,174</u>	<u>\$ 5,555,850</u>	<u>\$ 5,444,547</u>	<u>\$ -</u>	<u>\$ 67,995,999</u>

(Continued)

NOTE 13 – KENTUCKY STATE UNIVERSITY FOUNDATION, INC.

Description of the Organization

Kentucky State University Foundation, Inc. (the Foundation) is a Kentucky not-for-profit corporation formed to receive, invest and expend funds to promote and implement educational and developmental activities at Kentucky State University (the University). The Foundation is managed by a Board of Trustees independent from that of the University. The Foundation is supported primarily through contributions from alumni.

Summary of Significant Accounting Policies

Use of Estimates: The 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 the preparation of its financial statements.

Basis of Presentation: Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Foundation are classified and reported as follows:

Unrestricted net assets - Net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets - Net assets subject to donor-imposed stipulations that will be met by actions of the Foundation, pursuant to those stipulations or that expire by the passage of time. Assets released from restrictions during 2018 primarily relate to scholarships and University and student support.

Permanently restricted net assets - Net assets subject to donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or removed by actions of the Foundation pursuant to those stipulations. Permanently restricted net assets consist of assets from which the income can be used toward University scholarships and Foundation operations.

Cash and Cash Equivalents: The Foundation considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents. The Foundation has a concentration of credit risk in that it periodically maintains bank accounts which, at times, may exceed the coverage provided by the Federal Deposit Insurance Corporation (FDIC). The Foundation has not experienced any losses on such amounts. The Foundation believes it is not exposed to any significant credit risk on cash.

Investments: Investments are stated at fair value based on closing market quotations for such securities or similar securities.

Property and Equipment: Property and equipment is recorded at cost if purchased or fair market value at date of contribution if contributed. If the donors stipulate how long the assets must be used, the contributions of property and equipment are recorded as restricted support. In the absence of such stipulations, these contributions are recorded as unrestricted support. Depreciation is computed on a straight-line basis over the estimated useful lives of the respective assets.

(Continued)

NOTE 13 – KENTUCKY STATE UNIVERSITY FOUNDATION, INC. (Continued)

Summary of Significant Accounting Policies (Continued)

Revenue Recognition: Contributions are generally recognized when received. However, pledges are recognized when the donor makes a promise to give to the Foundation that is, in substance, unconditional. Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restrictions expire in the fiscal year in which the contributions are recognized. All other donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Income Taxes: Kentucky State University Foundation, Inc., a not-for-profit organization operating under Section 501(c)(3) of the Internal Revenue Code, is generally exempt from federal, state and local income taxes. The Foundation's management does not believe the Foundation has any unrelated business income. Accordingly, no provision for income taxes is recorded in the financial statements.

Recent Accounting Pronouncements: In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2017-14, Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities, that changes how a not-for-profit organization classifies its net assets, as well as the information it presents in the financial statements and notes about its liquidity, financial performance, and cash flows. The ASU includes a reduction in the number of net asset categories from three to two, conforming requirements on releases of capital restrictions, several new requirements related to expense presentation and disclosure (including investment expenses), and new required disclosures communicating information useful in assessing liquidity. This ASU will be effective for the Foundation for fiscal years beginning after December 15, 2017. Early adoption is permitted. The Foundation is currently evaluating the effects adoption of this guidance will have on the financial statements.

Subsequent Events: The Foundation's management has evaluated subsequent events for accounting and disclosure requirements through September 24, 2018, the date the financial statements were available to be issued. There were no events occurring during the evaluation period that require recognition or disclosure in the financial statements.

Investments

Investments as of June 30, 2018 are summarized as follows:

Equity securities	\$ 6,272,340
Debt securities	2,680,103
U.S. government securities	<u>432,873</u>
Total investments	<u>\$ 9,385,316</u>

(Continued)

NOTE 13 – KENTUCKY STATE UNIVERSITY FOUNDATION, INC. (Continued)

Fair Value Measurements

The Foundation classifies its investments based on a hierarchy consisting of: Level 1 (valued using quoted prices from active markets for identical assets), Level 2 (not traded on an active market but for which observable market inputs are readily available), and Level 3 (valued based on significant unobservable inputs). The investment'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.

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used as of June 30, 2018.

