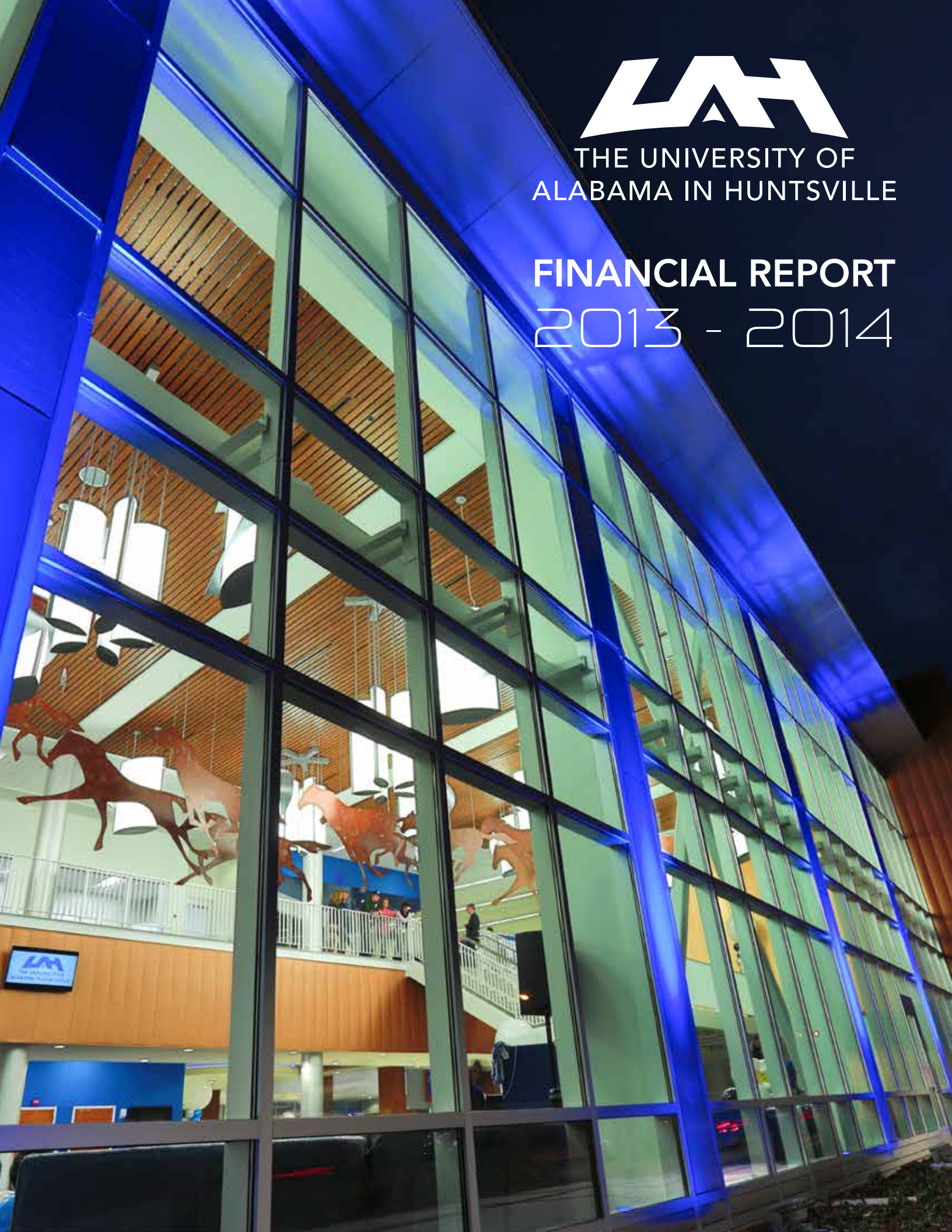




THE UNIVERSITY OF  
ALABAMA IN HUNTSVILLE

FINANCIAL REPORT  
2013 - 2014



# The University of Alabama in Huntsville

## FINANCIAL REPORT 2013-2014



Charger Union opened in January, 2014 and serves as the heart of The University of Alabama in Huntsville community, providing a comfortable, safe and welcoming environment for student life and engagement.

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## Independent Auditor's Report

To the Board of Trustees of The University of Alabama:

We have audited the accompanying financial statements of The University of Alabama in Huntsville ("UAH"), a campus of The University of Alabama System, which is a component unit of the State of Alabama, as of and for the years ended September 30, 2014 and 2013, and the related notes to the financial statements, which consist of the statements of net position and the related statements of revenues, expenses, and changes in net position and of cash flows of UAH and the statements of financial position and the related statements of activities of the University of Alabama in Huntsville Foundation ("UAHF"), UAH's discretely presented component unit.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

Our responsibility is to express opinions on the financial statements based on our audits. We did not audit the financial statements of UAHF, UAH's discretely presented component unit, as of September 30, 2014 and 2013, and for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for UAHF, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our 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, we consider internal control relevant to UAH'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 UAH's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

### ***Opinions***

In our opinion, based upon our audits and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of UAH



and its discretely presented component unit at September 30, 2014 and 2013, and the respective changes in financial position and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of Matter***

As discussed in Note 1, the financial statements of UAH are intended to present the financial position, the changes in financial position and, where applicable, the cash flows of only that portion of the business-type activities of the financial reporting entity of The University of Alabama System that is attributable to the transactions of UAH. They do not purport to, and do not, present fairly the financial position of The University of Alabama System as of September 30, 2014 and 2013, its changes in financial position, or, where applicable, its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

***Other Matters***

The accompanying management's discussion and analysis for the years ended September 30, 2014 and 2013 on pages 4 through 15 is required by accounting principles generally accepted in the United States of America 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.

*PricewaterhouseCoopers LLP*

January 26, 2015

## The University of Alabama in Huntsville Management's Discussion and Analysis (Unaudited)

The following discussion and analysis provides an overview of the financial performance and activities of The University of Alabama in Huntsville (the "University" or "UAH") during FY 2014 and 2013. This discussion and analysis has been prepared by University management and includes the Statements of Net Position; the Statements of Revenues, Expenses and Changes in Net Position; and the Statements of Cash Flows. These statements should be read in conjunction with the Notes to Financial Statements. As described in Note 1 of the financial statements, the University revised its previously issued 2013 financial statements.

### Introduction

The University is a public co-educational, state-supported research university and is classified by the Carnegie Foundation for the Advancement of Teaching as a "Very High Activity" research university, placing it among a select group of public universities in America. UAH has six research programs ranked in the top 25 in the nation, according to the National Science Foundation, including 5<sup>th</sup> in the United States in aeronautical and astronautical engineering.

The University offers 71 degree-granting programs that meet the highest standards of excellence, including 33 bachelor's degree programs, 23 master's degree programs, and 15 doctoral programs through its five colleges: Business Administration, Liberal Arts, Engineering, Nursing, and Science. UAH is an autonomous campus within The University of Alabama System (the "System") and is the anchor tenant for Cummings Research Park, the second largest university research park in the United States and home to numerous high technology and research companies.

The campus receives national recognition on a regular basis. UAH was listed as very competitive by *Barron's Profiles in American Colleges* and was one of only two public universities in Alabama to earn this designation. *U.S. News & World Report* consistently ranks UAH among the magazine's top tier national universities. Additionally, *USA Today* and *Princeton Review* reported UAH was one of the top 50 educational values in America.

The University received \$91.1 million for externally funded projects during FY 2014. Sponsors of research include federal and state agencies, academic institutions, industry and private foundations. Research is conducted within the five individual colleges and through the University's 10 independent research centers, laboratories and institutes. Major interdisciplinary research thrusts include: modeling and simulation; cybersecurity; systems engineering; rotorcraft and aerospace engineering; propulsion; optics; space physics and astrophysics; earth and atmospheric system science; information technology; materials science; biotechnology; nanotechnology; humanities; and lean supply chain, acquisition, and logistics.



## Statements of Net Position

The statements of net position present the assets, liabilities, and net position of the University as of the end of the fiscal year. The purpose of the statements of net position is to present a fiscal snapshot of the University to the readers of the financial statements. The statements of net position present end-of-year data for assets (current and noncurrent), liabilities (current and noncurrent), and net position (assets minus liabilities).

The statements of net position provide a summary of assets available to continue the operations of the University. The statements also show how much the University owes vendors, investors and lending institutions. Finally, the statements of net position provide a picture of the net position and the availability for expenditure by the University.

Net position is divided into three major categories. The first category, invested in capital assets, net of related debt, provides the University's equity in property, plant and equipment. The second asset category is restricted net position, which is divided into two categories, nonexpendable and expendable. The corpus of nonexpendable restricted resources, as it pertains to endowments, is only available for investment purposes. Donors have restricted income derived from these investments to primarily fund scholarships and fellowships. Expendable restricted net position is available for expenditure by the University but must be spent for purposes as determined by donors and/or external entities that have placed a time or purpose restriction on the use of the assets. The final category is unrestricted net position, which is available to the University as needed. Much of the University's unrestricted net position has been designated or reserved for specific purposes such as: repairs and replacement of equipment, capital projects, future debt service, quasi-endowments, insurance reserves, research centers and instructional departments.

A summarized comparison of the University’s assets, liabilities and net position as of September 30 is as follows:

<b>Summary of Statements of Net Position</b>			
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Current assets	\$ 145,140,584	\$ 155,908,246	\$ 147,826,985
Noncurrent assets:			
Endowment, life income and other investments	73,643,577	78,822,789	59,541,146
Capital assets, net	239,892,467	220,844,717	203,090,500
Legal settlement receivable	951,113	1,855,729	2,716,120
Other	171,882	219,742	268,124
<b>Total assets</b>	<b>459,799,623</b>	<b>457,651,223</b>	<b>413,442,875</b>
Current liabilities	60,187,022	54,979,041	49,898,977
Noncurrent liabilities	103,084,078	107,792,600	77,954,500
<b>Total liabilities</b>	<b>163,271,100</b>	<b>162,771,641</b>	<b>127,853,477</b>
Net position			
Invested in capital assets, net of related debt	128,446,531	124,034,324	125,072,139
Restricted	19,319,644	18,107,737	15,961,579
Unrestricted	148,762,348	152,737,521	144,555,680
<b>Total net position</b>	<b>\$ 296,528,523</b>	<b>\$ 294,879,582</b>	<b>\$ 285,589,398</b>

For FY 2014, the University’s current assets decreased \$10.8 million. Endowment, life income and other investments decreased \$5.2 million due to the net reclassification of \$8.3 million of cash and investments for capital activities to cash and cash equivalents and operating investments, offset by additional endowment investments of \$2.5 million. Capital assets, net of depreciation, increased \$19.0 million primarily due to the expansion and renovation of the Nursing Building and the construction of the Student Life Center and Severe Weather Institute and Radar & Lightning Laboratories. Current liabilities increased \$5.2 million. The majority of this increase is due to higher construction and payroll liabilities and unearned revenues that have increased consistent with our 2014 tuition increases. Noncurrent liabilities decreased \$4.7 million, the result of bond principal payments.

For FY 2013, the University’s current assets increased \$8.1 million. Endowment, life income and other investments increased \$19.3 million due to unspent bond proceeds of \$17.3 million, additional endowment investments of \$1.2 million and improved earnings from the portfolio offset by distributed endowment earnings. Capital assets, net of depreciation, increased \$17.8 million primarily due to the construction of the Student Life Center. The noncurrent portion of the legal settlement receivable of \$1.9 million is the net present value of an amount to be received in future years. Current liabilities increased \$5.1 million. The majority of this increase is due to the current portion of debt and deferred revenues. Noncurrent liabilities increased \$29.8 million, the result of the issuance of General Fee Revenue Bonds for the construction of the Student Life Center and renovation of the Nursing Building.

For FY 2012, the University's current assets increased \$16.3 million. Endowment, life income and other investments increased \$6.8 million due to additional endowment investments of \$5.2 million and improved earnings from the portfolio offset by distributed endowment earnings. Capital assets, net of depreciation, decreased \$3.6 million due to depreciation offset by capital expenditures. The noncurrent portion of the legal settlement receivable of \$2.7 million is the net present value of an amount to be received in future years. Current liabilities increased \$1.5 million. The majority of this increase is due to the current portion of debt and deferred revenues. Noncurrent liabilities decreased \$2.9 million, the result of bond principal payments.

For FY 2014, the University's total net position increased \$1.6 million. The University's investments in capital assets, net of related debt, increased approximately \$4.4 million primarily due to capital expenditures. Restricted net position increased \$1.2 million. Unrestricted net position decreased approximately \$4.0 million. Although unrestricted net position is not subject to externally imposed stipulations, substantially all of the University's unrestricted net position has been designated for capital projects, as well as various academic and research programs and initiatives.

For FY 2013, the University's total net position increased 3.3%. The University's investments in capital assets, net of related debt, decreased approximately \$1.0 million primarily due to depreciation offset by capital expenditures. Restricted net position increased \$2.1 million. Unrestricted net position increased approximately \$8.2 million. Although unrestricted net position is not subject to externally imposed stipulations, substantially all of the University's unrestricted net position has been designated for capital projects, as well as various academic and research programs and initiatives.

For FY 2012, the University's total net position increased 7.1%. The University's investments in capital assets, net of related debt, decreased approximately \$1.4 million primarily due to reduced capital expenditures during 2012. Restricted net position increased \$4.6 million. Unrestricted net position increased approximately \$15.7 million. Although unrestricted net position is not subject to externally imposed stipulations, substantially all of the University's unrestricted net position has been designated for capital projects, as well as various academic and research programs and initiatives.

