KENTUCKY STATE UNIVERSITY

Financial Statements

For the Years Ended June 30, 2016 and 2015
with Report of Independent Auditors

CONTENTS

DEANDORTON

DEAN DORTON ALLEN FORD, PLLC

Report of Independent Auditors

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 of Kentucky State University (the University) as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements which collectively comprise the University's basic financial statements as listed on the table of contents. We have also audited the financial statements of the Kentucky State University Foundation, Inc. (the Foundation), the University's discretely presented component unit, as of and for the years ended June 30, 2016 and 2015.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits 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.

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 and the report of other auditors is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, based on our audits 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, 2016 and 2015, and the respective changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 17 and required supplementary information on pages 63 through 64 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our 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 December 29, 2016 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.

Dean Dorton Allen Ford, PLLC

December 29, 2016
Lexington, Kentucky

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, 2016, with comparative information for the year ended June 30, 2015. 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, 2016, reflected total assets of $126.8 million and total liabilities of $118.4 million. Total net position was $8.3 million.

- Total assets increased $2.5 million or 2.0%, primarily due to increases in deferred pension outflows. Total liabilities increased by $282,000 by $5.5 million or 4.9% primarily due increases in deferred pension inflows.

- Unrestricted net position, which the University reserves for spending in programs and other capital-related contingencies, decreased $3.0 million. This decrease was primarily due to a revenue shortfall and 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 endowment earnings that are spendable, consistent with the University's spending policy.

- Operating revenues were $31.7 million and operating expenditures were $61.3 million, resulting in a loss from operations of $29.6 million. Net non-operating revenues were $26.6 million, including $23.4 million in state appropriations, which, when combined with the loss from operations and capital appropriations, resulted in an overall decrease in net position of $3.1 million.

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 and liabilities. Net position, the difference between total assets and total liabilities, 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

	2016	2015
ASSETS		
Current assets	$ 26,157,384	$ 26,731,772
Noncurrent assets	91,594,862	93,185,847
Total assets	$ 117,752,246	$ 119,917,619
DEFERRED OUTFLOWS OF RESOURCES	$ 9,056,663	$ 4,390,217
LIABILITIES		
Current liabilities	8,610,628	7,753,840
Non-current liabilities	98,952,303	99,943,423
Total liabilities	107,562,931	107,697,263
DEFERRED INFLOWS OF RESOURCES	$ 10,883,769	$ 5,164,405
NET POSITION		
Invested in capital assets, net of related debt	69,264,917	70,447,308
Restricted		
Nonexpendable	8,657,506	8,657,506
Expendable	3,197,211	3,358,791
Unrestricted	(72,757,426)	(71,017,437)
Total net position	$ 8,362,208	$ 11,446,168

Assets and deferred outflows: As of June 30, 2016, total assets amounted to $126.8 million. Of this amount, investment in capital assets (net of depreciation) of $75.1 million, or 63.8% of total assets, represented the largest asset class. Investments amounted to $15.3 million or 13.0% of total assets. During the year, total assets increased by $2.5 million, primarily due to increases in deferred outflows of resources related to pension funding.

Liabilities and deferred inflows: As of June 30, 2016, total liabilities amounted to $118.4 million. Net pension liabilities amounted to $93.3 million. The University's proportion of the net pension 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 plans relative to the projected contributions of all participating universities, actuarially determined. Long-term debt includes bonds payable for housing and dining system and energy-related equipment and technology equipment purchased under a Master Lease Agreement. During the year, total liabilities increased by $5.6 million, primarily due to increases in deferred inflows of resources related to pension funding.

Net Position: Net position of the University was $8.6 million at June 30, 2016 and was reported in four net position categories: invested in capital assets, net of related debt $69.4 million, restricted nonexpendable $8.7 million, restricted expendable $3.2 million, and unrestricted $(72.7) million.

Statement of Revenues, Expenses and Changes in Net Position

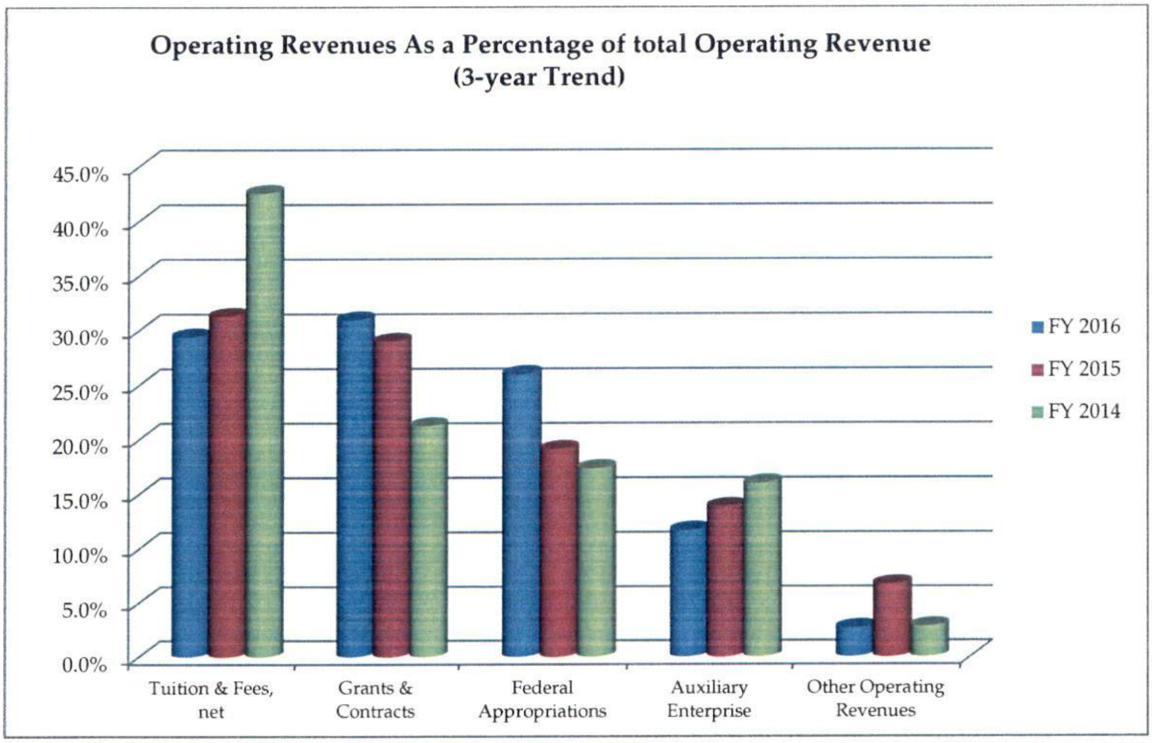
The Statement of Revenues, Expenses and Changes in Net Position is prepared on the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. All 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.

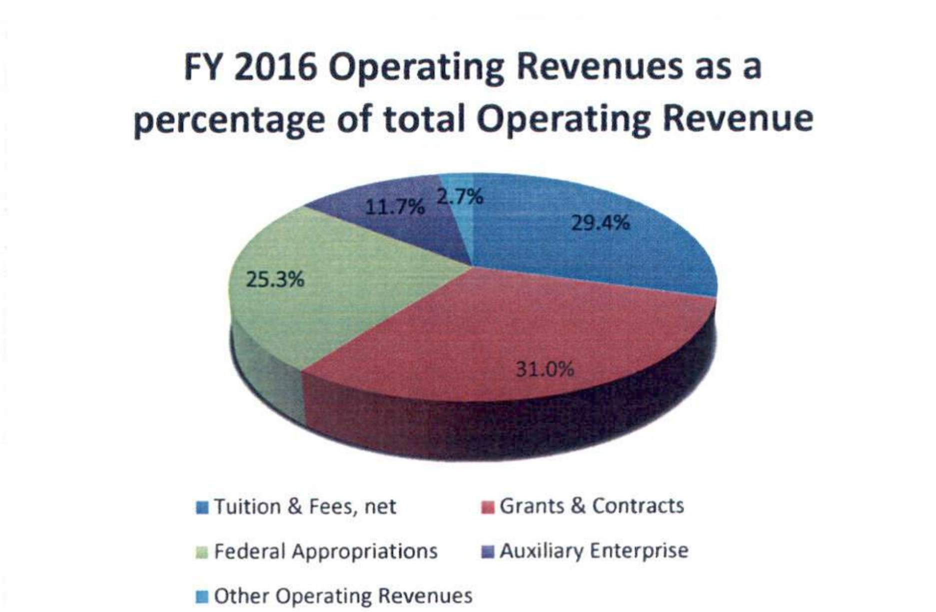
Financial activities are reported as either operating or non-operating. GASB Statement No. 35 requires state appropriations, gifts, investment income and endowment income to be classified as non-operating revenues. Accordingly, the University reports an operating loss prior to the addition of non-operating 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, 2016 and June 30, 2015 is as follows.