Common stocks, municipal bonds, corporate bonds, U.S. government securities, and equity exchange traded funds: Valued at the closing price reported on the active market on which the individual securities are traded. Some level 2 inputs are used for pricing of municipal and corporate bonds; therefore, they are all classified as level 2.

Mutual funds: Valued at the daily closing price as reported by the fund. Mutual funds held by the Foundation are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value (NAV) and to transact at that price. The mutual funds held by the Foundation are deemed to be actively traded.

Real estate investment trust: Valued at the NAV of shares held by the Foundation at year end.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Foundation believes its valuation methods are appropriate and consistent with those of other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Fair value measurements as of June 30, 2018 are as follows:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Common stocks	\$ 3,792,259	\$ -	\$ -	\$ 3,792,259
Mutual funds	2,276,686	-	-	2,276,686
Municipal bonds	-	259,760	-	259,760
Corporate bonds	-	2,420,343	-	2,420,343
U.S government securities	432,873	-	-	432,873
Equity exchange traded funds	<u>203,395</u>	<u>-</u>	<u>-</u>	<u>203,395</u>
Total	<u>\$ 6,705,213</u>	<u>\$ 2,680,103</u>	<u>\$ -</u>	<u>\$ 9,385,316</u>

(Continued)

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 13 – KENTUCKY STATE UNIVERSITY FOUNDATION, INC. (Continued)

Temporarily Restricted Net Assets

For the year ended June 30, 2018, net assets were released from donor restrictions by incurring expenses satisfying the purpose of the restrictions specified by donors as follows:

Endowment spending allocation	\$ 676,590
University support	116,122
Scholarships	120,107
Operating and other expenses	57,265
Student support	127,275
Personal services	18,864
Travel and other expenses	<u>55,936</u>
Total release from restrictions	<u>\$ 1,172,159</u>

Retirement Plan

The Foundation has a defined contribution profit sharing plan which covers all employees who meet certain requirements. Foundation contributions are discretionary. No contributions were made for the year ended June 30, 2018.

Endowment Composition

On July 15, 2010, The Commonwealth of Kentucky adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The Foundation follows UPMIFA and its own governing documents. The Foundation has interpreted UPMIFA as requiring the preservation of the corpus of the donor-restricted endowment funds absent explicit donor stipulations to the contrary, and other amounts as deemed necessary by the board. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment, (2) the original value of subsequent gifts to the permanent endowment, and (3) accumulations to permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The Foundation has determined that the balance of its endowments includes funds that require that the income and net appreciation be restricted to certain uses for the benefit of participants.

Upon review, the Foundation has determined that appropriate expenditures have been made to meet all donor restrictions regarding balances recorded in the endowment fund.

Spending Policy: The Foundation spending policy is to distribute an amount at least equal to 3-5% of a moving sixteen quarter average of the fair value of the endowment funds. Accordingly, over the long term, the Foundation expects its spending policy to allow its endowment assets to grow at an average rate of 3% annually. This is consistent with the Foundation's objective to maintain the purchasing power of endowment assets as well as to provide additional real growth through investment return.

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level the donor requires the Foundation to retain as a fund of perpetual duration. There were no such deficiencies as of June 30, 2018.

KENTUCKY STATE UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
June 30, 2018

NOTE 13 – KENTUCKY STATE UNIVERSITY FOUNDATION, INC. (Continued)

Endowment Composition (Continued)

Endowment net asset composition by type of fund as of June 30, 2018 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ <u>-</u>	\$ <u>3,788,318</u>	\$ <u>3,794,106</u>	\$ <u>7,582,424</u>

Changes in endowment net assets as of June 30, 2018 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets, beginning of year	\$ -	\$ 3,981,609	\$ 3,711,724	\$ 7,693,333
Contributions	-	-	78,882	78,882
Interest and dividends	-	186,272	-	186,272
Realized and unrealized gains	-	297,027	-	297,027
Amounts appropriated for expenditure	-	(676,590)	-	(676,590)
Reclassifications	<u>-</u>	<u>-</u>	<u>3,500</u>	<u>3,500</u>
Endowment net assets, end of year	\$ <u>-</u>	\$ <u>3,788,318</u>	\$ <u>3,794,106</u>	\$ <u>7,582,424</u>