### **Capital Assets**

For FY 2014, 2013, and 2012, the University had approximately \$450.3 million, \$426.9 million, and \$397.8 million invested in capital assets and accumulated depreciation of \$210.4 million, \$206.1 million, and \$194.7 million, respectively. Depreciation charges for FY 2014, 2013, and 2012 were \$13.1 million, \$12.4 million, and \$12.2 million, respectively.

The following table summarizes the University's capital assets, net of accumulated depreciation, as of September 30:



<b>Capital Assets, Net</b>			
	<u>2014</u>	<u>2013</u>	<u>2012</u>
Land	\$ 7,591,148	\$ 7,552,605	\$ 3,960,290
Land improvements and infrastructure, net	7,636,800	6,835,293	4,154,200
Buildings and building improvements, net	210,321,979	191,163,946	179,875,917
Equipment, net	11,021,764	11,441,690	11,258,269
Library books, net	1,752,622	1,989,054	2,299,817
Computer software, net	443,752	737,727	1,031,702
Collections	1,124,402	1,124,402	510,305
	<u>\$ 239,892,467</u>	<u>\$ 220,844,717</u>	<u>\$ 203,090,500</u>
Total capital assets, net	<u>\$ 239,892,467</u>	<u>\$ 220,844,717</u>	<u>\$ 203,090,500</u>

Major capital additions during FY 2014 included construction of the Severe Weather Institute and Radar & Lightning Laboratory, completion of the Student Life Center, completion of phase II of the Campus Greenway, expansion and renovation of the Nursing Building, and renovations in Wilson Hall, Frank Franz Hall, Salmon Library and Roberts Hall.

Major capital additions during FY 2013 included the construction of the Student Life Center, the Campus Greenway, and the Nursing Building renovations.

Major capital additions during FY 2012 included the Student Life Center and athletics improvements.

Additional information about the University's capital assets is presented in Note 5 to the financial statements.

### Debt

The following table summarizes outstanding debt by type, as of September 30:

<b>Debt</b>			
	<u>2014</u>	<u>2013</u>	<u>2012</u>
Bonds - Current	\$ 4,330,000	\$ 4,235,000	\$ 3,450,000
Bonds - Long Term	101,706,000	106,036,000	78,266,000
Notes - Current	368,600	368,600	-
Notes - Long Term	1,105,800	1,474,400	-
(Discount) or Premium	272,278	282,200	(311,500)
<b>Total debt outstanding</b>	<u><b>\$107,782,678</b></u>	<u><b>\$112,396,200</b></u>	<u><b>\$ 81,404,500</b></u>

Principal and interest on these revenue bonds are collateralized by a pledge of revenues produced by student housing and student tuition and fees.

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

Changes in total net position as presented on the statements of net position are based on the activity presented in the statements of revenues, expenses, and changes in net position, which reflect the University's results of operations. This presents the revenues, both operating and nonoperating, along with the increase/decrease in net position. State appropriations are nonoperating because they are provided by the State Legislature to the University without the Legislature directly receiving commensurate goods and services in return for those revenues. Without the nonoperating revenues, in particular the state appropriations, the University would not be able to cover its costs of operations. These sources are critical to the University's financial stability and directly impact the quality of its programs.

A summarized comparison of the University's revenues, expenses and changes in net position for the years ended September 30 is as follows:

<b>Summary of Statements of Revenues, Expenses, and Changes in Net Position</b>			
	<u><b>2014</b></u>	<u><b>2013</b></u>	<u><b>2012</b></u>
Operating revenues:			
Tuition and fees	\$ 72,713,243	\$ 69,207,640	\$ 68,218,529
Less: scholarship allowances	(19,244,242)	(18,612,696)	(18,185,728)
Tuition and fees, net	53,469,001	50,594,944	50,032,801
Federal, state and private grants and contracts	91,029,643	97,951,418	89,660,258
Sales and services of educational departments	3,678,370	3,530,514	3,451,345
Auxiliary, net of \$1,071,576 in 2014 and \$1,030,817 in 2013 of scholarship allowances	6,686,732	6,135,066	6,718,898
Total operating revenues	154,863,746	158,211,942	149,863,302
Operating expenses	208,922,729	207,551,745	195,630,564
Operating loss	(54,058,983)	(49,339,803)	(45,767,262)
Nonoperating revenues (expenses):			
State educational appropriations	43,102,390	42,710,964	43,240,587
Private gifts	3,172,745	4,043,840	6,020,498
Net investment income	6,926,302	6,334,687	9,961,393
Pell grant revenue	7,395,098	7,615,679	8,118,163
State fiscal stabilization funds	-	-	(1,442)
Legal settlement	-	-	4,665
Loss on disposal of capital assets	(1,461,846)	(276,840)	(559,937)
Interest expense	(3,454,765)	(2,435,540)	(3,345,280)
Capital gifts and grants	28,000	637,197	1,175,333
Net nonoperating revenues	55,707,924	58,629,987	64,613,980
Increase in net position	1,648,941	9,290,184	18,846,718
Net position, beginning of year	294,879,582	285,589,398	266,742,680
<b>Net position, end of year</b>	<b>\$296,528,523</b>	<b>\$294,879,582</b>	<b>\$ 285,589,398</b>

Approximately \$43.1 million in state appropriations were received in FY 2014, an increase of 0.9% or \$391 thousand from the prior year.

Gross tuition and fees increased approximately \$3.5 million in FY 2014. The tuition rate increased by 4.53% for the 2013-2014 academic year. Fall 2014 tuition remained constant as compared to Fall 2013. Enrollment declined by 3.4% in Fall 2013, followed by slight declines in Spring, Summer and Fall 2014. With the implementation of phased-in, block tuition starting in Fall 2014, full-time undergraduate students paid slightly less tuition than in 2013. The \$1.0 and \$5.5 million increases in FY 2013 and 2012 were the result of tuition increases. The following is a summary of revenues by source (both operating and nonoperating) for the years ended September 30. Significant recurring sources of the University's revenues, such as state appropriations, are considered nonoperating, as defined by GASB Statement No. 35, *Basic Financial Statements-Management's Discussion and Analysis – for Public Colleges and Universities*.

Revenue Sources						
	2014		2013		2012	
State educational appropriations	\$43,102,390	20.0%	\$42,710,964	19.5%	\$43,240,587	19.8%
Net investment income	6,926,302	3.2%	6,334,687	2.9%	9,961,393	4.6%
Grants and contracts	91,029,643	42.2%	97,951,418	44.6%	89,660,258	41.0%
Gifts	3,172,745	1.5%	4,043,840	1.9%	6,020,498	2.8%
Auxiliary	6,686,732	3.1%	6,135,066	2.8%	6,718,898	3.1%
Net tuition and fees	53,469,001	24.8%	50,594,944	23.0%	50,032,801	22.9%
Sales and services	3,678,370	1.7%	3,530,514	1.6%	3,451,345	1.6%
Capital gifts and grants	28,000	0.0%	637,197	0.3%	1,175,333	0.5%
Legal settlement	-	0.0%	-	0.0%	4,665	0.0%
Pell grants	7,395,098	3.5%	7,615,679	3.5%	8,118,163	3.7%
State fiscal stabilization funds	-	0.0%	-	0.0%	-1,442	0.0%
<b>Total revenues</b>	<b>\$215,488,281</b>		<b>\$219,554,309</b>		<b>\$218,382,499</b>	

Investments produced positive income for FY 2014, 2013, and 2012. Fluctuations between years are due primarily to changing market conditions.

Grants and contracts decreased \$6.9 million in FY 2014. The decline can be traced largely to a \$5.0 million pass-through federal contract for 2013 that was not renewed in 2014. Grants and contracts increased \$8.3 million and \$8.2 million in FY 2013 and 2012, respectively, primarily due to an increase in federal grants and contracts awarded.

The University received gifts totaling \$3.2 million in FY 2014, compared to \$4.0 million in FY 2013. FY 2012 was an exceptional year at \$6.0 million due primarily to a single donor gift of \$3.7 million.

The University's auxiliary activities are comprised primarily of the Bevill Conference Center and Hotel, food service, housing, and bookstore. Auxiliary activities increased \$552 thousand in FY 2014. Auxiliary activities decreased slightly by \$584 thousand in FY 2013. Auxiliary activities decreased \$1.5 million in FY 2012 due to the Bevill Center,

housing, bookstore and food service all experiencing a decline in revenue and changes in mandatory food and housing policies.

As fees were held flat, Sales and services revenue was stable for FY 2014 and FY 2013. Sales and services decreased \$1.8 million in the year ended September 30, 2012 primarily due to a prior year one-time \$1.5 million food service payment from the University's externally-contracted provider.

Capital gifts and grants decreased \$609 thousand during 2014 mainly due to a decrease in onetime capital asset gifts received in FY 2014 and 2013. Capital gifts and grants decreased \$538 thousand during 2013 mainly due to a decrease in onetime capital asset gifts received in FY 2013 and 2012. Capital gifts and grants decreased \$380 thousand during FY 2012 mainly due to the difference in value assigned to onetime capital asset gifts received in FY 2012 and 2011.

The University receives grant and contract revenue from federal, state and local governments and private agencies. These funds are used to further the mission of the University: research, education, and public service. These funds are recorded as operating revenues. The following chart reflects the funding sources for federal operating grant and contract revenue for the years ended September 30:

<b>Detail of Federal Grants &amp; Contracts Revenue</b>			
	<u>2014</u>	<u>2013</u>	<u>2012</u>
National Aeronautics and Space Administration	\$ 21,140,998	\$ 20,598,336	\$ 20,113,728
Department of Defense	50,183,241	58,534,186	53,552,714
National Science Foundation	3,227,998	5,617,878	3,278,044
Department of Education	585,406	425,351	337,118
Other	4,764,922	5,477,619	6,455,179
<b>Total</b>	<b>\$ 79,902,565</b>	<b>\$ 90,653,370</b>	<b>\$ 83,736,783</b>

Department of Defense revenues decreased \$8.4 million in FY 2014 primarily due to a \$5.0 million pass-through contract for 2013 that was not renewed for 2014. Department of Defense revenues increased \$5.0 million and \$7.9 million in FY 2013 and 2012 respectively, primarily due to an increase in Army contracts.

National Science Foundation revenues decreased \$2.4 million in FY 2014 primarily due to the completion of the \$1.0 million ESPCOR Research and the \$776 thousand Education contract received in FY 2013. National Science Foundation revenues increased \$2.3 million in FY 2013 primarily due to a \$1 million EPSCOR Research and Education contract and a \$776 thousand ARRA Alabama Cyber Connection Grant. National Science Foundation revenues increased \$863 thousand in FY 2012.

The following is a comparison of the University’s operating expenses for the years ended September 30:

<b>Operating expenses (by functional classification)</b>			
	<b><u>2014</u></b>	<b><u>2013</u></b>	<b><u>2012</u></b>
Instruction	\$ 52,052,721	\$ 48,871,266	\$ 50,230,099
Research	74,757,309	81,743,099	76,373,523
Public service	5,638,106	4,822,320	2,769,564
Academic support	10,830,804	9,815,843	9,203,532
Student services	14,590,093	13,796,950	12,963,863
Institutional support	19,218,556	18,048,016	15,618,176
Operations and maintenance of plant	13,267,827	12,481,938	11,675,038
Scholarships and fellowships	1,101,624	1,090,063	606,364
Auxiliary enterprises	4,407,374	4,465,484	4,018,964
Depreciation	13,058,315	12,416,766	12,171,441
<b>Total operating expenses</b>	<b><u>\$ 208,922,729</u></b>	<b><u>\$ 207,551,745</u></b>	<b><u>\$ 195,630,564</u></b>
<b>Operating expenses (by natural classification)</b>			
Compensation and benefits	\$ 151,092,560	\$ 143,546,057	\$ 136,791,650
Supplies and services	43,670,230	50,498,859	46,061,109
Depreciation	13,058,315	12,416,766	12,171,441
Scholarships and fellowships	1,101,624	1,090,063	606,364
<b>Total operating expenses</b>	<b><u>\$ 208,922,729</u></b>	<b><u>\$ 207,551,745</u></b>	<b><u>\$ 195,630,564</u></b>

In FY 2014, instruction expenses increased \$3.2 million primarily due to an increase in compensation and benefits. In FY 2013, instruction expenses decreased \$1.4 million primarily due to a decrease in supplies and services expenses. In FY 2012, instruction expenses decreased \$2.6 million primarily due to the end of the American Recovery and Reinvestment Act of 2009 funding.

Research expenses decreased \$7.0 million in FY 2014 primarily due to decreases in contracts and grants. Research expenses increased \$5.4 million and \$4.2 million in FY 2013 and 2012, respectively, primarily due to increases in contracts and grants.

Public service expenses increased \$816 thousand, \$2.1 million and \$1.5 million in FY 2014, 2013 and 2012, respectively, due to increases in federal public service contracts and grants.

Academic support increased \$1.0 million during FY 2014. Academic support saw a slight increase of \$612 thousand during FY 2013. Academic support decreased \$1.7 million during FY 2012 due to a prior year write-off of electronic databases.

Operations and maintenance of plant was stable during FY 2014 and 2013. Operations and maintenance of plant increased \$4.0 million during FY 2012 primarily due to

increases in utilities costs and other services, as well as the expiration of funding from the American Recovery and Reinvestment Act of 2009.

The increase in compensation and benefits of \$7.5 million, \$6.8 million and \$1.2 million in FY 2014, 2013 and 2012, respectively, was primarily due to annual merit based salary increases and increases in retirement, health insurance and other benefit costs.