Condensed Statement of Revenues, Expenses and Changes in Net Position

	2016	2015
OPERATING REVENUES		
Student tuition and fees, net	$ 9,316,745	$ 11,517,008
Grants and contracts	9,808,120	10,101,995
Federal appropriations	8,006,332	6,665,512
Auxiliary enterprises	3,702,842	4,826,037
Other operating revenue	846,985	1,741,780
Total operating revenues	31,681,024	34,852,332
OPERATING EXPENSES		
Educational and general	56,825,667	63,553,521
Auxiliary enterprises	4,499,210	4,982,456
Total operating expenses	61,324,877	68,535,977
OPERATING LOSS	(29,643,853)	(33,683,645)
NONOPERATING REVENUES (EXPENSES)		
State appropriations	23,429,600	23,429,600
Federal grants and contracts	3,785,004	5,024,963
Investment income (loss)	(209,844)	280,360
Interest on capital asset – related debt	(445,054)	(263,107)
Other	-	-
Endowment gifts	187	4,636
Total non-operating revenues	26,559,893	28,476,452
Decrease in net position before cumulative effect of change in accounting principle	(3,083,960)	(5,207,193)
Cumulative effect of a change in accounting principle	-	(93,364,175)
Decrease in net position	(3,083,960)	(98,571,368)
Net position, beginning of year	11,446,168	110,017,536
Net position, end of year	$ 8,362,208	$ 11,446,168

Figure1


Operating Revenues As a Percentage of total Operating Revenue
(3-year Trend)
45.0%
40.0%
35.0%
30.0%
25.0%
20.0%
15.0%
10.0%
5.0%
0.0%
Tuition & Fees, net
Grants & Contracts
Federal Appropriations
Auxiliary Enterprise
Other Operating Revenues
FY 2016
FY 2015
FY 2014


FY 2016 Operating Revenues as a percentage of total Operating Revenue
11.7%
2.7%
29.4%
25.3%
31.0%
Tuition & Fees, net
Grants & Contracts
Federal Appropriations
Auxiliary Enterprise
Other Operating Revenues

Operating Revenue

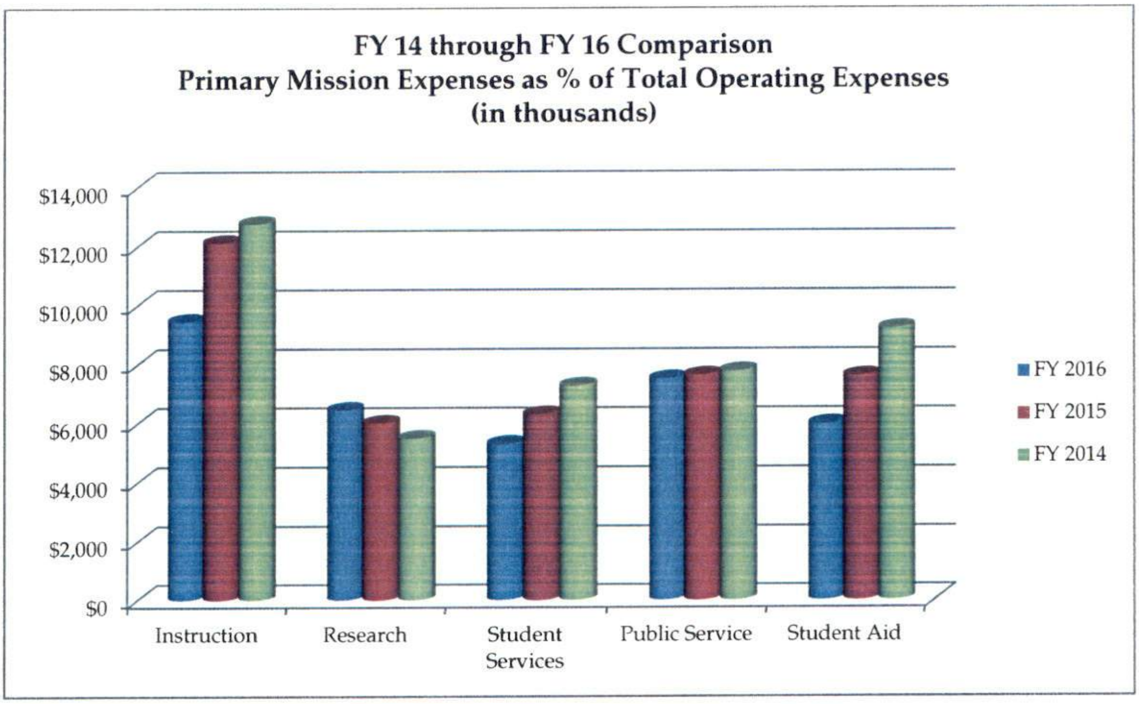
Total operating revenues were $31.7 million for the year ended June 30, 2016, a decrease of $3.2 million compared to FY15. The primary components of operating revenue were federal, state and local grants and contracts of $9.8 million (31.0%) student tuition and fees, net, of $9.3 million (29.4%), federal appropriations of $8.0 million (25.3%) and auxiliary services and other revenues of $4.5 million (14.4%). FY16 Student tuition and fees revenue decreased $2.2 million compared to FY15. FY16 Grants and contracts revenue decreased $1.3 million compared to FY15 due to decreased awards and spending. FY16 Federal appropriations increased $1.4 million compared to FY15. FY16 Auxiliary services and other revenue decreased $2.0 million compared to FY15. Refer to ***Figure 1*** for the three year trend of the operating revenues as a percent to total operating revenues and revenue by category.

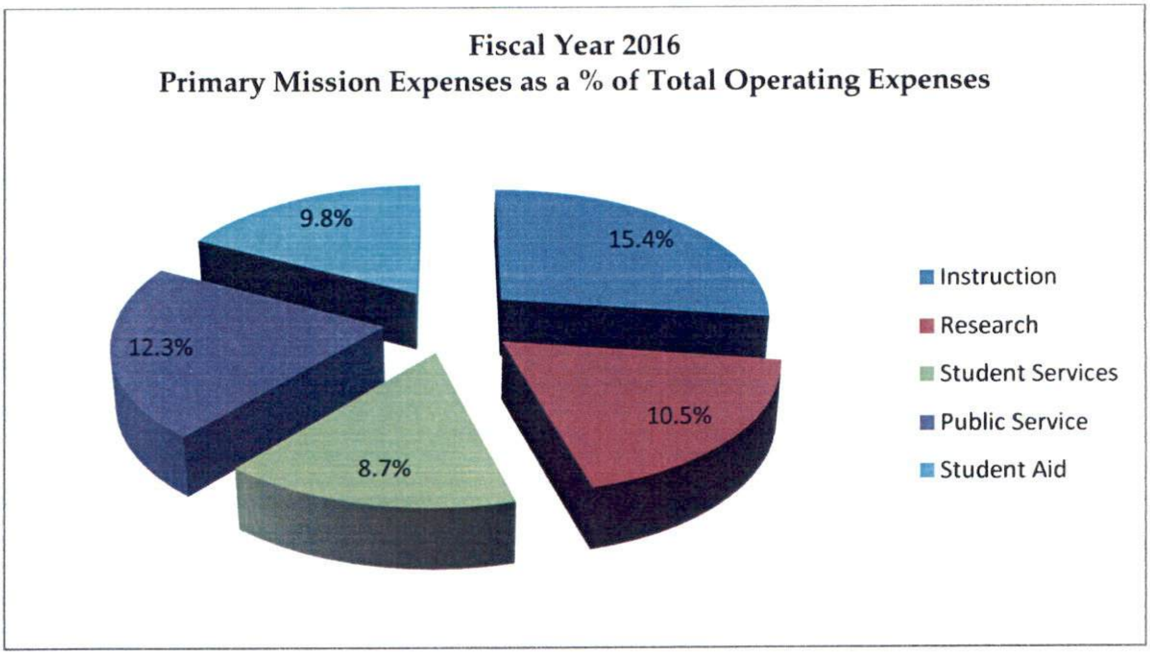
Operating Expenses

Operating expenses totaled $61.3 million, a decrease of $7.2 million from last year. Of this amount, $34.7 million (56.6%) was expended directly for the primary mission of the University – instruction (15.4%), research (10.5%), student services (8.7%), student aid (12.3%), and public service (9.8%). Instruction is the main component of Primary Mission expenses amounting to $9.5 million in fiscal year 2016 or 15.4%. Refer to ***Figure*** 2 for the operating expenses categorized into the Primary Mission of the University.

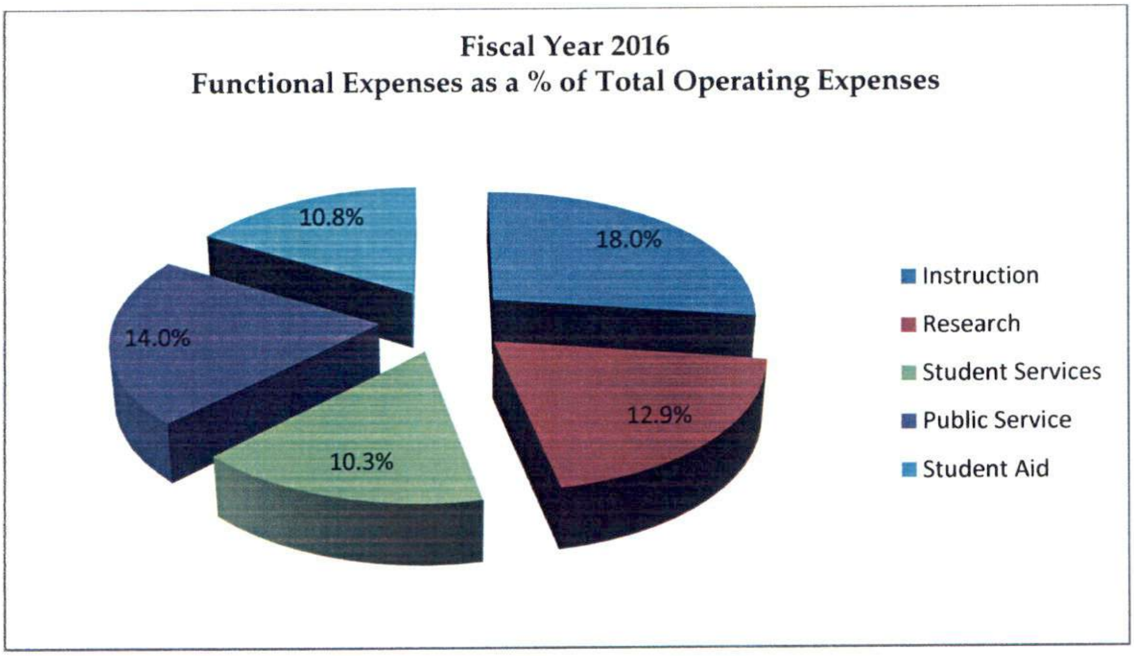
(Percentages below do not include depreciation or operations/maintenance allocations.)