REQUIRED SUPPLEMENTARY INFORMATION

KENTUCKY STATE UNIVERSITY
SCHEDULE OF THE UNIVERSITY'S (KSU)
PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
KENTUCKY EMPLOYEES' RETIREMENT SYSTEM
June 30, 2018
(Amounts in thousands)

<u>Non-hazardous</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
KSU's proportion of the net pension liability	\$ 32,618	\$ 29,146	\$ 29,408	\$ 28,555
KSU's proportionate share of the net pension liability	0.24%	0.26%	0.29%	0.32%
KSU's covered payroll	\$ 3,888	\$ 4,321	\$ 5,390	\$ 5,453
KSU's proportionate share of the net pension liability as a share of its covered payroll	838.94%	674.52%	545.60%	523.66%
Plan fiduciary net position as a percentage of total pension liability	13.30%	14.80%	18.83%	22.32%
<u>Hazardous</u>	<u>2018</u>			
KSU's proportion of the net pension liability	\$ 237			
KSU's proportionate share of the net pension liability	0.05%			
KSU's covered payroll	\$ 79			
KSU's proportionate share of the net pension liability as a share of its covered payroll	300.00%			
Plan fiduciary net position as a percentage of total pension liability	54.80%			

Changes in Assumptions: For fiscal year 2017, the demographic and economic assumptions that affect the measurement of the total pension liability have been updated as follows:

- The assumed investment rate of return was decreased from 6.75% to 5.25% (Non-hazardous) and 7.50% to 6.25% (Hazardous).
- The assumed rate of inflation was reduced from 3.25% to 2.30%.
- Payroll growth assumption was reduced from 4.00% to 3.05%.

Note: This table represents data that is one year in arrears.

KENTUCKY STATE UNIVERSITY
 SCHEDULE OF THE UNIVERSITY'S CONTRIBUTION
 KENTUCKY EMPLOYEES' RETIREMENT SYSTEM
 June 30, 2018
 (Amounts in thousands)

Non-hazardous

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Contractually required contribution	\$ 1,471	\$ 1,516	\$ 1,312	\$ 1,515
Contributions in relation to the contractually required contribution	\$ 1,471	\$ 1,516	\$ 1,312	\$ 1,515
Contribution deficiency (excess)	\$ -	\$ -	\$ -	\$ -
KSU covered payroll	\$ 3,583	\$ 3,888	\$ 4,321	\$ 5,390
Contributions as a percentage of covered payroll	41.05%	38.99%	30.36%	28.11%

Hazardous

	<u>2018</u>
Contractually required contribution	\$ 61
Contributions in relation to the contractually required contribution	\$ 61
Contribution deficiency (excess)	\$ -
KSU covered payroll	\$ 309
Contributions as a percentage of covered payroll	19.74%

Note: These are 10-year schedules. However, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until 10-years of information is available.

KENTUCKY STATE UNIVERSITY
SCHEDULE OF THE UNIVERSITY'S (KSU)
PROPORTIONATE SHARE OF THE NET PENSION LIABILITY
KENTUCKY TEACHERS' RETIREMENT SYSTEM
June 30, 2018
(Amounts in thousands)

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
KSU's proportion of the net pension liability	\$ 40,538	\$ 68,926	\$ 63,956	\$ 64,987
KSU's proportionate share of the net pension liability	0.14%	0.22%	0.23%	0.30%
State's proportionate share of the collective net pension liability	\$ 32,308	\$ 6,496	\$ 6,503	\$ 7,374
KSU's covered payroll	\$ 17,779	\$ 16,961	\$ 19,076	\$ 21,451
KSU's proportionate share of the net pension liability as a share of its covered payroll	228.01%	406.38%	335.27%	302.96%
Plan fiduciary net position as a percentage of total pension liability	39.83%	35.22%	42.49%	45.59%

Note: This table represents data that is one year in arrears.

Changes in assumptions: For fiscal year 2018, the KTRS plan discount rate increased from 4.20 percent to 4.49 percent. For fiscal year 2017, the KTRS plan discount rate decreased from 4.88 percent to 4.20 percent. For fiscal year 2016, there was a decrease in the assumed investment rate of return from 7.75 percent to 7.50 percent; a decrease in the assumed rate of inflation from 3.50 percent to 3.25 percent; a decrease in the assumed rate of wage inflation from 1.00 percent to 0.75 percent and a decrease in the payroll growth assumption from 4.50 percent to 4.00 percent.