Scholarships and fellowships expense increased \$12 thousand for FY 2014. Scholarships and fellowships expense decreased \$484 thousand for FY 2013. Scholarships and fellowships expenses decreased \$680 thousand for FY 2012. Scholarships and fellowships expenses represent the residual expense after applying the scholarship allowance to gross tuition and fees revenue. The scholarship allowance represents the discount applied to student accounts for internal scholarships and financial aid, including pell grant assistance that is reported as nonoperating revenue.

In FY 2014, supplies and services expenses decreased \$6.8 million due to the decline in federal contracts and grants. Supplies and services expenses increased \$4.4 million and \$2.4 million in FY 2013 and 2012 due to the University's continued growth.



## Statements of Cash Flows

The statements of cash flows present the significant sources and uses of cash. The University's cash, primarily held in demand deposit accounts, is minimized by sweeping available cash balances into investment accounts. The following is a condensed statements of cash flows for the years ended September 30:

<b>Condensed Statements of Cash Flows</b>		
	<b>2014</b>	<b>2013</b>
Cash received from operations	\$ 154,250,713	\$ 156,770,533
Cash payments for operations	(194,153,566)	(193,583,419)
Net cash used in operating activities	(39,902,853)	(36,812,886)
Net cash used in capital and related financing activities	(39,725,132)	(1,698,298)
Net cash used in investing activities	(1,166,778)	(6,387,141)
Net cash provided by noncapital financing activities	55,552,796	54,128,097
Net increase in cash and cash equivalents from other than operating activities	14,660,886	46,042,658
Net increase in cash	(25,241,967)	9,229,772
Cash and cash equivalents, beginning of year	57,026,086	47,796,314
Cash and cash equivalents, end of year	<u>\$ 31,784,119</u>	<u>\$ 57,026,086</u>

The University used \$39.9 million of cash for operating activities in FY 2014, offset by \$55.6 million of cash provided by noncapital financing activities. Similarly, in FY 2013, \$36.8 million of cash used for operating activities was offset by \$54.1 million in cash provided by noncapital financing activities. Noncapital financing activities, as defined by GASB, include state educational appropriations and gifts received for other than capital purposes that are used to support operating expenses. The increase in cash provided by noncapital financing activities was due mainly to an increase in private gifts.

Cash of \$39.7 million and \$1.7 million in FY 2014 and 2013, respectively, was used for capital and related financing activities, primarily for purchases of capital assets and principal and interest payments.

Cash used in investing activities totaled \$1.2 million in FY 2014. Cash used in investing activities totaled \$6.4 million in FY 2013. The change is primarily the result of investments made to the System Prime Fund during FY 2013.

### Economic Factors That Will Affect the Future

The University's state educational appropriations have not kept pace with the amounts recommended by the Alabama Commission on Higher Education (ACHE). For FY 2014, the University was funded at approximately 56.1% of the ACHE funding recommendation.

State appropriations at the University have been reduced from \$58.1 million in FY 2008 to \$43.1 million in FY 2014. Not surprisingly, the state appropriations received by UAH as a percent of the ACHE funding recommendation has been reduced from 78% in FY 2008 to 56.1% in FY 2014. The University utilizes savings from previous years to fund non-recurring expenditures, primarily in the areas of information technology infrastructure and various facilities renewal projects.

The University continues to attract additional federal grant and contract revenue. About 89% of the University's federal operating revenue comes from two agencies: the National Aeronautical and Space Administration and the Department of Defense. The outcome of the federal budget process has important ramifications for the University's research budget.

The University's achievement in sustaining private and federal support is a testament to the high regard in which the University is held. The level of support underscores the continued confidence among donors and grantors in the quality of the University's programs and the importance of its mission. The University must have a balanced array of many categories of facilities to meet its educational, research and public service goals and continues to assess long-term capital requirements. Support for the University's recent capital expenditures has been provided primarily from federal funds, bond issues repaid through student tuition and fees, rental and facility fees, and gifts.



### **Requests for Information**

These financial statements are designed to provide a general overview of the University and its component unit's financial activities and to demonstrate the University's accountability. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Office of Accounting and Financial Reporting, The University of Alabama in Huntsville, 301 Sparkman Drive, Huntsville, Alabama 35899.



# FINANCIAL STATEMENTS



**THE UNIVERSITY OF ALABAMA IN HUNTSVILLE**  
**STATEMENTS OF NET POSITION**  
**September 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Assets</b>		
Current Assets:		
Cash and cash equivalents	\$ 31,104,680	\$ 39,038,391
Operating investments	75,903,732	79,970,449
Accounts receivable, net	29,035,339	28,905,228
Other current assets	9,096,833	7,994,178
Total current assets	<u>145,140,584</u>	<u>155,908,246</u>
Noncurrent Assets:		
Restricted cash and cash equivalents	679,439	660,436
Endowment investments	30,699,638	27,595,094
Cash and investments for capital activities	42,264,500	50,567,259
Capital assets, net	239,892,467	220,844,717
Legal settlement receivable	951,113	1,855,729
Other noncurrent assets	171,882	219,742
Total noncurrent assets	<u>314,659,039</u>	<u>301,742,977</u>
<b>Total Assets</b>	<b><u>\$ 459,799,623</u></b>	<b><u>\$ 457,651,223</u></b>
<b>Liabilities and Net Position</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 23,214,476	\$ 18,565,766
Unearned revenues	28,689,929	28,444,114
Current portion of long-term debt	4,698,600	4,603,600
Deposits held for others	3,584,017	3,365,561
Total current liabilities	<u>60,187,022</u>	<u>54,979,041</u>
Noncurrent Liabilities:		
Long-term debt	103,084,078	107,792,600
Total noncurrent liabilities	<u>103,084,078</u>	<u>107,792,600</u>
<b>Total Liabilities</b>	<b><u>163,271,100</u></b>	<b><u>162,771,641</u></b>
Net Position:		
Invested in capital assets, net of related debt	128,446,531	124,034,324
Restricted:		
Nonexpendable	9,368,566	9,055,754
Expendable	9,951,078	9,051,983
Unrestricted	148,762,348	152,737,521
<b>Total Net Position</b>	<u>296,528,523</u>	<u>294,879,582</u>
<b>Total Liabilities and Net Position</b>	<b><u>\$ 459,799,623</u></b>	<b><u>\$ 457,651,223</u></b>

See accompanying notes to financial statements

**UNIVERSITY OF ALABAMA HUNTSVILLE FOUNDATION  
DISCRETELY PRESENTED COMPONENT UNIT  
STATEMENTS OF FINANCIAL POSITION  
September 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
Cash and cash equivalents	\$ 3,266,094	\$ 1,744,903
Investments	40,609,815	39,613,466
Investment real estate	2,757,376	2,802,731
Investment in trust	5,189,629	5,374,203
Accrued interest	387,955	379,329
Pledges receivable, net	139,736	225,948
Trust receivable	484,959	484,959
Related party receivable	1,474,400	1,883,950
Income tax receivable	-	120,794
<b>Total Assets</b>	<b><u>\$ 54,309,964</u></b>	<b><u>\$ 52,630,283</u></b>
Accounts payable	\$ 15,277	\$ 41,986
Annuity payable	146,984	149,303
Payroll tax payable	4,162	4,177
<b>Total Liabilities</b>	<b><u>166,423</u></b>	<b><u>195,466</u></b>
Unrestricted Net Assets	23,415,891	22,870,815
Temporarily Restricted Net Assets	10,410,763	9,483,117
Permanently Restricted Net Assets	20,316,887	20,080,885
<b>Total Net Assets</b>	<b><u>54,143,541</u></b>	<b><u>52,434,817</u></b>
<b>Total Liabilities and Net Assets</b>	<b><u>\$ 54,309,964</u></b>	<b><u>\$ 52,630,283</u></b>

See Note 16



**THE UNIVERSITY OF ALABAMA IN HUNTSVILLE**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**  
**Years Ended September 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Operating Revenues</b>		
Tuition and fees	\$ 72,713,243	\$ 69,207,640
Less: scholarship allowances	<u>(19,244,242)</u>	<u>(18,612,696)</u>
Tuition and fees, net	53,469,001	50,594,944
Grants and contracts		
Federal	79,902,565	90,653,370
State	9,150,735	5,223,746
Private	1,976,343	2,074,302
Sales and services of educational departments	3,678,370	3,530,514
Auxiliary, net of \$1,071,576 in 2014 and \$1,030,817 in 2013 of scholarship allowances	<u>6,686,732</u>	<u>6,135,066</u>
<b>Total Operating Revenues</b>	<b><u>154,863,746</u></b>	<b><u>158,211,942</u></b>
<b>Operating Expenses</b>		
Compensation and benefits	151,092,560	143,546,057
Supplies and services	43,670,230	50,498,859
Depreciation	13,058,315	12,416,766
Scholarships and fellowships	<u>1,101,624</u>	<u>1,090,063</u>
<b>Total Operating Expenses</b>	<b><u>208,922,729</u></b>	<b><u>207,551,745</u></b>
Operating loss	(54,058,983)	(49,339,803)
<b>Nonoperating Revenues (Expenses)</b>		
State educational appropriations	43,102,390	42,710,964
Private gifts	3,172,745	4,043,840
Net investment income	6,926,302	6,334,687
Pell grant revenue	7,395,098	7,615,679
Loss on disposal of capital assets	(1,461,846)	(276,840)
Interest expense	<u>(3,454,765)</u>	<u>(2,435,540)</u>
<b>Net Nonoperating Revenues</b>	<b><u>55,679,924</u></b>	<b><u>57,992,790</u></b>
Capital gifts	<u>28,000</u>	<u>637,197</u>
	<b><u>55,707,924</u></b>	<b><u>58,629,987</u></b>
Increase in net position	1,648,941	9,290,184
Net Position, Beginning of Year	<u>294,879,582</u>	<u>285,589,398</u>
<b>Net Position, End of Year</b>	<b><u>\$ 296,528,523</u></b>	<b><u>\$ 294,879,582</u></b>

See accompanying notes to financial statements

**UNIVERSITY OF ALABAMA HUNTSVILLE FOUNDATION  
DISCRETELY PRESENTED COMPONENT UNIT  
STATEMENTS OF ACTIVITIES  
Years Ended September 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Changes in net position</b>		
<b>Revenue, gains, and other support:</b>		
Contributions	\$ 1,305,839	\$ 1,873,847
Rent income	39,117	26,366
Investment income	1,779,775	1,750,138
Unrealized gain/(loss) on investments	-	1,719,071
Realized gain/(loss) on sale of investments	1,497,134	-
Equity in earnings of trust	348,360	594,251
Other income	320,539	337,484
Change in allowance for uncollectibles	6,739	6,750
Change in value of split-interest agreement	71,009	16,894
<b>Total Revenues</b>	<u><b>5,368,512</b></u>	<u><b>6,324,801</b></u>
<b>Expenses:</b>		
Unrealized gain/(loss) on investments	\$ 147,051	-
Realized gain/(loss) on sale of investments	-	105,099
Contributions to UAH	1,851,421	2,380,977
Scholarships to UAH	1,236,547	1,221,737
Professional services	65,339	85,398
Income tax expense	211,131	306,200
Labor/Payroll expense	114,109	114,109
Other expenses	34,190	39,851
<b>Total Expenses</b>	<u><b>3,659,788</b></u>	<u><b>4,253,371</b></u>
Change in net position	1,708,724	2,071,430
Net Position, Beginning of Year	<u>52,434,817</u>	<u>50,363,387</u>
<b>Net Position, End of Year</b>	<u><b>\$ 54,143,541</b></u>	<u><b>\$ 52,434,817</b></u>

See Note 16



**THE UNIVERSITY OF ALABAMA IN HUNTSVILLE**  
**STATEMENTS OF CASH FLOWS**  
**Years Ended September 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Cash Flows from Operating Activities</b>		
Student tuition and fees	\$ 52,919,538	\$ 51,365,503
Federal grants and contracts	78,477,050	87,437,398
State and local grants and contracts	8,902,979	4,965,143
Private grants and contracts	1,922,834	1,971,613
Sales and services of educational and other departmental activities	4,952,753	2,862,834
Auxiliary enterprises	7,075,559	8,168,042
Payments to suppliers	(43,611,364)	(47,200,483)
Payments to employees and related fringes	(148,519,009)	(145,666,222)
Payments for scholarships and fellowships	(2,023,193)	(716,714)
Net Cash Used in Operating Activities	<u>(39,902,853)</u>	<u>(36,812,886)</u>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Proceeds from issuance of bonds	-	32,005,000
Proceeds from issuance of note payable	-	1,843,000
Purchase of capital assets	(31,074,731)	(28,952,466)
Proceeds from sale of capital assets	(77,478)	263,236
Principal payments on capital debt	(4,603,600)	(3,450,000)
Interest payments on capital debt	(3,969,323)	(3,407,068)
Net Cash Used in Capital and Related Financing Activities	<u>(39,725,132)</u>	<u>(1,698,298)</u>
<b>Cash Flows from Investing Activities</b>		
Income distributions from System investment pool	1,370,660	1,348,408
Proceeds from sales and maturities of other investments	3,153	15,002,758
Contributions to System investment pool	(2,540,591)	(22,738,307)
Net Cash Used in Investing Activities	<u>(1,166,778)</u>	<u>(6,387,141)</u>
<b>Cash Flows from Noncapital Financing Activities</b>		
State educational appropriations	43,102,390	42,710,964
Private gifts	4,536,825	3,084,760
Student direct lending receipts	27,906,543	28,230,308
Student direct lending disbursements	(28,466,907)	(28,425,788)
Amounts received from affiliates	244,939	123,341
Amounts paid to affiliates	(26,483)	(29,496)
Legal settlement	860,391	818,329
Pell grant revenue	7,395,098	7,615,679
Net Cash Provided by Noncapital Financing Activities	<u>55,552,796</u>	<u>54,128,097</u>
Net increase in cash and cash equivalents	(25,241,967)	9,229,772
Cash and Cash Equivalents, Beginning of Year	57,026,086	47,796,314
<b>Cash and Cash Equivalents, End of Year</b>	<u><b>\$ 31,784,119</b></u>	<u><b>\$ 57,026,086</b></u>
<b>Reconciliation of Cash and Cash Equivalents to the Statement of Net Position</b>		
Cash and cash equivalents in current assets	31,104,680	39,038,391
Cash and cash equivalents for capital activities	-	17,327,259
Restricted cash and cash equivalents	679,439	660,436
<b>Total Cash and Cash Equivalents</b>	<u><b>\$ 31,784,119</b></u>	<u><b>\$ 57,026,086</b></u>