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 12 – 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.)*



The University continued to invest in student aid and support services to provide students with opportunities to be successful in fiscal 2016. For the year ended June 30, 2016, student aid expenses totaled $6.0 million and scholarship allowances totaled $5.2 million.

The University had an overall decrease in institutional support of $760,000, which was consistent with the overall expenditure reduction 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 $29.6 million. Non-operating revenues, net of expenses, amounted to $26.6 million, resulting in a decrease in income before other revenues, expenses, gains or loss of $3.1 million for the year. Non-operating revenues include state appropriations of $23.4 million and non-operating federal grants and contracts of $3.8 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

	2016	2015
Cash (used) provided by:		
Operating activities	$ (26,876,152)	$ (23,099,893)
Non-capital financing activities	27,216,483	28,457,420
Capital and related financing activities	(3,413,206)	(1,911,723)
Investment activities	-	-
Net increase (decrease) in cash	(3,072,875)	3,445,804
Cash and cash equivalents, beginning year	23,021,767	19,575,963
Cash and cash equivalents, end of year	$ 19,948,892	$ 23,021,767

Cash and Investments

Major sources of cash received from operating activities are student tuition and fees of $9.86 million and grants and contracts of $14.4 million. Major uses of cash for operating activities were payments to employees for salaries and benefits of $32.4 million and to vendors and contractors of $17.2 million.

Noncapital financing activities included state appropriations from the Commonwealth of Kentucky of $23.4 million.

Capital and related financing activities include purchases and payments of $3.4 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.

State Appropriations

State appropriations represent approximately 40.2% 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 appropriation is 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, 2016, 2015 and 2014.

	2016	2015	2014
Commonwealth appropriations	$ 23,429,600	$ 23,429,600	$ 23,537,400
Federal appropriations	8,006,332	6,665,512	6,722,332
Total appropriations	$ 31,435,932	$ 30,095,112	$ 30,259,732

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 2016, the Commonwealth provided no capital appropriations 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, 2016, 2015 and 2014.

	2016	2015	2014
Federal grants and contracts, operating	$ 7,254,074	$ 7,955,755	$ 5,935,012
Federal grants and contracts, non-operating	3,785,004	5,024,963	5,928,036
State grants and contracts	2,554,046	2,146,240	2,289,810
Total grants and contracts	$ 13,593,124	$ 15,126,958	$ 14,152,858

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 2015-16, the Commonwealth funded one capital project; appropriating $10.4 million in state bond funds toward Repair Boilers and Aging Distribution Lines. 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.

Designated and Non-designated Spending

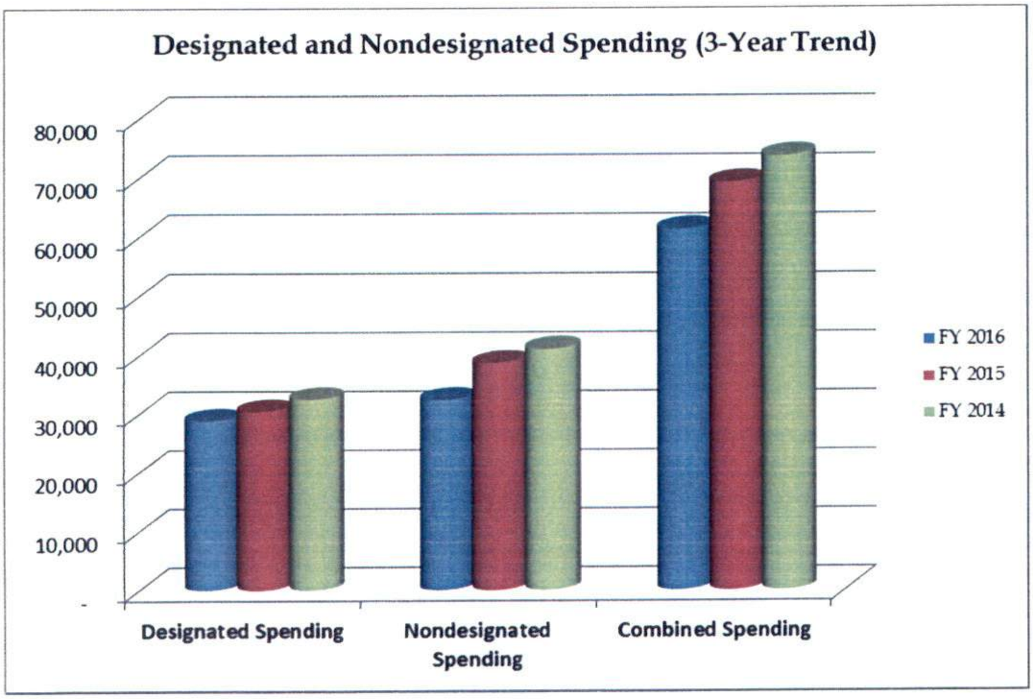
In the tables below, expenses have been categorized into designated or non-designated spending categories. The designated spending category includes funds expended by function from contracts and grants, land grant, auxiliary and depreciation. These funds must be expended for the purposes for which the 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 the non-designated category decreased by approximately $6.4 million in 2016, primarily due to decreases in available revenue and corresponding budget reductions.

	2016		
	Designated Spending	Non-designated Spending	Combined Spending
Instruction	$ 370,589	$ 9,090,312	$ 9,460,901
Research	5,300,249	1,160,763	6,461,012
Public service	5,309,416	2,205,324	7,514,740
Academic support	1,689,059	1,170,040	2,859,099
Student services	1,001,060	4,316,586	5,317,646
Institutional support	1,287,531	9,462,217	10,749,748
Operation and plant maintenance	-	4,627,724	4,627,724
Student aid	5,594,355	392,891	5,987,246
Auxiliary	4,196,218	-	4,196,218
Depreciation	4,150,543	-	4,150,543
Total	$ 28,899,020	$ 32,425,857	$ 61,324,877

	2015		
	Designated Spending	Non-designated Spending	Combined Spending
Instruction	$ 327,639	$11,797,807	$ 12,125,446
Research	4,625,650	1,391,407	6,017,057
Public service	5,354,315	2,284,045	7,638,360
Academic support	1,211,068	1,809,631	3,020,699
Student services	1,290,862	5,024,524	6,315,386
Institutional support	937,482	10,521,309	11,458,791
Operation and plant maintenance	-	5,229,721	5,229,721
Student aid	7,612,000	-	7,612,000
Auxiliary	4,658,295	-	4,658,295
Depreciation	4,460,222	-	4,460,222
Total	$ 30,477,533	$ 38,058,444	$ 68,535,977

The graph in ***Figure 3*** shows a three year trend of designated, non-designated, and combined spending. Non-designated spending is higher than designated spending in FY16. However, designated spending decreased $1.6 million in 2016 and $1.0 million in 2015. Non-designated spending decreased $2.4 million in 2015 and decreased $6.4 million in 2016. Overall, the combined spending followed the same trend as designated spending with a decrease of $4.5 million in 2015 and decrease of $7.9 million in 2016.

Figure 3



Capital Asset and Debt Administration

Capital Assets

Capital assets, net of accumulated depreciation, totaled $75.1 million at June 30, 2016, a decrease of $2.0 million. Capital assets as of June 30, 2016 and significant changes in capital assets during the year are as follows (in millions):

	June 30, 2016	Net Additions (Reductions) FY 15-16	June 30, 2015	Net Additions (Reductions) FY 14-15	June 30, 2014
Land and land improvements	$ 6.3	$ -	$ 6.3	$ -	$ 6.3
Buildings, fixed equipment and infrastructure	154.7		154.7	-	154.7
Equipment, vehicles and capitalized software	28.3	1.2	27.1	(5.2)	32.3
Library materials and art	10.5	0.1	10.4	-	10.4
Construction in progress	2.4	1.3	1.1	0.1	1.0
Accumulated depreciation	(127.1)	(4.6)	(122.5)	1.5	(124.0)
Total	$ 75.1	$ (2.0)	$ 77.1	$ (3.6)	$ 80.7

At June 30, 2016, the University has capital construction projects in progress with approximately $1.4 million remaining.

Long Term Debt

At June 30, 2016, bonds and lease payable amounted to $5.9 million, as summarized below:

	2016	2015	2014
Lease Obligations	$ 2,783,028	$ 3,300,007	$ 3,796,904
Note payable to City of Frankfort	150,000	200,000	250,000
General Receipts Bonds	2,980,000	3,195,000	3,405,000
Bond discount and issue costs	(49,798)	(49,798)	(49,798)
Total	$ 5,863,230	$ 6,645,209	$ 7,402,106

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
- State Funding Model – On January 16, 2013, Moody's Investor Service downgraded its outlook for the entire US higher education sector to negative. The state is being forced to innovate and come up with strategies for getting better results with less money. One of the strategies is the idea of tying state education allocations to performance metrics instead of enrollment.

The overall financial position of the University was stable during fiscal year 2016. 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 being a regional university of excellence.