KENTUCKY STATE UNIVERSITY
SCHEDULE OF THE UNIVERSITY'S CONTRIBUTION
KENTUCKY TEACHERS' RETIREMENT SYSTEM
June 30, 2018
(Amounts in thousands)

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Contractually required contribution	\$ 1,730	\$ 1,879	\$ 1,773	\$ 2,059
Contributions in relation to the contractually required contribution	\$ 1,730	\$ 1,879	\$ 1,773	\$ 2,059
Contribution deficiency (excess)	-	-	-	-
KSU covered payroll	\$ 19,083	\$ 17,779	\$ 16,961	\$ 19,076
Contributions as a percentage of covered payroll	9.07%	10.57%	10.45%	10.79%

Note: These are 10-year schedules. However, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until 10-years of information is available.

KENTUCKY STATE UNIVERSITY
 SCHEDULE OF THE UNIVERSITY'S (KSU)
 PROPORTIONATE SHARE OF THE NET OPEB LIABILITY
 KENTUCKY EMPLOYEES RETIREMENT SYSTEM
 June 30, 2018
 (Amounts in thousands)

<u>Non-hazardous</u>	<u>2018</u>
KSU's proportion of the net OPEB liability	\$ 6,178
KSU's proportionate share of the net OPEB liability	0.24%
KSU's covered payroll	\$ 3,888
KSU's proportionate share of the net OPEB liability as a share of its covered payroll	158.90%
Plan fiduciary net position as a percentage of total pension liability	24.40%
<u>Hazardous</u>	<u>2018</u>
KSU's proportion of the net OPEB liability	\$ 3
KSU's proportionate share of the net OPEB liability	0.05%
KSU's covered payroll	\$ 79
KSU's proportionate share of the net OPEB liability as a share of its covered payroll	3.80%
Plan fiduciary net position as a percentage of total pension liability	98.80%

Note: This table represents data that is one year in arrears.

SCHEDULE OF THE UNIVERSITY'S OPEB CONTRIBUTIONS
 KENTUCKY EMPLOYEES RETIREMENT SYSTEM
 June 30, 2018
 (Amounts in thousands)

<u>Non-hazardous</u>	<u>2018</u>
Contractually required contribution	\$ 301
Contributions in relation to the contractually required contribution	\$ 301
Contribution deficiency (excess)	\$ -
KSU covered payroll	\$ 3,583
Contributions as a percentage of covered payroll	8.40%

KENTUCKY STATE UNIVERSITY
SCHEDULE OF THE UNIVERSITY'S OPEB CONTRIBUTIONS
KENTUCKY EMPLOYEES RETIREMENT SYSTEM
June 30, 2018
(Amounts in thousands)

Hazardous

2018

Contractually required contribution	\$	12
Contributions in relation to the contractually required contribution	\$	12
Contribution deficiency (excess)	\$	-
KSU covered payroll	\$	309
Contributions as a percentage of covered payroll		3.88%

Note: These are 10-year schedules. However, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until 10-years of information is available.

KENTUCKY STATE UNIVERSITY
 SCHEDULE OF THE UNIVERSITY'S (KSU)
 PROPORTIONATE SHARE OF THE NET OPEB LIABILITY
 KENTUCKY TEACHERS' RETIREMENT SYSTEM
 June 30, 2018
 (Amounts in thousands)

	<u>2018</u>
KSU's proportion of the net OPEB liability	\$ 5,880
KSU's proportionate share of the net OPEB liability	0.24%
KSU's covered payroll	\$ 17,779
KSU's proportionate share of the net OPEB liability as a share of its covered employee payroll	33.07%
Plan fiduciary net position as a percentage of total pension liability	21.18%

Note: This table represents data that is one year in arrears.