See accompanying notes to financial statements

**THE UNIVERSITY OF ALABAMA IN HUNTSVILLE  
STATEMENTS OF CASH FLOWS -- Continued  
Years Ended September 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Reconciliation of Operating Loss to Net Cash Used in Operating Activities</b>		
Operating loss	\$ (54,058,983)	\$ (49,339,803)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization expense	13,096,253	13,612,848
Changes in allowance for doubtful accounts	(42)	126,060
Write-off of capital assets	-	725,506
Changes in assets and liabilities:		
Accounts receivable, net	(858,807)	(5,187,689)
Other current assets	(1,102,655)	292,947
Accounts payable and accrued liabilities	2,775,566	(662,796)
Deferred revenues	245,815	3,620,041
<b>Net Cash Used in Operating Activities</b>	<u>\$ (39,902,853)</u>	<u>\$ (36,812,886)</u>
 <b>Supplemental Noncash Activities Information</b>		
Loss on disposal of capital assets	\$ 1,461,846	\$ 276,840
Gift of capital assets	28,000	637,197
Capital assets acquired with a liability at year end	3,663,258	1,741,452

See accompanying notes to financial statements



**UAH Student Government Association, 2013-14**

**Notes to Financial Statements**  
**Years Ended September 30, 2014 and 2013**

**Note 1 – Organization and Summary of Significant Accounting Policies**

**Financial Reporting Entity** - The University of Alabama in Huntsville (the “University”) is one of three campuses of The University of Alabama System (the “System”), a discretely presented component unit of the State of Alabama. The financial statements of the University are intended to present the financial position, changes in financial position, and the cash flows of only that portion of the business type activities of the financial reporting entity of the System that is attributable to the transactions of the University. The financial statements include individual schools, colleges and departments, and certain affiliated operations determined to be a part of the University’s financial reporting entity. The System is recognized as an organization exempt from federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) of the Internal Revenue Code.

**Revision of Previously Issued Financial Statements** - During 2014, the University identified an error in its previously issued 2013 financial statements that resulted from the misclassification of restricted unspent bond proceeds as a component of Cash and cash equivalents as opposed to classification as a component of Cash and investments for capital activities. This error resulted in an overstatement of Cash and cash equivalents of approximately \$17.3 million and a corresponding understatement of Cash and investments for capital activities of \$17.3 million.

The University also identified a mathematical error in its determination of the Invested in capital assets, net of related debt category of Net position in its previously issued 2013 financial statements. This error resulted in an overstatement in Unrestricted net position as of September 30, 2013 of approximately \$2.2 million and an understatement of 2013 Invested in capital assets, net of related debt of approximately \$2.2 million.

The University’s management evaluated the impact of the errors on the previously issued financial statements and concluded that the impact was not material. The University revised the accompanying 2013 financial statements to correct these errors as follows:



	September 30, 2013		September 30, 2013	
	As Previously Reported	Adjustments	As Revised	
<b>Assets</b>				
<b>Current assets</b>				
Cash and cash equivalents	56,365,650	(17,327,259)	39,038,391	
<b>Total current assets</b>	<u>173,235,505</u>	<u>(17,327,259)</u>	<u>155,908,246</u>	
<b>Noncurrent assets</b>				
Cash and investments for capital activities	33,240,000	17,327,259	50,567,259	
<b>Total noncurrent assets</b>	<u>284,415,718</u>	<u>17,327,259</u>	<u>301,742,977</u>	
<b>Total assets</b>	<u>457,651,223</u>	-	<u>457,651,223</u>	
<b>Total liabilities</b>	<u>162,771,641</u>	-	<u>162,771,641</u>	
<b>Net Position:</b>				
Invested in capital assets, net of related debt	121,879,828	2,154,496	124,034,324	
Unrestricted	154,892,017	(2,154,496)	152,737,521	
<b>Total net position</b>	<u>294,879,582</u>	-	<u>294,879,582</u>	
<b>Total liabilities and net position</b>	<u>457,651,223</u>	-	<u>457,651,223</u>	
<b>Reconciliation of Cash and Cash Equivalents to the Statement of Net Position</b>				
	<b>September 30, 2013</b>		<b>September 30, 2013</b>	
	<b>Previously Reported</b>	<b>Adjustments</b>	<b>As Revised</b>	
Cash and cash equivalents in current assets	56,365,650	(17,327,259)	39,038,391	
Restricted cash and cash equivalents	660,436	-	660,436	
Cash for capital activities	-	17,327,259	17,327,259	
<b>Total Cash and Cash Equivalents</b>	<u>57,026,086</u>		<u>57,026,086</u>	

**Scope of Statements** - The University follows Governmental Accounting Standards Board (GASB) Statement Number 61, *The Financial Reporting Entity: Omnibus-an amendment of GASB Statements No. 14 and No. 34* ("GASB 61"). This Statement provides additional guidance in determining whether certain organizations affiliated with the University should be considered component units of the University for financial reporting purposes. The Statement also provides guidance on determining whether component units should be presented in the University's financial statements as "blended" or "discrete" components based on their relationship and organizational structure.

As defined by generally accepted accounting principles established by the GASB, the financial reporting entity consists of the University, as well as its discretely presented component unit, the University of Alabama Huntsville Foundation ("UAHF").

UAHF is a legally separate, tax-exempt component unit of the University. UAHF is organized exclusively for charitable, scientific, and educational purposes in order to benefit the University. UAHF is governed by a 34-member board of trustees. Although the University does not control the timing or amount of receipts from UAHF, the majority of resources or income that UAHF holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by UAHF can only be used by, or for the benefit of, the University, UAHF is considered a component unit of the University. UAHF is reported in separate financial statements because it does not meet the criteria to be blended with the University as described in GASB 61.

UAHF is a not-for-profit organization that reports its financial results under the Financial Accounting Standard Board (“FASB”) Statements. Most significant to UAHF’s operations and reporting model is Accounting Standards Codification (ASC) 958, *Not-for-Profit Entities*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to UAHF’s financial information in the University’s financial reporting entity for these differences; however, significant note disclosures (see Note 16) to UAHF’s financial statements have been incorporated into the University’s notes to the financial statements. During FY 2014 and 2013, UAHF distributed \$3,087,967 and \$3,602,714, respectively, to or for the University for both restricted and unrestricted purposes. Phone 256-824-6350 for complete financial statements for UAHF.

The University is also affiliated with the Eminent Scholars Foundation, Alabama Engineering Foundation and UAH Alumni Association. These entities’ resources are not significant to the University; therefore, they are not included as component units under GASB guidance.

**Basis of Accounting:** For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities as defined by GASB Statement No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities*, an amendment of GASB Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services. Accordingly, the financial statements of the University have been prepared in accordance with accounting principles generally accepted in the United States of America, as issued by the GASB, using the economic measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred.

**Net Position:** Net position is classified into the following four categories according to external donor restrictions or availability of assets for satisfaction of University obligations:

- **Invested in capital assets, net of related debt:** Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

- **Restricted:**

**Nonexpendable** – Net position subject to externally imposed stipulations that they be maintained permanently by the University. Such assets include the corpus of 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 that is not subject to externally imposed stipulations. Unrestricted net position may be designated for specific purposes by action of management. Substantially all unrestricted net position is designated for academic, research, and capital programs.

**Cash and Cash Equivalents:** For purposes of 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. Cash equivalents representing assets of the University's endowment, life income, and other long-term investments are included in the noncurrent investments category.

**Investments:** The University's investments are primarily reported at fair value. The University's investment portfolio is primarily invested in three separate investment pools maintained by The University of Alabama. Fair value for the investment pools is provided by the System, based on the fair value of the underlying investment securities held by each investment pool. Fair value of the underlying securities held in each investment pool is based on quoted market prices or dealer quotes, where available, or determined using net asset values provided by underlying investment partnerships or companies, which primarily invest in readily marketable securities. Certain real estate and non-readily marketable securities held in the System-sponsored Endowment Fund and Prime fund (Note 3) are carried at cost, unless impaired. Fair value for investments held directly by the University is determined from quoted market prices or market prices of similar instruments. Net investment income, including realized and unrealized gains and losses, is reported as nonoperating revenues (expenses) in the statements of revenues, expenses and changes in net position.

Investments are reported in three categories in the statement of net position. Investments recorded as endowment investments are those invested funds that cannot be used to fund current operations and thus are included in noncurrent assets. Investments for capital activities are included in noncurrent assets, except for amounts included in current assets to offset current construction-related payables. All other investments are included as operating investments.

**Accounts Receivable:** Accounts receivable consist primarily of tuition and fees charged to students, amounts due from the federal government, state and local governments, or private sources in connection with reimbursement of allowable expenditures made pursuant to the University's contracts and grants, and current amounts due to the University related to a legal settlement. Accounts receivable are recorded net of estimated uncollectible amounts.

**Capital Assets:** Capital assets are recorded at cost at the date of acquisition, or fair value at date of donation in the case of gifts, less accumulated depreciation. For

equipment, the University's capitalization policy includes all items with a unit cost of \$5,000 or more and an estimated useful life of greater than one year. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense was incurred. The University capitalizes certain software and development costs associated with obtaining and developing internal-use computer software. Implementation costs, which are capitalized, include consulting expenses and allocation of internal salaries and fringes for the core implementation team. Training costs are expensed as incurred.

Capital assets acquired through federal grants and contracts where the federal government retains a reversionary interest are capitalized and depreciated. Interest costs, net of any related investment earnings, for certain assets acquired with the proceeds of tax-exempt borrowings are capitalized as a component of the cost of acquiring those assets.

Depreciation of buildings and building improvements (5-40 years), land improvements and infrastructure (10 years), library collection (10 years), computer software (10 years) and inventoried equipment (5-8 years) is computed on a straight-line basis. The University computes depreciation for certain buildings and building improvements using a componentized method.

Collections are recognized as an asset on the accompanying statements of net position in accordance with GASB guidance. The University defines collections as works of art or similar assets that are held for public exhibition, education, or research in furtherance of public service rather than financial gain which are protected, kept unencumbered, cared for, and preserved. Collection items are recorded at cost as of the date of acquisition or at their appraised or fair value on the date of donation in the case of gifts. Gains or losses from the sale of collection items are reflected on the statement of revenues, expenses, and changes in net assets as changes in the appropriate net asset classes, depending on the existence and type of donor-imposed restrictions.

**Unearned Revenues:** Unearned revenues consist primarily of amounts received for fall semester student tuition and fees and housing fees that are not earned until the next fiscal year. Unearned revenues also include amounts received from grant and contract sponsors that have not yet been earned.

**Revenues:** The University's policy for defining operating activities as reported on the statement of revenues, expenses, and changes in net position are those that generally result from exchange transactions such as payments received for providing services and payments made for services or goods received. Nearly all of the University's operating revenues are from exchange transactions. Certain significant revenue streams relied upon to support operations are recorded as nonoperating revenues, as defined by GASB guidance, including state educational appropriations, private gifts for other than capital purposes, investment income, and Federal Pell Grants.

Auxiliary enterprise revenues are generated primarily by University Housing.

Revenues received for capital activities are considered neither operating nor nonoperating activities, and are presented after nonoperating activities on the accompanying statement of revenues, expenses, and changes in net position.

**Contract and Grant Revenue:** The University receives contract and grant revenues from governmental and private sources. The University recognizes revenues associated with the sponsored programs in accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, based on the terms of the individual contract or grant.

**Scholarship Allowances and Student Aid:** Scholarship allowances applied to student accounts are recorded as an offset to student tuition and fees and auxiliary revenue. Payments of financial aid made directly to students are classified as scholarship and fellowship expenses.

**Internal Sales Activities:** All internal sales activities to the University departments from sales and service units (motor pool, postal services, telecommunications, etc.) have been eliminated in the accompanying financial statements.

**Compensated Absences:** The University accrues annual leave for employees at rates based upon length of service and job classification and compensatory time based upon job classification and years worked.