KENTUCKY STATE UNIVERSITY

Statements of Net Position

June 30, 2016 and 2015

	2016	2015
ASSETS		
Current assets		
Cash and cash equivalents	$ 19,948,892	$ 23,021,767
Accounts, grants and loans receivable, net	6,067,885	3,565,529
Inventory and other current assets	140,607	144,476
Total current assets	26,157,384	26,731,772
Noncurrent assets		
Accounts, grants and loans receivable, net	1,093,100	509,872
Investments	15,373,614	15,583,458
Capital assets, net	75,128,148	77,092,517
Total noncurrent assets	91,594,862	93,185,847
DEFERRED OUTFLOWS OF RESOURCES		
Deferred outflows – KERS	2,946,915	1,953,418
Deferred outflows – KTRS	6,109,748	2,436,799
Total deferred outflows	9,056,663	4,390,217
Total assets and deferred outflows	126,808,909	124,307,836
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	5,274,209	4,345,584
Accrued compensated absences	1,003,343	1,310,815
Unearned revenue	1,050,268	874,549
Deposits	169,134	167,442
Other current liabilities	303,807	276,536
Long-term debt, current portion	809,868	778,914
Total current liabilities	8,610,629	7,753,840
Noncurrent liabilities		
Net pension liability	93,364,026	93,542,214
Long-term debt, noncurrent portion	5,053,363	5,866,295
Federal grants refundable	534,914	534,914
Total noncurrent liabilities	98,952,303	99,943,423
DEFERRED INFLOWS OF RESOURCES		
Deferred inflows – KERS	1,581,041	367,000
Deferred inflows – KTRS	9,302,728	4,797,405
Total deferred inflows	10,883,769	5,164,405
Total liabilities and deferred inflows	118,446,701	112,861,668
NET POSITION		
Invested in capital assets, net of related debt	69,264,917	70,447,308
Restricted		
Nonexpendable	8,657,506	8,657,506
Expendable	3,197,211	3,358,791
Unrestricted	(72,757,426)	(71,017,437)
Total net position	$ 8,362,208	$ 11,446,168

KENTUCKY STATE UNIVERSITY FOUNDATION, INC.

Statements of Financial Position

June 30, 2016 and 2015

		2016		2015
Assets				
Current assets:				
Cash and cash equivalents	$	**2,153,581**	$	1,956,892
Total current assets		**2,153,581**		1,956,892
Investments, at fair value		**8,446,484**		9,487,554
Property and equipment:				
Equipment		**140,400**		140,400
Buildings and improvements		**65,526**		65,526
		205,926		205,926
Accumulated depreciation		**(178,134)**		(175,259)
Property and equipment, net		**27,792**		30,667
Other assets		**32,472**		35,722
Total assets	$	**10,660,329**	$	11,510,835
Liabilities and Net Assets				
Current liabilities:				
Accounts payable	$	**3,572**	$	49,814
Accrued liabilities		**281**		2,777
Total liabilities		**3,853**		52,591
Net assets:				
Unrestricted		**261,113**		334,691
Temporarily restricted		**6,786,750**		7,492,125
Permanently restricted		**3,608,613**		3,631,428
Total net assets		**10,656,476**		11,458,244
Total liabilities and net assets	$	**10,660,329**	$	11,510,835

KENTUCKY STATE UNIVERSITY

Statements of Revenues, Expenses and Changes in Net Position

Years ended June 30, 2016 and 2015

	2016	2015
REVENUES		
Operating revenues		
Student tuition and fees (net of scholarship allowances of $5,187,952 and $5,431,851)	$ 9,316,745	$ 11,517,008
Federal grants and contracts	7,254,074	7,955,755
Federal appropriations	8,006,332	6,665,512
State and local grants and contracts	2,554,046	2,146,240
Auxiliary enterprises:		
Residence halls	1,949,920	2,478,446
Dining	1,719,895	2,229,515
Bookstore	-	85,922
Other auxiliaries	33,027	32,154
Other operating revenues	846,985	1,741,780
Total operating revenues	31,681,024	34,852,332
EXPENSES		
Operating expenses		
Educational and general		
Instruction	9,460,901	12,125,446
Research	6,461,012	6,017,057
Public service	7,514,740	7,638,360
Academic support	2,859,099	3,020,699
Student services	5,317,646	6,315,386
Institutional support	10,749,748	11,458,791
Operation and maintenance of plant	4,627,724	5,229,721
Student aid	5,987,246	7,612,000
Depreciation	3,847,551	4,136,061
Auxiliary enterprises		
Residence halls	1,844,913	2,043,210
Dining	1,669,271	1,929,366
Other auxiliaries	682,034	685,719
Depreciation	302,992	324,161
Total operating expenses	61,324,877	68,535,977
Operating loss	(29,643,853)	(33,683,645)

KENTUCKY STATE UNIVERSITY

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

Years ended June 30, 2016 and 2015

	2016	2015
NONOPERATING REVENUES (EXPENSES)		
State appropriations	**$ 23,429,600**	$ 23,429,600
Federal grants and contracts	**3,785,004**	5,024,963
Investment (loss) income (net of investment expense)	**(209,844)**	280,360
Interest on capital asset-related debt	**(445,054)**	(263,107)
Endowment gifts	**187**	4,636
Net non-operating revenues	**26,559,893**	28,476,452
Decrease in net position before cumulative effect of change	**(3,083,960)**	(5,207,193)
Cumulative effect of a change in accounting principle	**-**	(93,364,175)
Decrease in net position	**(3,083,960)**	(98,571,368)
NET POSITION		
Net position, beginning of year	**11,446,168**	110,017,536
Net position, end of year	**$ 8,362,208**	$ 11,446,168

KENTUCKY STATE UNIVERSITY FOUNDATION, INC.

Statement of Activities

Year ended June 30, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains and other support:				
Contributions	$ 5,281	$ 942,248	$ 72,553	$ 1,020,082
Investment income:				
Interest and dividends	4,836	229,473	-	234,309
Realized and unrealized losses	(2,717)	(81,451)	-	(84,168)
Total investment income	2,119	148,022	-	150,141
Releases from restrictions	1,982,834	(1,982,834)	-	-
Total revenues, gains and other support	1,990,234	(892,564)	72,553	1,170,223
Expenses:				
Scholarships	180,791	-	-	180,791
Operating expenses	234,661	-	-	234,661
Personal services	327,756	-	-	327,756
University support	1,135,934	-	-	1,135,934
Student support	63,601	-	-	63,601
Travel and promotion	29,248	-	-	29,248
Total expenses	1,971,991	-	-	1,971,991
Change in net assets	18,243	(892,564)	72,553	(801,768)
Net assets, beginning of year	334,691	7,492,125	3,631,428	11,458,244
Reclassification	(91,821)	187,189	(95,368)	-
Net assets, end of year	$ 261,113	$ 6,786,750	$ 3,608,613	$ 10,656,476

KENTUCKY STATE UNIVERSITY FOUNDATION, INC.

Statement of Activities

Year ended June 30, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains and other support:				
Contributions	$ 23,913	$ 583,878	$ 126,439	$ 734,230
Investment income:				
Interest and dividends	5,335	232,353	-	237,688
Realized and unrealized gains	4,843	207,401	-	212,244
Total investment income	10,178	439,754	-	449,932
Releases from restrictions	810,832	(810,832)	-	-
Total revenues, gains and other support	844,923	212,800	126,439	1,184,162
Expenses				
Scholarships	163,574	-	-	163,574
Operating expenses	159,846	-	-	159,846
Personal services	79,289	-	-	79,289
University support	206,351	-	-	206,351
Student support	156,036	-	-	156,036
Travel and promotion	89,252	-	-	89,252
Total expenses	854,348	-	-	854,348
Change in net assets	(9,425)	212,800	126,439	329,814
Net assets, beginning of year	377,256	7,285,817	3,465,357	11,128,430
Reclassification	(33,140)	(6,492)	39,632	-
Net assets, end of year	$ 334,691	$ 7,492,125	$ 3,631,428	$ 11,458,244

KENTUCKY STATE UNIVERSITY

Statements of Cash Flows

Years ended June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities		
Tuition and fees	$ 9,856,592	$ 13,157,159
Grants and contracts	14,375,643	18,844,897
Payments to suppliers	(17,377,862)	(19,301,690)
Payments to employees	(32,448,182)	(35,439,941)
Student financial aid	(5,915,937)	(7,268,917)
Collection of loans issued to students	(106,875)	(518,095)
Collection of loans issued to students	172,642	249,253
Auxiliary enterprises:		
Residence halls and dining	3,669,815	4,707,961
Bookstore	-	85,922
Other auxiliaries	33,027	32,154
Other receipts	864,985	2,351,404
Net cash from operating activities	(26,876,152)	(23,099,893)
Cash flows from non-capital financing activities		
State appropriations	23,429,600	23,429,600
Federal grants and contracts	3,785,004	5,024,963
Endowment gifts	187	4,636
Student organization agency receipts	1,692	90,344
Student organization agency disbursements	-	(92,123)
Net cash from non-capital financing activities	27,216,483	28,457,420
Cash flows from capital financing activities		
Purchases of capital assets	(2,186,174)	(891,719)
Principal paid on capital debt	(781,978)	(756,897)
Interest paid on capital debt	(445,054)	(263,107)
Net cash from capital financing activities	(3,413,206)	(1,911,723)
Cash flows from investing activities		
Investment income	275,241	347,130
Investment expenses	(65,397)	(66,770)
Proceeds from sale of investments	8,620,976	5,901,009
Purchases of investments	(8,830,820)	(6,181,369)
Net cash from investing activities	-	-
Net decrease in cash and cash equivalents	(3,072,875)	3,445,804
Cash and cash equivalents at beginning of year	23,021,767	19,575,963
Cash and cash equivalents at end of year	$ 19,948,892	$ 23,021,767

KENTUCKY STATE UNIVERSITY

Statements of Cash Flows, continued

Years ended June 30, 2016 and 2015

Reconciliation of net operating loss to net cash from operating activities	2016	2015
Operating loss	$ (29,643,853)	$ (33,683,645)
Adjustments to reconcile operating loss to net cash from operating activities:		
Depreciation expense	4,150,543	4,460,222
Actuarially calculated pension expense	5,541,176	5,342,444
Bad debt expense	727,573	2,478,056
Changes in assets and liabilities:		
Receivables, net	(3,813,157)	2,223,015
Deferred outflows	(4,666,446)	(4,390,217)
Inventory and other current assets	3,869	13,368
Accounts payable and accrued liabilities	928,625	943,342
Accrued compensated absences	(307,472)	(246,535)
Other liabilities	27,271	184,836
Unearned revenue	175,719	(424,779)
Net cash from operating activities	$ (26,876,152)	$ (23,099,893)

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.