SCHEDULE OF THE UNIVERSITY'S OPEB CONTRIBUTIONS
 KENTUCKY TEACHERS' RETIREMENT SYSTEM
 June 30, 2018
 (Amounts in thousands)

	<u>2018</u>
Contractually required contribution	\$ 287
Contributions in relation to the contractually required contribution	\$ 287
Contribution deficiency (excess)	\$ -
KSU covered payroll	\$ 19,083
Contributions as a percentage of covered payroll	1.50%

Note: These are 10-year schedules. However, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until 10-years of information is available.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE
WITH *GOVERNMENT AUDITING STANDARDS*

Members of the Board of Regents
Kentucky State University
Frankfort, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Kentucky State University (the University), a component unit of the Commonwealth of Kentucky, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the University's basic financial statements and have issued our report thereon dated October 31, 2018. Our report includes a reference to other auditors who audited the financial statements of Kentucky State University Foundation, Inc. (Foundation) as described in our report on the University's financial statements. The financial statements of the Foundation were not audited in accordance with *Government Auditing Standards*.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the University's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control. Accordingly, we do not express an opinion on the effectiveness of the University's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be a material weakness and a significant deficiency.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and questioned costs to be a material weakness (Finding 2018-002).

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule of findings and questioned costs to be a significant deficiency (Finding 2018-001).

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The University's Response to Findings

The University's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The University's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Crowe LLP". The letters are cursive and slightly slanted to the right.

Crowe LLP

Lexington, Kentucky
October 31, 2018

KENTUCKY STATE UNIVERSITY
SCHEDULE OF FINDINGS AND RESPONSES
June 30, 2018

Finding 2018-001 – Controls Over Financial Reporting

Criteria: Applicable standards state that management is responsible for having internal controls in place to provide appropriate and reliable financial reports, and to select and apply appropriate accounting principles. Management is not required to prepare their financial reports, but management needs to demonstrate the level of qualifications and controls to prepare their financial reports without significant deficiencies in these controls.

Condition: During the current year audit, the University did not have adequate controls in place over financial reporting to allow for timely, accurate financial reporting. We noted that not all general ledger accounts had been reconciled to subsidiary ledgers or other supporting detail on at least a quarterly basis.

Context: The University experienced turnover in key accounting positions resulting in a lack of timely reconciliations and production of timely financial reports. Management also identified errors in the system-generated calculation of depreciation expense of certain capital assets resulting in an adjusting entry during the audit.

Effect: The existence of inaccurate transaction postings, as well as unreconciled accounts can affect the financial statement information that is available for making informed business decisions and supervision of operations. This weakness in the financial reporting controls infrastructure increases the risk of errors in the financial records and is less likely to detect irregularities, including fraud, on a timely basis. A periodic reconciliation process allows for the preparation of accurate and timely financial statements.

Cause: The above condition appears to be the result of the inability to fully implement a timely review and reconciliation process.

Recommendation: We recommend the University implement internal control procedures, which require general ledger accounts to be reconciled at least quarterly.

Views of responsible officials and planned corrective action: Management agrees with the finding. See corrective action plan.

KENTUCKY STATE UNIVERSITY
SCHEDULE OF FINDINGS AND RESPONSES
June 30, 2018

Finding 2018-002 – Controls Over Payroll Procedures

Criteria: Management is responsible for maintaining an adequate internal control structure surrounding key processes and cycles, in order to facilitate accurate and timely financial reporting.

Condition: During the current year audit, the University did not have adequate internal controls in place over payroll procedures.

Context: During the current year audit, the following issues relating to payroll were identified:

- Certain employees who are required to submit time sheets are not completing them
- Completed time sheets are not properly approved by a supervisor
- Vacation leave is not being properly reported to payroll via time sheets
- Leave time not being taken in accordance with University policy
- Withholdings not tracked and remitted to appropriate agencies in a timely manner resulting in inaccuracies and additional payments for penalties
- Improper classification of employees related to retirement plans
- Former employees being paid benefits after termination
- Current employees not having appropriate withholding from payroll for benefits
- No documentation of required levels of approval of new hires, promotions or pay rate changes
- No payroll change reports processed or reviewed by someone independent of payroll

Effect: The absence of effective internal controls in relation to the payroll process could affect the accuracy of financial statement information. This weakness in accounting infrastructure increases the risk of errors in the financial records and is less likely to detect irregularities, including fraud on a timely basis.

Cause: The above condition appears to be the result of a lack of internal controls and segregation of duties within payroll procedures.

Recommendation: We recommend the University review internal controls surrounding payroll procedures to ensure adequate segregation of duties and approvals are put in place. Further, all supporting documentation including pay rate approvals and timesheets should be maintained.

Views of responsible officials and planned corrective action: Management agrees with the finding. See corrective action plan.