**Endowment Spending:** For donor restricted endowments, the Uniform Prudent Management of Institutional Funds Act (UPMIFA), as adopted in Alabama, permits The Board of Trustees of the University of Alabama (the Board) to appropriate an amount of realized and unrealized endowment appreciation as the Board determines to be prudent. UPMIFA also prescribes the guidelines for the expenditure of donor-restricted endowment funds in the absence of overriding, explicit donor stipulations. UPMIFA focuses on the entirety of a donor-restricted endowment fund, that is, both the original gift amount(s) and net appreciation. UPMIFA includes a robust set of guidelines about what constitutes prudent spending, explicitly requiring consideration of the duration and preservation of the fund. The University's policy is to retain the endowment realized and unrealized appreciation with the endowment after the spending rate distributions in a manner consistent with the standards of prudence prescribed by UPMIFA. The Board approved a spending rate for FY 2014 and 2013 of 5.0% of a trailing three-year average of the market (unit) value.

**Pledges:** The University receives pledges and bequests of financial support. Revenue is recognized when a pledge representing an unconditional promise to give is received and all eligibility requirements, including time requirements, have been met. In the absence of such a promise, revenue is recognized when the gift is received. Pledges are recorded at their gross, undiscounted amount, net of a reasonable provision for doubtful accounts. Endowment pledges do not meet eligibility requirements and are not recorded as assets until the related gift is received. Due to uncertainties with regard to their realization and valuation, bequest intentions and other conditional promises are not recognized as assets

until the specified conditions are met. The University's trust policies do not differ in nature from endowment policies.

**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 amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

## **Note 2 - Cash**

The Board approves, by resolution, all banks or other financial institutions utilized as depositories for University funds. Prior to approval, each proposed depository must provide evidence of its designation by the Alabama State Treasurer as a qualified public depository under the Security of Alabama Funds Enhancement Act (SAFE). From time to time, the Board may request that the depository provide evidence of its continuing designation as a qualified public depository. Under the mandatory SAFE program, each qualified public depository (QPD) is required to hold collateral for all its public depositories on a pooled basis in a custody account established for the State Treasurer as SAFE administrator. In the unlikely event a public entity should suffer a deposit loss due to QPD insolvency or default, a claim form would be filed with the State Treasurer who would use the SAFE pool collateral or other means to reimburse the loss.

The System maintains a short-term investment pool for the System entities to invest operating cash reserves. The Short-Term Fund is invested in a treasury obligation money market fund managed by Federated investors. For FY 2014 and 2013, the University had approximately \$3.2 million and \$22.2 million in the Short-Term Fund, all of which was invested in the money market fund. The assets held in the money market fund are presented in cash and cash equivalents.

For FY 2014 and 2013, the University had cash and cash equivalents totaling \$31,784,119 and \$57,026,086 respectively. Included in the amounts are deposits with trustees held for reserves, which totaled \$679,439 in FY 2014 and \$660,436 in FY 2013. Also included in the amounts are unspent bond proceeds presented in cash and investments for capital activities, which totaled \$17,327,259 in FY 2013. There were no such unspent bond proceeds in FY 2014 at year end.

## **Note 3 – Investments**

The University invests its endowment funds in accordance with applicable limitations set forth in gift instruments, Board guidelines, or applicable laws. Also certain bond indentures require the University to invest the amounts held in specific construction funds, redemption funds, and bond funds in federal securities, eligible certificates, or eligible investments.

At September 30, 2014 and 2013, the University's investments included custodial credit risk category I investments (investments that are insured or registered, or securities held

by the University or its agent in the University's name) and other investments not categorized by risk category as follows:

	2014	2013
Category I:		
Time deposits	\$ 135,522	\$ 135,423
Not categorized:		
Mutual funds	44,985	44,247
System Short-term Fund	3,192,102	22,194,565
System Intermediate Fund	45,101,373	44,723,748
System Prime Fund	70,334,695	65,815,899
Pooled Endowment Fund	30,699,638	27,595,094
Agency Funds	2,551,657	2,491,132
Total Investments	<u>\$ 152,059,972</u>	<u>\$ 163,000,108</u>

The Board has the responsibility for the establishment of the investment policy and the oversight of the investments for the System and related entities. In order to facilitate System-wide investment objectives and achieve economies of scale, the Board has established four distinct investment pools based primarily on the projected investment time horizons for System funds. These investment pools are the Endowment Fund, Prime Fund, Intermediate Fund and the Short-Term Fund (collectively, the "System Pools"). Pursuant to Board investment policies, each System or related entity may include all or a portion of their investments within the System-sponsored investment pools. These investment funds are considered 'internal' investment pools under GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, with the assets pooled on a market value basis. Separately managed funds that are resident with each entity are to be invested consistent with the asset mix of the corresponding System investment pool. The following disclosures relate to both the System Pools, which include the investments of other System entities and other affiliated entities, and the University-specific investment portfolio.

**Endowment Fund:** The purpose of the Endowment Fund is to pool endowment and similar funds to support the System campuses, hospital and related entities in carrying out their respective missions over a perpetual time frame. Accordingly, the primary investment objectives of the Endowment Fund are to preserve the purchasing power of the principal and provide a stable source of perpetual financial support to the endowment beneficiaries. To satisfy the long-term rate of return objective, the Endowment Fund relies on a total return strategy in which investment returns are achieved through both capital appreciation and natural income. Asset allocation targets are established to meet the return objectives while providing adequate diversification in order to minimize investment volatility. As discussed in Note 1, the Endowment Fund invests in securities with non-readily determinable market values which are valued at cost, unless impaired. For FY 2014 and 2013, the portion of the University's investment in the Endowment Fund, reported at cost, is \$3,403,853 and \$3,167,391, respectively. The remainder of the investment is reported at fair value.

**Prime Fund:** The Prime Fund is a longer-term fund used as an investment vehicle to manage operating reserves with a time horizon of seven to ten years. This fund has an investment objective of growth and income and is invested in a diversified asset mix of liquid and semi-liquid securities. This fund is not currently invested in long-term lockup funds with illiquid assets. As discussed in Note I, certain investments within the Prime Fund are valued at cost, unless impaired. For FY 2014 and 2013, the University's portion of investments in the Prime fund, and measured at cost, totaled approximately \$784,000 and \$771,000, respectively. The remainder of the investment is reported at fair value.

**Intermediate Fund:** The Intermediate Fund serves as an investment vehicle to manage operating reserves with a time horizon of two to six years. This fund is also used to balance the other funds when looking at the System's entire asset allocation of operating reserves relative to its investment objectives. The Intermediate Fund has an investment objective of income with preservation of capital and is invested in intermediate-term fixed income securities. System policy states that at least one of the Intermediate Fund investment managers must be a large mutual fund providing daily liquidity.

**Short-Term Fund:** The Short-Term Fund contains the short term operating reserves of the various System entities. Because of the different income and disbursement requirements of each entity, consolidation of these funds reduces daily cash fluctuations and minimizes the amount of short-term cash reserves needed. Assets held in the Short-Term Fund are invested with the primary objective of stability of principal and liquidity. Such investments are restricted to high quality, liquid, money market funds and other fixed income obligations with a maturity of one year or less. Refer to Note 2 for additional information related to the Short-Term Fund.

At the September 2014 Investment Committee meeting of the Board of Trustees of The University of Alabama, the committee approved the consolidation of three working capital pools to two and a name change for these investment pools. The Intermediate Fund will be renamed the Short Term Liquidity Pool (STLP) and the Prime Investment Fund will be renamed the Long Term Reserve Pool (LTRP). The Short Term Fund (Federated Account) will become part of the Short Term Liquidity Pool. The name changes became effective for October 1, 2014.

Although the investment philosophy of the Board is to minimize the direct ownership of investment vehicles, preferring ownership in appropriate investment fund groups, there are certain direct investments that are held in the name of the Board. All other investments in the System Pools are classified as commingled funds.



The composition of the System's investments, by investment type for the System Pools, at September 30, 2014 and 2013 is as follows:

	ENDOWMENT FUND		PRIME FUND		INTERMEDIATE FUND		SHORT TERM FUND	
	2014	2013	2014	2013	2014	2013	2014	2013
<b>RECEIVABLES:</b>								
ACCRUED INCOME RECEIVABLES	\$ 1,003,301	\$ 1,096,967	\$ 881,205	\$ 651,549	\$ 3,704,124	\$ 4,056,788	\$ -	\$ -
<b>TOTAL RECEIVABLES</b>	<b>1,003,301</b>	<b>1,096,967</b>	<b>881,205</b>	<b>651,549</b>	<b>3,704,124</b>	<b>4,056,788</b>	<b>-</b>	<b>-</b>
<b>CASH EQUIVALENTS:</b>								
CERTIFICATES OF DEPOSIT	-	-	-	-	-	8,094,239	-	-
COMMERCIAL PAPER	-	-	-	-	-	2,599,751	-	-
OPTIONS	-	-	-	-	-	-	-	-
MONEY MARKET FUNDS	57,886,211	56,519,604	40,085,104	50,827,901	89,200,493	69,728,143	176,466,706	201,099,030
<b>TOTAL CASH EQUIVALENTS</b>	<b>57,886,211</b>	<b>56,519,604</b>	<b>40,085,104</b>	<b>50,827,901</b>	<b>89,200,493</b>	<b>80,422,133</b>	<b>176,466,706</b>	<b>201,099,030</b>
<b>EQUITIES:</b>								
U.S. COMMON STOCK	91,626,275	74,460,258	64,167,500	53,886,837	-	-	-	-
U.S. PREFERRED STOCK	1,081,641	1,238,188	970,703	1,125,625	-	-	-	-
NON-U.S. STOCK	9,122,500	10,624,062	7,016,834	6,771,037	-	-	-	-
<b>TOTAL EQUITIES</b>	<b>101,830,416</b>	<b>86,322,508</b>	<b>72,155,037</b>	<b>61,783,499</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>FIXED INCOME SECURITIES:</b>								
U.S. GOVERNMENT OBLIGATIONS	16,426,862	21,850,510	14,060,742	11,213,984	356,983,685	317,145,893	-	-
MUNICIPAL GOVERNMENT OBLIGATIONS	-	-	-	-	-	217,383	-	-
MORTGAGE BACKED SECURITIES	-	-	-	-	107,336,734	120,283,662	-	-
COLLATERALIZED MORTGAGE OBLIGATIONS	-	-	-	-	36,037,561	50,078,274	-	-
CORPORATE BONDS	32,525,649	59,987,039	25,320,584	30,751,076	243,885,772	343,033,010	-	-
NON-U.S. BONDS	4,717,740	-	3,586,194	-	86,740,041	1,046,990	-	-
<b>TOTAL FIXED INCOME SECURITIES</b>	<b>53,670,251</b>	<b>81,837,549</b>	<b>42,967,520</b>	<b>41,965,060</b>	<b>830,983,793</b>	<b>831,805,212</b>	<b>-</b>	<b>-</b>
<b>COMMINGLED FUNDS:</b>								
U.S. EQUITY FUNDS	70,497,226	102,773,998	90,049,678	110,668,279	-	-	-	-
NON-U.S. EQUITY FUNDS	299,154,328	280,637,986	277,766,811	259,399,547	-	-	-	-
U.S. BOND FUNDS	59,672,727	31,464,754	44,754,545	59,945,698	88,967,993	78,977,321	-	-
NON-U.S. BOND FUNDS	62,211,203	61,765,298	61,965,572	56,698,721	-	-	-	-
HEDGE FUNDS	237,682,807	153,064,178	196,514,795	120,473,011	-	-	-	-
PRIVATE EQUITY FUNDS	67,605,100	62,791,546	-	-	-	-	-	-
TIMBERLAND FUNDS	-	16,960	-	-	-	-	-	-
REAL ESTATE FUNDS	136,647,983	131,161,560	90,219,359	104,551,847	-	-	-	-
<b>TOTAL COMMINGLED FUNDS</b>	<b>933,471,374</b>	<b>823,676,280</b>	<b>761,270,760</b>	<b>711,737,103</b>	<b>88,967,993</b>	<b>78,977,321</b>	<b>-</b>	<b>-</b>
<b>TOTAL FUND INVESTMENTS</b>	<b>1,146,858,252</b>	<b>1,048,355,941</b>	<b>916,478,421</b>	<b>866,313,563</b>	<b>1,009,152,280</b>	<b>991,204,667</b>	<b>176,466,706</b>	<b>201,099,030</b>
<b>TOTAL FUND ASSETS</b>	<b>1,147,861,553</b>	<b>1,049,452,908</b>	<b>917,359,626</b>	<b>866,965,112</b>	<b>1,012,856,403</b>	<b>995,261,455</b>	<b>176,466,706</b>	<b>201,099,030</b>
<b>TOTAL FUND LIABILITIES</b>	<b>(254,559)</b>	<b>(122,926)</b>	<b>(175,311)</b>	<b>(85,447)</b>	<b>(566,898)</b>	<b>(584,144)</b>	<b>-</b>	<b>-</b>
<b>AFFILIATED ENTITY INVESTMENTS IN FUNDS</b>	<b>(147,147,272)</b>	<b>(138,865,562)</b>	<b>(56,162,298)</b>	<b>(53,288,957)</b>	<b>(106,232,340)</b>	<b>(88,296,301)</b>	<b>-</b>	<b>-</b>
<b>TOTAL NET ASSET VALUE</b>	<b>\$ 1,000,459,721</b>	<b>\$ 910,464,420</b>	<b>\$ 861,022,018</b>	<b>\$ 813,590,708</b>	<b>\$ 906,057,165</b>	<b>\$ 906,381,010</b>	<b>\$ 176,466,706</b>	<b>\$ 201,099,030</b>

**Investment Risk Factors:** There are many factors that can affect the value of investments. Some, such as custodial credit risk, concentration of credit risk and foreign currency risk, may affect both equity and fixed income securities. Equity securities respond to such factors as economic conditions, individual company earnings performance and market liquidity, while fixed income securities are particularly sensitive to credit risks and changes in interest rates.