1. Organization and Summary of Significant Accounting Policies, continued

Basis of Accounting, continued

- **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.

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.

1. Organization and Summary of Significant Accounting Policies, continued

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. Short-term investments are investments that are not cash equivalents but mature within the next fiscal year and are classified as current assets.

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.

1. Organization and Summary of Significant Accounting Policies, continued

Capital Assets, 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 statements of net position and as a component of compensation and benefit expense in the statements 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

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension 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.

1. Organization and Summary of Significant Accounting Policies, continued

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.

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.

1. Organization and Summary of Significant Accounting Policies, continued

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, 2016 and 2015, the Foundation made distributions of approximately $1,135,900 and $206,400 respectively, 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.

Cumulative Effect of Change in Accounting Principle

In fiscal year 2015, the University adopted GASB Statement 68, *Accounting and Financial Reporting for Pensions*. The primary objective of GASB's Statement 68 is to improve accounting and financial reporting by state and local governments for pensions. The financial statements include the accrued actuarial pension liability for the Kentucky Employees Retirement System (KERS) and Kentucky Teachers' Retirement System (KTRS) and the additional components associated with recording the pension liability. The effect of this change was an increase to operating expenses of $5.34 million. The cumulative effect of the change, totaling $93.4 million, is shown as a one-time decrease to net position in the 2015 Statement of Revenues, Expenses and Changes in Net Position.

Recent Pronouncements

In June 2015, the GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. 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. This Statement requires reporting of the entity's OPEB liability on the face of the financial statements and more extensive note disclosures and required supplementary information about OPEB liabilities. The provisions of this Statement are effective for reporting periods beginning after June 15, 2017. The University is currently evaluating the effects of this statement on its financial statements.

1. Organization and Summary of Significant Accounting Policies, continued

Recent Pronouncements, continued

In March 2016, the GASB issued Statement No. 82, *Pension Issues – an amendment of GASB Statements No. 67, No. 68, and No. 73*. The objective of this Statement is to address certain issues that have been raised with respect to Statements No. 67, *Financial Reporting for Pension Plans*, No. 68 *Accounting and Financial Reporting for Pensions*, and No. 73 *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an Actuarial Standard of Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016, except for the requirements of paragraph 7 in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements of paragraph 7 are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. The University is currently evaluating the effects of this statement on its financial statements.

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, demand deposits, certificates of deposit and temporary investments in marketable securities with original maturities less than three months.

At June 30, 2016 and 2015, the University had petty cash funds totaling zero, and deposits as reflected by bank balances as follows:

	2016	2015
Insured, commercial banks	$ 250,000	$ 250,000
Uninsured, commercial banks; collateral held by pledging institution's agent in the University's name	8,772,759	3,330,624
Maintained by Commonwealth of Kentucky, collateral held by the Commonwealth in the Commonwealth's name	10,920,349	19,459,607
	$ 19,943,108	$ 23,040,231

2. Cash, Cash Equivalents, and Investments, continued

The difference in the cash carrying amount per the statement of net position and the above balances represented items in transit. At June 30, 2016 and 2015, the University had no cash and cash equivalents that are restricted for capital expenditures.

As of June 30, 2016, the University had the following investments and maturities:

Investment Maturities (in years)

Investment Type	**Fair Value**	**< 1**	**1-5**	**6-10**	**11-20**
Bonds	**$ 2,012,879**	**$ 105,000**	**$ 1,049,438**	**$ 711,639**	**$ 146,802**
Bond mutual funds	**4,713,857**	**-**	**4,713,857**		
Money market funds	**905,632**	**905,632**	**-**	**-**	**-**
Real estate funds	**888,418**	**-**	**888,418**	**-**	**-**
	8,520,786	**$ 1,010,632**	**$ 6,651,713**	**$ 711,639**	**$ 146,802**
Equities and equity mutual funds	**6,852,828**				
	$ 15,373,614				

As of June 30, 2015, the University had the following investments and maturities:

Investment Maturities (in years)

Investment Type	Fair Value	< 1	1-5	6-10	11-20
Bonds	$ 1,566,149	$ 65,000	$ 792,521	$ 554,361	$154,267
Bond mutual funds	4,253,115	-	4,253,115		
Money market funds	1,175,640	1,175,640	-	-	-
Real estate funds	986,234	-	986,234	-	-
	7,981,138	$ 1,240,640	$ 6,031,870	$ 554,361	$ 154,267
Equities and equity mutual funds	7,602,320				
	$ 15,583,458				

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

2. Cash, Cash Equivalents, and Investments, continued

The University has the following recurring fair value measurements as of June 30, 2016:

	Total	Level 1	Level 2	Level 3
Money market funds	$ 905,632	$ 905,632	$ -	$ -
Fixed income	5,366,206	5,366,206	-	-
Common stock	6,852,828	6,852,828	-	-
Mutual funds:				
Alternative strategies	1,360,530	1,360,530	-	-
Real estate funds	888,418	888,418	-	-
	$ 15,373,614	$ 15,373,614	$ -	$ -

The University had the following recurring fair value measurements as of June 30, 2015:

	Total	Level 1	Level 2	Level 3
Money market funds	$ 1,175,640	$ 1,175,640	$ -	$ -
Fixed income	3,768,269	3,768,269	-	-
Common stock	7,602,320	7,602,320	-	-
Mutual funds:				
Alternative strategies	2,050,995	2,050,995	-	-
Real estate funds	986,234	986,234	-	-
	$ 15,583,458	$ 15,583,458	$ -	$ -

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.

2. Cash, Cash Equivalents, and Investments, continued

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.

3. Accounts, Grants and Loan Receivable

Accounts, grants and loans receivable consist of the following as of June 30, 2016 and 2015.

	2016	2015
Student tuition and fees	$ 12,157,002	$ 11,791,939
Student loans	2,453,991	2,134,649
Grants and contracts	5,681,734	2,036,872
Other	34,758	258,999
	20,327,485	16,222,459
Less: allowance for doubtful accounts	(13,166,500)	(12,147,058)
	7,160,985	4,075,401
Non-current portion	1,093,100	509,872
Current portion	$ 6,067,885	$ 3,565,529

4. Capital Assets, Net

Capital assets as of June 30, 2016, are summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Cost				
Land and improvements	$ 6,275,031	$ -	$ -	$ 6,275,031
Buildings	154,741,818	-	-	154,741,818
Equipment	21,712,184	1,108,689	-	22,820,873
Computer software	1,481,493	48,254	-	1,529,747
Library holdings	10,372,986	115,380	-	10,488,366
Transportation equipment	3,853,344	96,259	-	3,949,603
Construction in progress	1,143,779	1,322,858	505,266	1,961,371
	199,580,635	2,691,440	505,266	201,766,809
Accumulated depreciation				
Buildings	94,544,089	2,493,002	-	97,037,091
Equipment	14,669,742	1,319,133	-	15,988,875
Library holdings	9,985,722	203,398	-	10,189,120
Transportation equipment	3,288,565	135,010	-	3,423,575
	122,488,118	4,150,543	-	126,638,661
Capital assets, net	$ 77,092,517	$ (1,459,103)	$ 505,266	$ 75,128,148

Capital assets as of June 30, 2015, are summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Cost				
Land and improvements	$ 6,275,031	$ -	$ -	$ 6,275,031
Buildings	154,740,029	1,789	-	154,741,818
Equipment	26,013,295	676,804	4,977,915	21,712,184
Computer software	1,476,993	4,500	-	1,481,493
Library holdings	10,372,986	-	-	10,372,986
Transportation equipment	4,847,974	35,097	1,029,727	3,853,344
Construction in progress	970,250	173,529	-	1,143,779
	204,696,558	891,719	6,007,642	199,580,635
Accumulated depreciation				
Buildings	92,048,221	2,495,868	-	94,544,089
Equipment	18,050,947	1,596,710	4,977,915	14,669,742
Library holdings	9,748,260	237,462	-	9,985,722
Transportation equipment	4,188,110	130,182	1,029,727	3,288,565
	124,035,538	4,460,222	6,007,642	122,488,118
Capital assets, net	$ 80,661,020	$ (3,568,503)	$ -	$ 77,092,517

5. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities as of June 30, 2016 and 2015, are as follows:

	2016	2015
Payable to vendors and contractors	$ 3,531,052	$ 1,915,422
Accrued sick leave liability	292,360	292,360
Accrued salaries and other liabilities	1,450,796	2,137,802
	$ 5,274,208	$ 4,345,584

6. Unearned Revenue

Unearned revenue consists of the following as of June 30, 2016 and 2015:

	2016	2015
Unearned summer school tuition and fees	$ 175,077	$ 205,411
Unearned grants and contracts	875,191	669,138
	$ 1,050,268	$ 874,549

7. Long-Term Liabilities

Long-term liabilities as of June 30, 2016, are summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion	Noncurrent portion
General receipts bonds	$ 3,195,000	$ -	$ 215,000	$ 2,980,000	$ 225,000	$ 2,755,000
Note payable – City of Frankfort	200,000	-	50,000	150,000	50,000	100,000
Capital lease – police vehicles	67,469	-	33,735	33,734	33,734	-
Capital lease obligations-energy savings	3,232,538	-	483,243	2,749,295	504,198	2,245,097
Bond discount	(49,798)	-	-	(49,798)	(3,064)	(46,734)
Total bonds payable and capital lease obligations	6,645,209	-	781,978	5,863,231	809,868	5,053,363
Federal grants refundable	534,914	-	-	534,914	-	534,914
Total long-term liabilities	$ 7,180,123	$ -	$ 781,978	$ 6,398,145	$ 809,868	$ 5,588,277

7. Long-Term Liabilities, continued

Long-term liabilities as of June 30, 2015, are summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion	Noncurrent portion
General receipts bonds	$ 3,405,000	$ -	$ 210,000	$ 3,195,000	$ 215,000	$ 2,980,000
Note payable – City of Frankfort	250,000	-	50,000	200,000	50,000	150,000
Capital lease – police vehicles	101,204	-	33,735	67,469	33,735	33,734
Capital lease obligations- energy savings	3,695,700	-	463,162	3,232,538	483,243	2,749,295
Bond discount	(49,798)	-	-	(49,798)	(3,064)	(46,734)
Total bonds payable and capital lease obligations	7,402,106	-	756,897	6,645,209	778,914	5,866,295
Federal grants refundable	534,914	-	-	534,914	-	534,914
Total long-term liabilities	$ 7,937,020	$ -	$ 756,897	$ 7,180,123	$ 778,914	$ 6,401,209

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, 2016.