**Credit Risk:** Fixed income securities are subject to credit risk, which is the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. These circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation, and/or adverse political developments. Certain fixed

income securities, primarily obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have significant credit risk. A bond's credit quality is an assessment of the issuer's ability to pay interest on the bond, and ultimately, to pay the principal. Credit quality is evaluated by one of the independent bond-rating agencies, for example Moody's Investors Service (Moody's) or Standard and Poor's (S&P). The lower the rating, the greater the chance - in the rating agency's opinion - that the bond issuer will default, or fail to meet its payment obligations. Generally, the lower a bond's credit rating, the higher its yield should be to compensate for the additional risk.

Board policy recognizes that a limited amount of credit risk, properly managed and monitored, is prudent and provides incremental risk adjusted return over its benchmark. Credit risk in each investment pool is managed primarily by diversifying across issuers and limiting the amount of portfolio assets that can be invested in non-investment grade securities. Fixed income holdings in a single entity (excluding obligations of the U.S. government and its agencies) may not exceed 5% of a manager's portfolio measured at market value. At least 95% of these fixed income investments must be in investment grade securities (securities with ratings of BBB- or Baa3) or higher. However, multi-strategy fixed income managers may have up to 20% of their investments in non-investment grade securities. Securities of foreign entities denominated in U.S. dollars are limited to 10% of a manager's portfolio. Securities denominated in currencies other than U.S. dollars are not permissible unless part of a multi-strategy fixed income account where the limitation is 20% of the manager's portfolio.

The investment policy recognizes that credit risk is appropriate in balanced investment pools such as the Endowment and Prime Funds, which are tracked against the Barclays Government Credit Index for U.S. investments and the Citigroup WGBI Index for international investment benchmarks for the fixed income portion of these pools. Fixed income investments within the Endowment and Prime Funds include corporate and U.S. treasury and/or agency bonds with a minimum BBB- rating and an average duration of four years. In addition, approximately \$1,500,000 and \$0 in the Endowment and Prime Funds, for FY 2014 and 2013, is invested in unrated fixed income securities, excluding fixed income commingled funds. Fixed income commingled funds were approximately \$326,600,000 and \$317,200,000 in the Endowment and Prime Funds, for FY 2014 and 2013, respectively.

The Intermediate Fund is benchmarked against the 1-3 year Barclays Government Credit Index with funds invested with four separate fund managers. Fixed income investments include corporate, mortgage backed, asset backed, collateralized mortgage and U.S. treasury and/or agency bonds with a minimum rating of BB or higher. For FY 2014 and 2013, respectively, approximately \$64,900,000 and \$135,800,000 was invested by the Intermediate Fund in unrated fixed income securities, excluding commingled bond funds, money market funds and commercial paper. Fixed income commingled funds and commercial paper totaled approximately \$178,200,000 and \$151,300,000 for FY 2014 and 2013, respectively.

For FY 2014 and 2013, \$0 and \$8,100,000, respectively, was invested by the Intermediate Fund in certificates of deposit.

The Short-Term Fund is committed to immediate liquidity to meet the operating needs of the System campuses and hospital. The Short-Term Fund is invested in a money market fund, which in turn invests mostly in U.S. Treasury securities and repurchase agreements that are collateralized by U.S. Treasury securities. These funds are all commingled with funds of other investors. Refer to Note 2 for additional information related to the Short-Term Fund.

The credit risk for fixed and variable income securities, for the System Pools, at September 30, 2014 and 2013 are as follows:

	ENDOWMENT FUND		PRIME FUND		INTERMEDIATE FUND		SHORT TERM FUND	
	2014	2013	2014	2013	2014	2013	2014	2013
Fixed or Variable Income Securities								
U.S. Government Obligations	\$ 16,426,862	\$ 21,850,510	\$ 14,060,742	\$ 11,213,984	\$ 356,983,685	\$ 317,145,893	\$ -	\$ -
Municipal Government Obligations	-	-	-	-	-	217,383	-	-
Other U.S. and Non-U.S. Denominated:								
AAA		1,254,938		642,291	48,981,389	18,861,309	-	-
AA	6,632,713	11,441,938	5,082,925	5,792,481	83,143,881	85,433,796	-	-
A	16,894,747	27,814,947	13,410,517	14,242,504	151,341,278	182,513,978	-	-
BBB	12,850,553	19,475,216	9,766,791	10,073,800	84,810,054	78,670,892	-	-
BB		-	-	-	29,352,911	6,740,499	-	-
B	-	-	-	-	8,810,464	3,613,132	-	-
C and < C	-	-	-	-	2,648,442	2,818,596	-	-
Unrated	865,375	-	646,545	-	64,911,689	135,789,735	-	-
Commingled Funds:								
U.S. Bond Funds: Unrated	59,672,727	31,464,754	44,754,545	59,945,698	88,967,993	78,977,321	-	-
Non-U.S. Bond Funds: Unrated	62,211,203	61,765,298	61,965,572	56,698,721	-	-	-	-
Money Market Funds: Unrated	57,886,211	56,519,604	40,085,105	50,827,901	89,200,493	69,728,143	176,466,706	201,099,030
Commercial Paper: Unrated	-	-	-	-	-	2,599,751	-	-
Certificate of Deposits	-	-	-	-	-	8,094,239	-	-
<b>TOTAL</b>	<b>\$ 233,440,391</b>	<b>\$ 231,587,205</b>	<b>\$ 189,772,742</b>	<b>\$ 209,437,380</b>	<b>\$ 1,009,152,279</b>	<b>\$ 991,204,667</b>	<b>\$ 176,466,706</b>	<b>\$ 201,099,030</b>

**Custodial Credit Risk:** Custodial credit risk is the risk that in the event of the corporate failure of the custodian, the System's investment securities may not be returned. Investment securities in the System Pools are registered in the Board's name by the custodial bank as an agent for the System. Other types of investments (i.e. open-ended mutual funds, money market funds) represent ownership interests that do not exist in physical or book-entry form. As a result, custodial credit risk is remote.

**Concentration of Credit Risk:** Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers, thereby exposing the organization to greater risks resulting from adverse economic, political, regulatory, geographic, or credit developments. As previously mentioned, credit risk in each investment pool is managed primarily by diversifying across issuers and limiting the amount of portfolio assets that can be invested in non-investment grade securities. As of FY 2014 and 2013, there was no investment in a single issuer that represents 5% or more of total investments held by any single investment manager of the System Pools, except for investments issued by the U.S. government and money market fund investments held by the Short Term Fund.

**Interest Rate Risk:** Interest rate risk is the risk that the value of fixed income securities will decline because of changing interest rates. The prices of fixed income securities with a longer time to maturity, measured by effective duration, tend to be more sensitive to changes in interest rates and, therefore, more volatile than those with shorter durations. Effective duration is the approximate change in price of a security resulting from a 100 basis point (1 percentage point) change in the level of interest rates. It is not a measure of time. The Board does not have a specific policy relative to interest rate risk. As such, there are no restrictions on weighted average maturity for each portfolio as they are managed relative to the investment objectives and liquidity demands of the investors.

The effective durations for fixed or variable income securities, for the System Pools, for FY 2014 and 2013 are as follows:

	ENDOWMENT FUND		PRIME FUND		INTERMEDIATE FUND	
	2014	2013	2014	2013	2014	2013
U.S. GOVERNMENT OBLIGATIONS	7.1	5.6	6.5	5.4	3.2	1.8
MUNICIPAL GOVERNMENT OBLIGATIONS	0.0	0.0	0.0	0.0	0.0	0.2
CORPORATE BONDS	3.8	4.2	3.8	4.2	1.9	1.5
NON-US BONDS	0.0	0.0	0.0	0.0	1.9	1.5
COMMINGLED BOND FUNDS	2.3	1.5	2.2	2.3	2.8	2.3

The information presented does not take into account the relative weighting of the portfolio components to the total portfolio.

Investments may also include mortgage pass through securities and collateralized mortgage obligations that may be considered to be highly sensitive to changes in interest rates due to the existence of prepayment or conversion features. For FY 2014 and 2013, the fair market value of these investments for the System Pools, are as follows:

	ENDOWMENT FUND		PRIME FUND		INTERMEDIATE FUND	
	2014	2013	2014	2013	2014	2013
MORTGAGE BACKED SECURITIES	\$ -	\$ -	\$ -	\$ -	\$ 107,336,734	\$ 120,283,662
COLLATERALIZED MORTGAGE OBLIGATIONS	-	-	-	-	36,037,561	50,078,274
TOTAL FIXED	\$ -	\$ -	\$ -	\$ -	\$ 143,374,296	\$ 170,361,936

**Mortgage Backed Securities:** These securities are issued by the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae) and Federal Home Loan Mortgage Association (Freddie Mac) and include short embedded prepayment options. Unanticipated prepayments by the obligees of the underlying asset reduce the total expected rate of return.

**Collateralized Mortgage Obligations:** Collateralized mortgage obligations (CMOs) generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.

For FY 2014 and 2013 the effective durations for these securities are as follows:

	ENDOWMENT FUND		PRIME FUND		INTERMEDIATE FUND	
	2014	2013	2014	2013	2014	2013
MORTGAGE BACKED SECURITIES	-	-	-	-	1.3	0.7
COLLATERALIZED MORTGAGE OBLIGATIONS	-	-	-	-	1.0	1.0

**Foreign Currency Risk:** The strategic asset allocation policy for the Endowment Fund and the Prime Fund includes an allocation to non-United States equity securities and fixed income securities. Each international equity manager must hold a minimum of 30 individual stocks with equity holdings in a single company remaining below 8% of the investment manager's portfolio, measured at market value. Currency hedging of foreign bonds and stocks is allowed under System Policy. For FY 2014 and 2013, all foreign investments in the System Pools are denominated in U.S. dollars and are in international commingled funds, which in turn invest in equity securities and bonds of foreign issuers except for approximately \$86,700,000 and \$1,000,000 of foreign bonds denominated in U.S. dollars and held by the Intermediate Fund for FY 2014 and 2013, respectively.

**Securities Lending:** Board policies permit security lending as a mechanism to augment income. Loans of the securities are required to be collateralized by cash, letters of credit or securities issued or guaranteed by the U.S. Government or its agencies. The collateral must equal at least 102% of the current market value of the loaned securities. Securities lending contracts must state acceptable collateral for securities loaned, duties of the borrower, delivery of loaned securities and acceptable investment of the collateral.

At September 30, 2014 and 2013, there were no securities on loan from the investment pools.

**Note 4 – Accounts Receivable**

The composition of accounts receivable for FY 2014 and 2013 is summarized as follows:

	<u>2014</u>	<u>2013</u>
Tuition and fees (net of allowance for doubtful accounts of \$804,045 in 2014 and \$804,045 in 2013)	\$ 5,058,673	\$ 5,278,520
Auxiliary enterprises and other operating activities	53,640	165,184
Federal, state, and private grants and contracts (net of allowance for doubtful accounts of \$371,577 in 2014 and \$371,619 in 2013)	22,526,286	20,834,626
Legal settlement receivable, net present value	904,616	860,391
Other	492,124	1,766,507
Net accounts receivable	<u>\$ 29,035,339</u>	<u>\$ 28,905,228</u>

**Note 5 – Capital Assets**

Capital assets activity for FY 2014 and 2013 is summarized as follows:

	October 1, <u>2013</u>	<u>Additions</u>	<u>Retirements</u>	<u>Adjustments</u>	September 30, <u>2014</u>
Land	\$ 7,552,605	\$ 38,543	-	-	\$ 7,591,148
Land improvements and infrastructure	14,870,571	1,895,615	-	-	16,766,186
Buildings and building improvements	290,629,408	2,447,308	(3,416,722)	21,523,729	311,183,723
Construction in progress	18,454,776	25,786,071	-	(21,523,729)	22,717,118
Equipment	65,428,773	3,193,435	(6,679,817)	-	61,942,391
Library books	25,945,675	129,461	(51,298)	-	26,023,838
Computer software	2,939,750	-	-	-	2,939,750
Collections	1,124,402	-	-	-	1,124,402
Total cost of capital assets	<u>426,945,960</u>	<u>33,490,433</u>	<u>(10,147,837)</u>	<u>-</u>	<u>450,288,556</u>
Less accumulated depreciation	206,101,243	13,058,315	(8,763,469)	-	210,396,089
Capital assets, net	<u>\$ 220,844,717</u>	<u>\$ 20,432,118</u>	<u>\$ (1,384,368)</u>	<u>\$ -</u>	<u>\$ 239,892,467</u>

	October 1, <u>2012</u>	<u>Additions</u>	<u>Retirements</u>	<u>Adjustments</u>	September 30, <u>2013</u>
Land	\$ 3,960,290	\$ 3,653,083	\$ (60,768)	-	\$ 7,552,605
Land improvements and infrastructure	11,174,484	3,696,087	-	-	14,870,571
Buildings and building improvements	287,330,900	3,597,740	(299,232)	-	290,629,408
Construction in progress	2,224,158	16,956,124	-	(725,506)	18,454,776
Equipment	63,744,811	2,773,646	(1,089,684)	-	65,428,773
Library books	25,878,434	145,788	(78,547)	-	25,945,675
Computer software	2,939,750	-	-	-	2,939,750
Collections	510,305	614,097	-	-	1,124,402
Total cost of capital assets	<u>397,763,132</u>	<u>31,436,565</u>	<u>(1,528,231)</u>	<u>(725,506)</u>	<u>426,945,960</u>
Less accumulated depreciation	194,672,632	12,416,766	(988,155)	-	206,101,243
Capital assets, net	<u>\$ 203,090,500</u>	<u>\$ 19,019,799</u>	<u>\$ (540,076)</u>	<u>\$ (725,506)</u>	<u>\$ 220,844,717</u>