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 $3,160,000 and $3,660,000 as of June 30, 2016 and 2015, respectively.

In August 2009, the University signed a 10 year promissory note with the City of Frankfort, for the purchase of real property. The note and all current and prior payments were recognized and recorded as of June 30, 2016.

The following is a schedule of future minimum payments required for the note payable at June 30, 2016:

Year ending June 30,	
2017	$ 50,000
2018	50,000
2019	50,000
Total	$ 150,000

7. Long-Term Liabilities, continued

The principal and interest repayment requirements relating to the outstanding bonds payable at June 30, 2016, are as follows:

	Principal	Interest	Total
Year ending June 30,			
2017	$ 225,000	$ 114,241	$ 339,241
2018	230,000	105,916	335,916
2019	240,000	97,291	337,291
2020 – 2024	1,350,000	341,651	1,691,651
2025 – 2027	935,000	73,431	1,008,431
Total	$ 2,980,000	$ 732,530	$ 3,712,530

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, 2016:

Year ending June 30,	
2017	$ 650,527
2018	616,792
2019	616,792
2020	616,792
Thereafter	616,791
Total minimum lease payments	3,117,694
Less: amounts representing interest	334,665
Present value of minimum lease payment	$ 2,783,029

8. Operating Lease

The University leases computer equipment under operating leases, which expire on various dates through 2017. Lease payments to the lessors under these leases totaled $174,239 and $106,104 for the years ended June 30, 2016 and 2015, respectively. Minimum lease payments for 2017 are $69,794.

9. Pension Plans

Regular full-time employees of the University, faculty and staff are required to participate in a retirement plan.

Kentucky Teachers Retirement System

All faculty and exempt employees required to hold a degree and occupying full-time positions, defined as seven-tenths (7/10) of normal full-time service on a daily or weekly basis, are required by state law to participate either in the Kentucky Teachers Retirement System (KTRS) or the Optional Retirement Plan (ORP).

Plan Description

All qualifying employees not participating in the defined contribution plan sponsored by the University are provided with pensions through the Teachers Retirement System of Kentucky (KTRS)—a cost-sharing multiple-employer defined benefit pension plan. Pursuant to the provisions of KRS 161.250 the Board of Trustees of KTRS is vested with the responsibility for the general administration and management of the retirement system. The Board may adopt procedures necessary to conduct the business of the retirement system as needed. The applicable provisions of the Kentucky Revised Statutes (state law) shall control if any inconsistency exists between state law and this policy. KTRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Teachers Retirement System, 479 Versailles Road, Frankfort, Kentucky 40601-3868 or by calling (505) 848-8500.

Benefits Provided

KTRS, a cost sharing, multiple-employer, public employee retirement system, provides retirement benefits based on an employee's final average salary and number of years of service. Benefits are subject to certain reductions if the employee retires before reaching age sixty, unless the employee has twenty-seven or more years of participation in the plan. The plan also provides for disability retirement, death and survivor benefits and medical insurance.

9. Pension Plans, continued

Contributions

Benefit and contribution rates are established by state statute. Per Kentucky Revised Statute 161.250 contribution requirements of the active employees and the participating universities are established and may be amended by the KTRS Board. For the fiscal years ended June 30, 2016 and 2015 employees were required to contribute 8.18% and 7.16%, respectively, of their annual pay for retirement benefits. The University's contractually required contribution rate for the year ended June 30, 2016 and 2015, was 15.86% and 14.84%, respectively, of current employees' salaries, actuarially determined as an amount that, when combined with employee contributions, is expected to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. Contributions to the pension plan from the University were $2,183,786 and $2,436,799 for the years ended June 30, 2016 and 2015, respectively.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2016, the University reported a liability for its proportionate share of the net pension liability that reflected a reduction for State pension support provided to the University. 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 is as follows:

	2016	2015
University proportionate share of the net pension liability	$63,955,762	$64,987,214
State's proportionate share of the net pension liability associated with the University	6,503,709	7,374,016
Total	$70,459,471	$72,361,230

The net pension liability was measured as of June 30, 2015, 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 a projection of the University's long-term share of contributions to the pension plan relative to the projected contributions of all participating universities and the Commonwealth, actuarially determined. At June 30, 2016 and 2015 respectively, the University's proportion was 0.23% and 0.34%.

9. Pension Plans, continued

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

For the years ended June 30, 2016, and 2015 the University recognized pension expense of $1,408,369 and $3,184,443. The University reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	2016 Deferred Outflows of Resources	2016 Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ 698,257
Changes in assumptions	3,925,962	617,415
Net difference between projected and actual earnings on pension plan investments	-	1,611,765
Changes in proportion and differences between University contributions and proportionate share of contributions	-	6,375,291
University contributions subsequent to the measurement date	2,183,786	-
Total	$ 6,109,748	$ 9,302,728

	2015 Deferred Outflows of Resources	2015 Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	879,356
Net difference between projected and actual earnings on pension plan investments	-	3,918,049
Changes in proportion and differences between University contributions and proportionate share of contributions	-	-
University contributions subsequent to the measurement date	2,436,799	-
Total	$ 2,436,799	$ 4,797,405

9. Pension Plans, continued

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

$2,183,786 reported as deferred outflows of resources related to pensions resulting from University contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Years ended June 30:

2017	$1,532,025
2018	1,532,025
2019	1,532,025
2020	630,808
2021	149,883
Total	$5,376,766

Actuarial Assumptions

The total pension liability in the June 30, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.5 percent
Salary increases	4.00-8.20 percent
Investment rate of return	7.50 percent, net of pension plan investment expense, including inflation

Mortality rates were based on the RP-2000 Combined Mortality Table for Males or Females, as appropriate, with adjustments for mortality improvements based on a projection of Scale AA to 2020 with a setback of 1 year for females.

The long-term expected rate of return on pension 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 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 weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation.

9. Pension Plans, continued

Actuarial Assumptions, continued

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

Asset Class	Target Allocation	Long-Term Nominal Rate of Return
U.S. Equity	45%	6.4%
Non U.S. Equity	17%	6.5%
Fixed Income	24%	1.6%
High Yield Bonds	4%	3.1%
Real Estate	4%	5.8%
Alternatives	4%	6.8%
Cash	2%	1.5%
Total	100%	

Discount Rate

The discount rate used to measure the total pension liability was 4.88%. 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 pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members until the 2039 plan year. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments through 2038 and a municipal bond index rate of 3.82% was applied to all periods of projected benefit payments after 2038. The Single Equivalent Interest Rate (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.

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, calculated using the discount rate of 4.88%, as well as what the University's net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (3.88%) or 1-percentage-point higher (5.88%) than the current rate:

	1% Decrease (3.88%)	Discount Rate (4.88%)	1% Increase (5.88%)
University's share of the net pension liability	$79,599,983	$63,955,762	$51,009,921

9. Pension Plans, continued

Sensitivity of the University's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate, continued

Detailed information about the pension plans' fiduciary net position is available in the separately issued KTRS financial reports.

Kentucky Employees Retirement System

Substantially all other full-time University employees are required by law to participate in the Kentucky Employees Retirement System (KERS), a cost sharing multiple-employer, public employee retirement system. KERS provides retirement benefits based on an employee's final average salary and number of years of service. Benefits are subject to certain reductions if the employee retires before reaching age sixty-five, or less than twenty-seven years of service. The plan also provides for disability retirement, death and survivor benefits and medical insurance.

The Kentucky Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Employees Retirement System, 1260 Louisville Road, Perimeter Park West, Frankfort, Kentucky 40601 or by calling (502) 564-4646.

Health care and life insurance benefits are provided for eligible retired employees through the above pension plans. Expenditures for all employee benefits are included as expenditures within the appropriate functional areas.

Benefits Provided

KERS provides retirement, disability, and death benefits. Each employee covered by KERS is entitled to a monthly benefit based upon their months of service multiplied by the average of 5 full fiscal years of salary (highest 5 or last 5 based on date of participation) upon attainment of KERS specified age (or age and service combinations). Participants have a fully vested interested after the completion of 60 months of service.

Retirement benefits are determined as a percent of the employee's final 5-year average compensation times the employee's years of service. Employees hired prior to September 1, 2008 can retire at any age with 27 years of service or at age 65 with 4 years of service. Employees hired after September 1, 2008 can retire when their age plus years of service equal 87 (must be at least age 57) or at age 65 with 5 years of service. Employees are eligible for service-related disability benefits regardless of length of service. Five years of service is required for nonservice-related disability eligibility. Disability benefits are determined based the employee's participation date. Death benefits are based on age, months of service and whether the employee was active or retired.