**Note 6 – Long-term Debt**

Long-term debt activity for FY 2014 and 2013 is summarized as follows:

<u>Type/Supported by</u>	<u>October 1, 2013</u>	<u>New Debt</u>	<u>Principal Repayment</u>	<u>September 30, 2014</u>
Bonds:				
Student housing revenue	\$ 41,911,000	\$ -	\$ 2,055,000	\$ 39,856,000
General fee revenue	68,360,000	-	2,180,000	66,180,000
Note payable	1,843,000	-	368,600	1,474,400
Total debts	<u>112,114,000</u>	<u>\$ -</u>	<u>\$ 4,603,600</u>	<u>107,510,400</u>
Less current portion	(4,603,600)			(4,698,600)
(Discount) or premium	<u>282,200</u>			<u>272,278</u>
Total long-term debt	<u>\$107,792,600</u>			<u>\$ 103,084,078</u>

<u>Type/Supported by</u>	<u>October 1, 2012</u>	<u>New Debt</u>	<u>Principal Repayment</u>	<u>September 30, 2013</u>
Bonds:				
Student housing revenue	\$ 43,446,000	\$ -	\$ 1,535,000	\$ 41,911,000
General fee revenue	38,270,000	32,005,000	1,915,000	68,360,000
Note payable	-	1,843,000	-	1,843,000
Total debts	<u>81,716,000</u>	<u>\$ 33,848,000</u>	<u>\$ 3,450,000</u>	<u>112,114,000</u>
Less current portion	(3,450,000)			(4,603,600)
(Discount) or premium	<u>(311,500)</u>			<u>282,200</u>
Total long-term debt	<u>\$ 77,954,500</u>			<u>\$ 107,792,600</u>

Maturities and interest on long-term debt for the next five years and subsequent five-year periods ended September 30 are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015	\$ 4,698,600	\$ 3,873,870	\$ 8,572,470
2016	4,818,600	3,767,720	8,586,320
2017	4,143,600	3,651,535	7,795,135
2018	4,253,600	3,555,142	7,808,742
2019	3,995,000	3,450,047	7,445,047
2020-2024	21,716,000	15,312,746	37,028,746
2025-2029	22,005,000	10,958,209	32,963,209
2030-2034	16,060,000	7,107,397	23,167,397
2035-2039	13,920,000	4,036,084	17,956,084
2040-2043	11,900,000	988,483	12,888,483
	<u>\$ 107,510,400</u>	<u>\$ 56,701,233</u>	<u>\$ 164,211,633</u>

The following is a detailed schedule of long-term debt:

<u>Description and Purpose</u>	<u>Date Issued</u>	<u>Final Maturity</u>	<u>Interest Rate - %</u>	<u>Original Indebtedness</u>	<u>Outstanding Indebtedness September 30, 2014</u>	<u>Outstanding Indebtedness September 30, 2013</u>
<b>Bonds Payable:</b>						
Dormitory Revenue Bonds of 1980	5/1/1980	5/1/2020	3.00	\$ 2,180,000	\$ 525,000	\$ 605,000
Dormitory Revenue Bonds of 1981	7/23/1982	5/1/2021	3.00	2,602,000	686,000	776,000
Student Housing Revenue Bonds-Series 2004-A	9/30/2004	9/1/2034	3.00-4.625	13,130,000	10,390,000	10,705,000
Student Housing Revenue Bonds-Series 2004-B	9/30/2004	9/1/2016	3.00-3.625	7,515,000	1,505,000	2,215,000
Revenue Bonds-Series 2005-A	10/1/2005	6/1/2025	3.00-4.375	8,580,000	5,425,000	5,810,000
Revenue Bonds-Series 2009A	8/4/2009	7/1/2029	3.0-4.50	8,115,000	6,585,000	6,905,000
Student Housing Revenue Bonds-Series 2010-A	7/14/2010	6/1/2042	2.85-6.125	27,990,000	27,220,000	27,610,000
General Fee Revenue Bonds-Series 2012-A	4/3/2012	10/1/2031	0.73-4.28	11,170,000	10,230,000	10,700,000
General Fee Revenue Bonds-Series 2012-B	9/5/2012	12/1/2026	0.74-3.84	13,700,000	12,175,000	12,940,000
General Fee Revenue Bonds-Series 2013-A-1	4/4/2013	4/1/2023	1.57	7,550,000	6,840,000	7,550,000
General Fee Revenue Bonds-Series 2013-A-2	4/4/2013	4/1/2043	4.00	24,455,000	24,455,000	24,455,000
<b>Total Bonds Payable</b>				<u>126,987,000</u>	<u>106,036,000</u>	<u>110,271,000</u>
<b>Note Payable:</b>						
UAH Foundation	7/10/2013	7/1/2018		1,843,000	1,474,400	1,843,000
<b>Total Note Payable</b>				<u>1,843,000</u>	<u>1,474,400</u>	<u>1,843,000</u>
<b>Total Debt</b>				<u>\$128,830,000</u>	<u>\$ 107,510,400</u>	<u>\$ 112,114,000</u>

In December 2014, the University refinanced the Student Housing Revenue Bonds Series 2004-A and Series 2004-B, which resulted in a reduction of future principal and interest payments of \$1.5 million. This savings will average \$77 thousand a year for the next 20 years. The amounts outstanding on these bonds were paid in January 2015 in the amount of \$11.8 million. There was no defeased debt outstanding related to the Student Housing Revenue Bonds Series 2004-A and Series 204-B at September 30, 2014.

During FY 2013 the University issued General Fee Revenue Bonds - Series 2013-A-1 and 2013-A-2 for the purpose of constructing and equipping of a new Charger Union facility, constructing and equipping of a Nursing Building expansion, and other related campus infrastructure improvements and additions. The Series 2013-A-1 bond was privately issued in April 2013 directly to a bank for \$7,550,000. This bond principal matures each year from 2014 until 2023 and carries an interest rate of 1.57%. The Series 2013-A-2 bonds were also issued in April 2013 in the form of \$16,445,000 serial bonds with principal maturing each year from 2024 through 2038 and an \$8,010,000 term bond maturing in 2043. Each form of the Series 2013-A-2 bonds carries an interest rate of 4.00%.

The University's general fee bonds and student housing bonds are subject to certain covenants. These covenants, among other things, require the University to establish and maintain reasonable fees, rates, and other charges to ensure pledged revenues are sufficient for debt service coverage; to maintain books and records pertaining to the pledged revenues; to furnish annual audits and other periodic reports that reflect the financial condition of the Borrower, the project, other pledged facilities, and other pledged assets;



and to comply with certain restrictions as to additional indebtedness. The University is in compliance with all restrictive financial covenants as of September 30, 2014.

### Note 7 – Self-Insurance

The University participates with other campuses in the System in a self-insurance program for general liability risks. The Board established a separate revocable trust fund for payment of these self-insurance claims under its risk retention program. Annual contributions are made to the consolidated trust fund, at an actuarially determined rate, to provide funding for the retained risk. The accompanying statements of net position include a reserve of \$345,155 and \$326,168 for general liability for FY 2014 and 2013, respectively.

The University also maintains a self-insurance health plan. For FY 2014, the University paid \$22.25 and \$5.00 per month per health insurance contract for administrative charges and stop loss coverage, respectively. The accompanying statements of net assets include a self-insurance reserve of \$1,161,963 and \$1,179,280 for health insurance for FY 2014 and 2013, respectively. Annual contributions are made to the health plan, utilizing an actuarially determined rate, to provide funding for the reserve. The changes in the total reported self-insurance liabilities are summarized as follows:

	<b>2014</b>	<b>2013</b>
Balance, beginning of year	\$ 1,505,448	\$ 1,398,403
Claims paid	(9,295,703)	(9,434,244)
Contributions and adjustments	9,297,373	9,541,289
Balance, end of year	<u>\$ 1,507,118</u>	<u>\$ 1,505,448</u>

### Note 8 – Retirement Plans

Most employees of the University participate in the Teachers' Retirement System of Alabama (TRS), a cost sharing, multiple-employer public retirement system. In addition, certain employees meeting eligibility requirements participate in optional programs with the Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA - CREF) and the Variable Annuity Life Insurance Company (VALIC). TRS is a defined benefit plan while the TIAA – CREF and VALIC programs are defined contribution plans.

The TRS was established as of September 1939 under the provisions of Act 419 of the Legislature of 1939 for the purpose of providing retirement allowances and other specified benefits for qualified persons employed by State-supported educational institutions. The responsibility of the general administration and operation of TRS is vested in its Board of Control.

Participants in TRS who were hired before January 1, 2013, (Tier 1 employees) who retire at age 60 with 10 years of credited service, or after completing 25 years of

credited service, regardless of age, are entitled to an annual benefit, payable monthly for life. Service retirement benefits are calculated by three methods with the participants receiving payments under the method which yields the highest monthly benefit. These methods include (1) minimum guaranteed, (2) money purchase, or (3) formula. Under the formula method, participants are allowed 2.0125% of their final average salary (average of three highest years of annual compensation during the last 10 years of service) for each year of service. A participant terminating before reaching retirement age, but after completing 10 years of credited service, is eligible for a vested allowance at age 60 provided accumulated employee contributions are not withdrawn. TRS also provides death and disability benefits.

Participants in TRS hired on or after January 1, 2013, (Tier 2 employees) who retire at age 62 with 10 years or more of credited service, are entitled to an annual monthly benefit, payable for life. Service retirement benefits are calculated by three methods with the participants receiving payments under the method which yields the highest monthly benefit. These methods include (1) minimum guaranteed, (2) money purchase, or (3) formula. Under the formula method, participants are allowed 1.65% of their final average salary (average of highest five years of annual compensation during the last 10 years of service) for each year of service up to a benefit cap of 80% of average final salary. A participant terminating before reaching retirement age, but after completing 10 years of credited service, is eligible for a vested allowance at age 62 provided accumulated employee contributions are not withdrawn. TRS also provides death and disability benefits.

Covered employees are required by statute to contribute to TRS. All regular employees of the University are members of TRS with the exception of temporary employees who, by definition, are those employees hired for a predetermined period of employment of less than one year and employees working less than one half of a regular schedule. The following is a comparative presentation of contributions:

	<b><u>2014</u></b>		<b><u>2013</u></b>	
University contributions	\$ 11,931,714		\$ 9,654,665	
Employee contributions	7,544,985		7,167,693	
Total contributions	<u>\$ 19,476,699</u>		<u>\$ 16,822,358</u>	
	<b><u>2014</u></b>	<b><u>2014</u></b>	<b><u>2013</u></b>	<b><u>2013</u></b>
	<b><u>Tier 1</u></b>	<b><u>Tier 2</u></b>	<b><u>Tier 1</u></b>	<b><u>Tier 2</u></b>
University contribution regular rate	11.71%	11.08%	10.08%	9.44%
Employee contribution rate	7.50%	6.00%	7.50%	6.00%
Employee contribution law enforcement rate	8.50%	7.00%	8.50%	7.00%

The 10-year historical trend information shows TRS's progress in accumulating sufficient assets to pay benefits when due and the significant actuarial assumptions used to compute the pension benefit obligation, including the discount rate, projected salary increases, and postretirement benefit increases presented in the

September 30, 2013 annual financial report of the TRS. That report is publicly available and may be obtained by contacting the TRS Communication Department at 1-877-517-7000. State law required employee contribution rates for Teachers' Retirement to increase to 7.50% and 8.50%. The new rates took effect October 1, 2012.

The actuarial accrued liability (AAL), which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The actuarial value of assets, which is the actuarial present value of assets, is a standardized disclosure measure of the present value of accumulated assets, adjusted for projected investment performance and contributions. TRS does not make separate measurements of assets and the AAL for individual employers. The AAL at September 30, 2013 (the most recent valuation date) and September 30, 2012 for TRS as a whole, determined through actuarial valuations performed as of that date, was approximately as follows:

	<b>2013</b>	<b>2012</b>
Actuarial accrued liability (AAL)	\$ 29,665,843,000	\$ 28,251,367,000
Actuarial valuations of assets	19,629,816,000	18,786,006,000
Overfunded (underfunded) AAL	\$ (10,036,027,000)	\$ (9,465,359,000)

As previously noted, some employees participate in the optional TIAA-CREF programs, which are defined contribution plans. In defined contribution plans, benefits depend solely on amounts contributed plus investment earnings. All full time regular monthly exempt employees are eligible to participate from the date of employment. The University contributes a matching amount up to 5% of total salaries for participating employees. The University's contributions are funded as they accrue and, along with that of employees, are immediately and fully vested.