9. Pension Plans, continued

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. KERS participants hired with an effective date prior to September 1, 2008 contribute 5 percent of their covered compensation; the University contributes 38.77 percent. KERS participants hired with an effective date on or after September 1, 2008 contribute 6 percent of their covered compensation; the University contributes 38.77 percent. These amounts were actuarially determined as an amount that, when combined with employee contributions, is expected to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. Contributions to the pension plan from the University were $1,390,663 and $1,953,418 for the year ended June 30, 2016 and 2015.

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2016, and 2015 the University reported a liability of $29,408,264 and $28,555,000 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015, and June 30, 2014, 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 a projection of the University's long-term share of contributions to the pension plan relative to the projected contributions of all participating universities, actuarially determined. At June 30, 2016 and 2015 the University's proportion was .29 percent and 0.32 percent.

9. **Pension Plans, continued**

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

For the year ended June 30, 2016, and 2015, the University recognized pension expense of $3,099,791 and $2,158,000. The University reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	2016 Deferred Outflows of Resources	2016 Deferred Inflows of Resources
Differences between expected and actual experience	$ 62,828	$ -
Changes in assumptions	1,409,663	-
Net difference between projected and actual earnings on pension plan investments	83,761	-
Changes in proportion and differences between University contributions and proportionate share of contributions	-	1,581,041
University contributions subsequent to the measurement date	1,390,663	-
Total	$ 2,946,915	$ 1,581,041

9. Pension Plans, continued

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

	2015 Deferred Outflows of Resources	2015 Deferred Inflows of Resources
Differences between expected and actual experience	$ -	$ -
Changes in assumptions	-	-
Net difference between projected and actual earnings on pension plan investments	-	367,000
Changes in proportion and differences between University contributions and proportionate share of contributions	-	-
University contributions subsequent to the measurement date	1,953,418	-
Total	$ 1,953,418	$ 367,000

9. Pension Plans, continued

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

$1,390,663 reported as deferred outflows of resources related to pensions resulting from University contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended June 30:

2017	$ 311,252
2018	311,250
2019	311,250
2020	311,250
2021	311,250
Total	$1,556,252

Actuarial Assumptions

The total pension liability in the June 30, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.25 percent
Salary increases	4.0 percent, average, including inflation
Investment rate of return	7.50 percent, net of pension plan investment expense, including inflation

The total pension liability in the June 30, 2014 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.5 percent
Salary increases	4.5 percent, average, including inflation
Investment rate of return	7.75 percent, net of pension plan investment expense, including inflation

The mortality table used for active members is RP-2000 Combined Mortality Table projected with Scale BB to 2013 (multiple 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.

9. Pension Plans, continued

Actuarial Assumptions, continued

The long-term expected return on plan assets is reviewed as part of the regular experience studies prepared every five years for the Kentucky Retirement Systems. The most recent analysis, performed for the period covering fiscal years 2008 through 2013, is outlined in a report dated April 30, 2014. Several factors are considered in evaluating the 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 capital market assumptions developed by the investment consultant are intended for use over a 10-year horizon and may not be useful in setting the long-term rate of return for funding pension plans which covers a longer timeframe. 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.

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 28-year amortization period of the unfunded actuarial accrued liability. The discount rate determination does not use a municipal bond rate. Projected future benefit payments for all current plan members were projected through 2117. The target asset allocation and best estimates of arithmetic nominal rates of return for each major asset class are summarized in the Commonwealth's Comprehensive Annual Financial Report.

The net pension liability as of June 30, 2016 is based on the June 30, 2015 actuarial valuation. Deferred outflows and inflows related to differences between projected and actual earnings on plan investments are netted and amortized over a closed five-year period.

9. Pension Plans, continued

Actuarial Assumptions, 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:

Asset Class	Target Allocation	Long-Term Nominal Rate of Return
Combined Equity	42%	5.40%
Combined Fixed Income	20%	1.50%
Real Return (Diversified Inflation Strategies)	10%	3.50%
Real Estate	3%	4.50%
Absolute Return (Diversified Hedge Funds)	10%	4.25%
Private Equity	10%	8.50%
Cash Equivalent	5%	-0.25%
Total	100%	

Discount rate

The discount rate used to measure the total pension liability was 7.50 percent. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and employers will be made at actuarially determined contribution rate of projected compensation over the remaining 28 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.

Sensitivity of the University's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate

The following presents the University's proportionate share of the net pension liability calculated using the discount rate of 7.50 percent, as well as what the University's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.50 percent) or 1-percentage-point higher (8.50 percent) than the current rate:

	1% Decrease (6.50%)	Discount Rate (7.50%)	1% Increase (8.50%)
University's share of the net pension liability	$33,125,900	$29,408,264	$26,263,200

Pension plan fiduciary net position. Detailed information about the pension plans' fiduciary net position is available in the separately issued KERS financial reports.

9. Pension Plans, continued

Optional Retirement Plan

All faculty and exempt employees who are eligible to participate in the KTRS retirement plan may elect to participate in the Optional Retirement Plan (ORP) instead of KTRS. In doing so, the employee may choose both Teachers Insurance and Annuity Association of America, (TIAA-CREF) or The Variable Annuity Life Insurance Company (VALIC). Both offer a defined contribution, 403b plan.

TIAA-CREF Individual & Institutional Services, Inc. distributes CREF and TIAA Real Estate Account variable annuities. Teachers Personal Investors Services, Inc. distributes Personal Annuity variable annuities, TIAA-CREF Mutual Funds, TIAA-CREF Institutional Mutual Funds, and TIAA-CREF Tuition Financing, Inc. products. TIAA-CREF Trust Company, FSB, provides trust services. Located in New York, NY, Teachers Insurance and Annuity Association of America (TIAA) and TIAA-CREF Life Insurance Company issue insurance and annuities. Financial statements are available on the website, www.tiaa-cref.com.

VALIC is the marketing name for the family of companies comprising VALIC Financial Advisors, Inc.; VALIC Retirement Services Company; VALIC Trust Company; and The Variable Annuity Life Insurance Company (VALIC); which are all members of American International Group, Inc. (AIG).

Complete information about VALIC's variable annuities, including financial statements, fees, charges, expenses and contract limitations, can be obtained by visiting the website www.aigvalic.com or by calling 1-800-428-2542.

Funding for the ORP is provided from eligible employees who contribute 6.16% of their salary through payroll deductions and the Commonwealth of Kentucky, which also indirectly contributes 8.74% of current eligible employees' salaries to the ORP through appropriations to the University. The University's contributions to ORP for the years ended June 30, 2016, and 2015 were $561,715 and $618,796, respectively, and equaled the required contribution for the year.

Effective July 1, 2010, KRS 61.546 states that the value of any accumulated sick leave that is added to the member's service credit in the KERS and KTRS on or after July 1, 2010 shall be paid to the retirement system by the last participating employer, based upon a formula adopted by the KERS and KTRS Boards. The KERS/KTRS sick leave liability as of June 30, 2015 and 2014 was $292,360.

10. Commitments and Contingencies

The University is a party to various law suits 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, as the maximum exposure to the University is in the range of $500,000 - $775,000.

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.

The United States Department of Agriculture (USDA) is currently performing a review of the University's administration of NIFA (National Institute of Food and Agriculture)-sponsored programs and associated financial activity. As part of this review, the USDA is questioning if the University has complied with the matching requirements of the grants for the period from 2011 to 2013. If it is determined that the University has not complied with the matching requirements the University could be required to spend an additional amount to meet the matching requirements. The amount could be up to $3,000,000. As of the date of the audit report, the review was not complete.

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.

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 2016. Functional expense purpose is classified by natural classification as follows:

12. Schedule of Expenses by Program, continued

2016

	Compensation & Benefits	Supplies & Services	Scholarships & Fellowships	Depreciation	Operations & Maintenance	Total
Instruction	$ 8,980,364	$ 477,037	$ 3,500	$ 607,816	$ 945,478	$11,014,195
Research	4,042,057	2,418,955	-	766,505	678,682	7,906,199
Public service	4,221,968	2,989,412	303,360	350,541	738,569	8,603,850
Academic support	1,819,686	1,039,413	-	253,891	292,317	3,405,307
Student services	3,911,422	1,404,337	1,887	430,320	539,748	6,287,714
Institutional support	6,839,097	3,910,651	-	760,169	1,082,043	12,591,960
Operation & maintenance of plant	1,828,836	2,798,888	-	636,508	(5,264,232)	-
Auxiliary enterprises	1,099,510	3,096,708	-	302,992	421,253	4,920,463
Student financial aid	295,620	84,436	5,607,190	41,801	566,142	6,595,189
Total operating expense	$ 33,038,560	$18,219,837	$ 5,915,937	$ 4,150,543	$ -	$61,324,877

12. Schedule of Expenses by Program, continued

2015

	Compensation & Benefits	Supplies & Services	Scholarships & Fellowships	Depreciation	Operations & Maintenance	Total
Instruction	$ 11,603,206	$ 515,489	$ 6,750	$ 644,558	$ 1,194,401	$13,964,404
Research	3,774,674	2,236,993	5,391	768,783	592,702	7,378,543
Public service	4,506,604	2,972,510	159,246	362,122	752,406	8,752,888
Academic support	1,879,853	1,139,846	1,000	308,775	297,549	3,627,023
Student services	4,731,292	1,584,094	-	453,339	622,088	7,390,813
Institutional support	5,815,688	5,643,103	-	900,415	1,220,732	13,579,938
Operation & maintenance of plant	2,329,718	2,900,003	-	658,837	(5,888,558)	-
Auxiliary enterprises	1,218,074	3,440,221	-	324,161	458,870	5,441,326
Student financial aid	516,960	123	7,094,917	39,232	749,810	8,401,042
Total operating expense	$ 36,376,069	$20,432,382	$ 7,267,304	$ 4,460,222	$ -	$68,535,977

13. Kentucky State University Foundation, Inc.

a. 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.

13. Kentucky State University Foundation, Inc., continued

b. Summary of Significant Accounting Policies

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 2016 and 2015 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. Depreciation expense was $2,875 and 16,958 for the years ended June 30, 2016 and 2015, respectively.

13. Kentucky State University Foundation, Inc., continued

b. 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. 2016-14, *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 December 29, 2016, 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.

13. Kentucky State University Foundation, Inc., continued

Reclassification

The presentation of certain items in 2015 were reclassified to conform with the 2016 presentation, this reclassification had no impact on net assets or change in net assets.

During 2016 and 2015, the Foundation determined that certain amounts were improperly classified between the net asset categories. Certain amounts have been reclassified to more accurately reflect the net asset balances of the Foundation based on donor intent. This reclassification had no effect on total change in net assets or total net assets.

c. Investments

Investments as of June 30, 2016 and 2015 are summarized as follows:

	2016	2015
Equity securities	**$ 5,427,028**	$ 6,422,743
Debt securities	**2,625,817**	2,252,883
Real estate investment trust	**8,129**	160,258
U.S government securities	**385,510**	651,670
Total investments	**$ 8,446,484**	$ 9,487,554

d. 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, 2016 and 2015.

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.

13. Kentucky State University Foundation, Inc., continued

d. Fair Value Measurements, continued

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, 2016 are as follows:

	Level 1	Level 2	Level 3	Total
Common stocks	**$ 3,481,670**	**$ -**	**$ -**	**$ 3,481,670**
Mutual funds	**1,762,207**	**-**	**-**	**1,762,207**
Municipal bonds	**-**	**270,742**	**-**	**270,742**
Corporate bonds	**-**	**2,355,075**	**-**	**2,355,075**
U.S government securities	**385,510**	**-**	**-**	**385,510**
Real estate investment trust	**-**	**8,129**	**-**	**8,129**
Equity exchange traded funds	**183,151**	**-**	**-**	**183,151**
Total	**$ 5,812,538**	**$ 2,633,946**	**$ -**	**$ 8,446,484**

Fair value measurements as of June 30, 2015 are as follows:

	Level 1	Level 2	Level 3	Total
Common stocks	$ 4,152,722	$ -	$ -	$ 4,152,722
Mutual funds	2,054,938	-	-	2,054,938
Municipal bonds	-	292,540	-	292,540
Corporate bonds	-	1,960,343	-	1,960,343
U.S government securities	651,670	-	-	651,670
Real estate investment trust	-	160,258	-	160,258
Equity exchange traded funds	215,083	-	-	215,083
Total	$ 7,074,413	$ 2,413,141	$ -	$ 9,487,554

13. Kentucky State University Foundation, Inc., continued

e. Temporarily Restricted Net Assets

For the years ended June 30, 2016 and 2015, net assets were released from donor restrictions by incurring expenses satisfying the purpose of the restrictions specified by donors as follows:

	2016	2015
Endowment spending allocation	$ 1,299,043	$ 235,616
University support	494,610	163,257
Scholarships	64,894	134,784
Operating and other expenses	51,090	66,971
Student support	47,929	137,869
Travel and other expenses	23,818	66,637
Personal services	1,450	5,698
Total release from restrictions	$ 1,982,834	$ 810,832

f. 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 years ended June 30, 2016 and 2015.

g. 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.

13. Kentucky State University Foundation, Inc., continued

g. Endowment Composition, continued

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, 2016 and 2015.

Endowment net asset composition by type of fund as of June 30, 2016 is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Donor-restricted endowment funds	$ -	$ 4,030,448	$ 3,608,613	$ 7,639,061

Endowment net asset composition by type of fund as of June 30, 2015 was as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Donor-restricted endowment funds	$ -	$ 5,032,261	$ 3,631,428	$ 8,663,689

Changes in endowment net assets as of June 30, 2016 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Endowment net assets, beginning of year	$ -	$ 5,032,261	$ 3,631,428	$ 8,663,689
Contributions	-	-	72,553	72,553
Interest and dividends	-	197,122	-	197,122
Realized and unrealized losses	-	(73,321)	-	(73,321)
Amounts appropriated for expenditure	-	(1,299,043)	-	(1,299,043)
Reclassifications	-	173,429	(95,368)	78,061
Endowment net assets, end of year	$ -	$ 4,030,448	$ 3,608,613	$ 7,639,061

13. Kentucky State University Foundation, Inc., continued

g. Endowment Composition, continued

Changes in endowment net assets as of June 30, 2015 were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Endowment net assets, beginning of year	$ -	$ 4,891,754	$ 3,465,357	$ 8,357,111
Contributions	-	-	126,439	126,439
Interest and dividends	-	201,540	-	201,540
Realized and unrealized gains	-	174,583	-	174,583
Amounts appropriated for expenditure	-	(235,616)	-	(235,616)
Reclassifications	-	-	39,632	39,632
Endowment net assets, end of year	$ -	$ 5,032,261	$ 3,631,428	$ 8,663,689

KENTUCKY STATE UNIVERSITY

Required Supplementary Information

Schedule of Kentucky State University's (KSU) Proportionate Share of the Net Pension Liability

Kentucky Employees Retirement System
(amounts in thousands)

	2016	2015
KSU's proportion of the net pension liability	$ 29,408	$ 28,555
KSU's proportionate share of the net pension liability	0.29%	0.32%
KSU's covered-employee payroll	$ 3,585	$ 5,262
KSU's proportionate share of the net pension liability as a share of its covered employee payroll	820.25%	542.60%
Plan fiduciary net position as a percentage of total pension liability	18.83%	22.32%

Schedule of Kentucky State University's Contribution
Kentucky Employees Retirement System
(amounts in thousands)

	2016	2015
Contractually required contribution	$ 1,390	$ 1,953
Contributions in relation to the contractually required contribution	$ 1,390	$ 1,953
Contribution deficiency (excess)	$ -	$ -
KSU covered-employee payroll	$ 3,585	$ 5,263
Contributions as a percentage of covered-employee payroll	38.77%	38.77%

Schedule of Kentucky State University's (KSU) Proportionate Share of the Net Pension Liability

Kentucky Teachers' Retirement System
(amounts in thousands)

	2016	2015
KSU's proportion of the net pension liability	$ 63,956	$ 64,987
KSU's proportionate share of the net pension liability	0.23%	0.30%
State's proportionate share of the collective net pension liability	$ 6,503	$ 7,374
KSU's covered-employee payroll	$ 14,212	$ 20,169
KSU's proportionate share of the net pension liability as a share of its covered employee payroll	450.01%	322.22%
Plan fiduciary net position as a percentage of total pension liability	42.49%	45.59%

Schedule of Kentucky State University's Contribution
Kentucky Teachers' Retirement System
(amounts in thousands)

	2016	2015
Contractually required contribution	$ 2,183	$ 2,436
Contributions in relation to the contractually required contribution	$ 2,183	$ 2,436
Contribution deficiency (excess)	-	-
KSU covered-employee payroll	$ 14,212	$ 20,169
Contributions as a percentage of covered-employee payroll	15.36%	15.36%

DEANDORTON
DEAN DORTON ALLEN FORD, PLLC

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*

Report of Independent Auditors

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) as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise Kentucky State University's basic financial statement as listed on the table of contents, and have issued our report thereon dated December 29, 2016.

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 opinion 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 Responses, we identified a deficiency in internal control that we consider to be a material weakness.

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 Responses to be a material weakness, Finding 2016-001. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free from 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

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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 the Finding

The University's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Responses. The University's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control 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.

Dean Dorton Allen Ford, PLLC

December 29, 2016
Lexington, Kentucky

Section I – Summary of Auditors' Results:

Financial Statements:

a. The type of report issued on the financial statements: **Unmodified Opinion**

b. Internal control over financial reporting:

Material weaknesses: **Yes**

Significant deficiencies identified that are not considered to be material weaknesses: **None noted**

c. Non-compliance which is material to the financial statements: **No**

Section II – Financial Statement Finding:

Finding 2016-001 (repeated from prior year):

Condition:

During the year ended June 30, 2016 the University did not have adequate controls over financial reporting to allow for timely, accurate financial reporting. All general ledger accounts were not reconciled to subsidiary ledgers or other supporting detail at least on a quarterly basis.

Effect:

Subsequent to the beginning of fieldwork, management provided an updated trial balance to accurately reflect activity recorded by the University that was not captured in the initial trial balance. After this revised trial balance was received, 11 adjusting journal entries were recorded to accurately reflect the financial position of the University as of June 30, 2016. Net Position for the year ended June 30, 2016 was increased by $535,968 as a result of these entries. These journal entries primarily related to student accounts receivable, grants, cash, and accounts payable.

Recommendation:

We recommend the University implement internal control procedures which require general ledger accounts to be reconciled at least quarterly. Not having accurate transactions posted in a timely manner can affect the financial statement information that is available for making informed business decisions and supervision of operations. 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. The quarterly reconciliation process allows for the preparation of accurate quarterly financial statements. For bank reconciliations, management should satisfy themselves as to the nature of any unusual reconciling items before authorizing adjustments to correct the balances. These adjustments should be thoroughly documented and promptly made so that it will not be necessary to carry them forward to the next reconciliation.

Finding 2016-001, continued:

Management response:

Management concurs. The University has begun revising procedures related to general ledger accounts. Procedures requiring monthly reconciliation of all general ledger accounts cash accounts will be implemented. Procedures requiring all other general ledger accounts to be reconciled at least quarterly will be implemented. Reconciliations for each month and quarter will be reviewed by department management as part of the financial statement development process. The University's internal auditor will test compliance at least twice during each fiscal year.