The contributions for FY 2014 and 2013, excluding amounts from employees who are not eligible for matching, are summarized as follows:

	<b>2014</b>	<b>2013</b>
University contributions	\$ 2,990,512	\$ 2,881,646
Employee contributions	5,645,945	5,457,994
Total contributions	<u>\$ 8,636,457</u>	<u>\$ 8,339,640</u>

The University’s total salaries and wages subject to benefit plan participation for FY 2014 and 2013 are summarized in the table below:

	<u>2014</u>	<u>2013</u>
Total Salaries and Wages	\$ 115,323,572	\$ 110,787,026
Salaries and Wages of employees participating in:		
TRS	\$ 97,032,526	\$ 96,142,144
TIAA - CREF	\$ 64,403,831	\$ 59,981,242

**Note 9 – Other Post-Employment Benefits**

The University offers postemployment health care benefits to all employees who officially retire from the University. Health care benefits are offered to retirees through the Alabama Retired Education Employees' Health Care Trust or the Public Education Employee Health Insurance Plan (PEEHIP) with TRS. Certain retired employees may also elect to continue to participate in the University's group health plan until they are eligible for Medicare by paying the full cost of the plan premium. Retired employees age sixty-five or older who are eligible for Medicare must enroll in the Medicare Coordinated Plan under which Medicare is the primary insurer and the University's health care plan becomes the secondary insurer. Despite the availability of the University's plan, most retirees elect to participate in PEEHIP with TRS, in which case the retirees pay a portion of the PEEHIP premium, with the University paying an allocation toward the cost of retiree coverage.

Certain retirees may also elect to continue their basic term life insurance coverage and accidental death and dismemberment insurance up to certain maximum amounts. The retirees pay the full amount of the premiums in such cases. Retirees are eligible for tuition assistance benefits for themselves as well as for their spouse and unmarried dependent children.

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (“GASB 45”), requires governmental entities to recognize and match other postretirement benefit costs with related services received and also to provide information regarding the actuarially calculated liability and funding level of the benefits associated with past services. GASB 45 does not have a material impact on the University's financial statements principally because most retirees elect to participate in the State-sponsored PEEHIP. PEEHIP is a cost-sharing multiple-employer defined benefit health care plan administered by the Public Education Employee Health Insurance Board. PEEHIP offers a basic hospital/medical plan that provides basic medical coverage for up to 365 days of care during each hospital confinement. The basic hospital/medical plan also provides for physicians' benefits, outpatient care, prescription drugs, and mental health benefits. Major medical benefits under the basic hospital/medical plan are subject to a lifetime contract maximum of \$1,000,000 for each covered individual. The *Code of Alabama 1975, Section 16-25A-8* provides the authority to set the contribution requirements for retirees and employers. The required rates of retirees are as follows for FY 2014:

*Retired Member Rates:*

- Individual Coverage/Non-Medicare Eligible - \$151.00
- Family Coverage/Non-Medicare Eligible Retired Member and Non-Medicare Eligible Dependents - \$391.00
- Family Coverage/Non-Medicare Eligible Retired Member and Dependent Medicare Eligible - \$250.00
- Individual Coverage/Medicare Eligible Retired Member - \$10.00
- Family Coverage/Medicare Eligible Retired Member and Non-Medicare Eligible Dependent(s) - \$250.00
- Family Coverage/Medicare Eligible Retired Member and Dependent Medicare Eligible - \$109.00
- Tobacco surcharge - \$28.00 per month
- PEEHIP Supplemental Plan - \$0
- Optional plans (Hospital Indemnity, Cancer, Dental, Vision) – Up to two optional plans can be taken by retirees at no cost if the retiree is not also enrolled in one of the Hospital Medical Plans. Otherwise, retirees can purchase the Optional Plans at the normal monthly rate of \$38.00 or \$45.00 for family dental.
- Members who retired on or after October 1, 2005, and before January 1, 2012, pay two percent of the employer premium for each year under 25 years of service, and for each year over 25 years of service, the retiree premium is reduced by two percent.
- Employees who retire on or after January 1, 2012, with less than 25 years of service, are required to pay 4% for each year under 25 years of service. Additionally, non-Medicare eligible employees who retire on or after January 1, 2012 are required to pay 1% more for each year less than age 65 (age premium) and to pay the net difference between the active employee subsidy and the non-Medicare eligible retiree subsidy (subsidy premium). When the retiree becomes Medicare eligible, the age and subsidy premium will no longer apply. However, the years of service premium (if applicable to the retiree) will continue to be applied throughout retirement. These changes are being phased in over a five year period.

The required contribution rate of the employer was \$356 per retiree per month for FY 2014. The University paid \$1,574,568 and \$1,405,824 for 384 and 358 retirees for FY 2014 and 2013, respectively. The required contribution rate is determined by PEEHIP in accordance with State statute. The complete financial report for PEEHIP can be obtained at the Retirement Systems of Alabama Members PEEHIP website [http://www.rsa-al.gov/uploads/files/PEEHIP\\_Fin\\_State\\_13.pdf](http://www.rsa-al.gov/uploads/files/PEEHIP_Fin_State_13.pdf) under the PEEHIP Financial Reports/Financial Statements.

**Note 10 – Compensated Absences**

Certain University employees accrue vacation and sick leave at varying rates depending upon their years of continuous service and payroll classification, subject to maximum limitations. Upon termination of employment, employees are paid all unused accrued

vacation at their regular rate of pay up to a designated maximum number of days. The statement of net position includes vacation pay and salary-related payments associated with vacation pay accruals of \$4,717,832 and \$4,610,600 for FY 2014 and 2013, respectively. There is no such accrual recognized for sick leave benefits because no terminal cash benefit is available to employees for accumulated sick leave.

### **Note 11 – Federal Direct Lending Program**

The Federal Direct Student Loan Program (“FDSLPL”) was established under the Higher Education Act of 1965, as amended in the Student Loan Reform Act of 1993. The FDSLPL enables an eligible student or parent to obtain a loan to pay for the student’s cost of attendance directly through the University rather than through private lenders. The University began participation in the FDSLPL on July 1, 1995. As a university qualified to originate loans, the University is responsible for handling the complete loan process, including funds management as well as promissory note functions. The University is not responsible for collection of these loans. For FY 2014 and 2013, the University disbursed \$28,466,907 and \$28,425,788, respectively, under the FDSLPL.

### **Note 12 – Contracts and Grants**

As of FY 2014 and FY 2013, the University was awarded approximately \$47.7 million and \$60.2 million, respectively, in contracts and grants which have not been expended. These awards, which represent commitments of sponsors to provide funds for specific research, training, and service projects, have not been reflected in the financial statements.

During FY 2014, the University received and expended federal funding under the American Recovery and Reinvestment Act (“ARRA”). In 2014 and FY 2013, those funds were primarily in the form of sponsored research grants in the amount of \$1,193,514 and \$1,137,748 respectively.

### **Note 13 – Contingencies and Commitments**

The University has sovereign immunity and is therefore, in the opinion of System Counsel, immune to ordinary tort actions. The University has consistently been dismissed from lawsuits on the basis of the sovereign immunity doctrine. That doctrine also protects the University from vicarious liability arising from the negligence of its employees. As a matter of policy, the University has chosen to indemnify its employees through a self-insured trust fund against liability arising from the performance of their official duties. There are some exceptions to the sovereign immunity doctrine, most notably in federal court cases arising under the federal constitution or federal statutes. The University is engaged in various legal actions in the ordinary course of business. Management does not believe the ultimate outcome of those actions will have a material adverse effect on the financial statements. However, the settlement of legal actions is subject to inherent uncertainties and it is possible that such outcomes could differ materially from management’s current expectations.

The University has contracted for the construction and renovation of several facilities. At September 30, 2014, the estimated remaining cost to complete the construction and renovation of these facilities was approximately \$3.1 million which is expected to be financed from grants, bond proceeds, University funds and private gifts.

**Note 14 – Operating Expenses by Function**

Operating expenses by functional classification for FY 2014 and 2013 are summarized as follows:

	Year Ended September 30, 2014					
	Salaries and Wages	Fringe Benefits	Supplies and Services	Depreciation	Scholarships and Fellowships	Total
Instruction	\$ 36,079,255	\$ 11,854,298	\$ 4,119,168	\$ -	\$ -	\$ 52,052,721
Research	48,970,008	14,337,790	11,449,511	-	-	74,757,309
Public service	2,128,126	603,394	2,906,586	-	-	5,638,106
Academic support	6,091,175	1,814,676	2,924,953	-	-	10,830,804
Student services	6,427,408	1,976,915	6,185,770	-	-	14,590,093
Institutional support	10,531,518	3,423,856	5,263,182	-	-	19,218,556
Operations and maintenance of plant	3,971,769	1,471,928	7,824,130	-	-	13,267,827
Scholarships and fellowships	-	-	-	-	1,101,624	1,101,624
Auxiliary enterprises	1,124,313	286,131	2,996,930	-	-	4,407,374
Depreciation	-	-	-	13,058,315	-	13,058,315
<b>Total Operating Expenses</b>	<b>\$ 115,323,572</b>	<b>\$ 35,768,988</b>	<b>\$ 43,670,230</b>	<b>\$ 13,058,315</b>	<b>\$ 1,101,624</b>	<b>\$ 208,922,729</b>

	Year Ended September 30, 2013					
	Salaries and Wages	Fringe Benefits	Supplies and Services	Depreciation	Scholarships and Fellowships	Total
Instruction	\$ 34,437,189	\$ 10,792,058	\$ 3,642,019	\$ -	\$ -	\$ 48,871,266
Research	48,463,342	14,364,788	18,914,969	-	-	81,743,099
Public service	1,834,775	539,127	2,448,418	-	-	4,822,320
Academic support	5,439,264	1,540,081	2,836,498	-	-	9,815,843
Student services	5,987,761	1,808,127	6,001,062	-	-	13,796,950
Institutional support	9,667,027	2,072,926	6,308,063	-	-	18,048,016
Operations and maintenance of plant	3,775,968	1,351,575	7,354,395	-	-	12,481,938
Scholarships and fellowships	-	-	-	-	1,090,063	1,090,063
Auxiliary enterprises	1,181,700	290,349	2,993,435	-	-	4,465,484
Depreciation	-	-	-	12,416,766	-	12,416,766
<b>Total Operating Expenses</b>	<b>\$ 110,787,026</b>	<b>\$ 32,759,031</b>	<b>\$ 50,498,859</b>	<b>\$ 12,416,766</b>	<b>\$ 1,090,063</b>	<b>\$ 207,551,745</b>

**Note 15 – Recently Issued Accounting Standards**

The GASB issued Statement No. 66, *Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62* (“GASB 66”), in March 2012. The objective of this Statement is to improve accounting and financial reporting for a governmental financial

reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 and AICPA Pronouncements*. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012. The University has determined there was no material impact from adoption of GASB 66.

The GASB issued Statement No. 68, *Financial Reporting for Pension Plans – an amendment of GASB Statement No. 27* (“GASB 68”), in June 2012. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement is effective for financial statements for fiscal years beginning after June 15, 2014. The GASB issued Statement No. 71, *Pension Transitions for Contributions Made Subsequent to the Measurement Date – an Amendment of GASB Statement No. 68* (“GASB 71”), in November 2013. The objective of this Statement is to address an issue regarding application of the transition provisions of GASB 68. The provisions of this Statement should be applied simultaneously with the provisions of Statement 68. The University is currently evaluating the impact that GASB 68 will have on its financial statements, but notes that the adoption of this standard will likely result in the recognition of a material long-term liability and a material reduction of the University’s unrestricted net position.

The GASB issued Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees* (“GASB 70”), in April 2013. The objective of this Statement is to improve accounting and financial reporting by state and local governments that extend and receive nonexchange financial guarantees. This statement is effective for fiscal years beginning after June 13, 2013. The University has determined there was no material impact from the adoption of GASB 70.

#### **Note 16 – Discretely Presented Component Unit-UAH Foundation**

**Basis of Accounting-** The financial statements of UAHF have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

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

- **Unrestricted-** Net assets that are not subject to donor-imposed stipulations.
- **Temporarily Restricted-** Net assets subject to donor-imposed stipulations that may or will be met either by actions of UAHF and/or the passage of time.
- **Permanently Restricted-** Net assets subject to donor-imposed stipulations to be maintained permanently by UAHF. Generally, the donors of these assets restrict



UAHF to use all or a part of the income earned on the related investments for specific purposes. Unrealized and realized gains and losses and dividends and interest from investing in income producing assets may be included in any of these net asset classifications depending on donor-imposed stipulations.

In accordance with ASC 958-320, *Not-for-Profit Entities*, investments in debt securities and investments in equity securities with readily determinable fair values are reported at their fair values based on published market prices. Other investments, including real estate, are stated at cost or fair value at date of donation in the case of gifts. Changes in fair values are reported as unrealized gains or losses in the statement of activities and changes in net assets. All interest income and realized gains and losses are reported in the statement of activities.

**Investments** – The cost and reported value of investments at September 30, 2014 and 2013 are presented below:

	<b>2014</b>		<b>2013</b>	
	<b>Reported Value</b>	<b>Cost</b>	<b>Reported Value</b>	<b>Cost</b>
Certificates of deposit	\$ 509,081	\$ 509,081	\$ 504,520	\$ 504,520
Pooled Endowment Fund	37,167,663	35,320,231	35,899,846	34,014,884
Marketable debt securities	241,880	240,988	722,009	733,218
Marketable equity securities	1,405,357	1,125,271	1,455,922	1,154,319
Mutual funds	1,285,834	1,299,264	1,031,169	934,557
Total	<u>\$ 40,609,815</u>	<u>\$ 38,494,835</u>	<u>\$ 39,613,466</u>	<u>\$ 37,341,498</u>

UAHF invests certain amounts in a commingled investment pool ("Pooled Endowment Fund") sponsored by The University of Alabama System. The value recognized for the investment pool is determined by the System and is based on UAHF's proportionate share of the net asset value of the investment pool. The System has no variance power over the funds. Instead, the funds are distributed by the System to the Foundation upon its request. The investment pool invests in various investment securities, including both marketable and non-marketable securities. Since UAHF reports under FASB, all investments are reported at fair value and the GASB guidance for carrying certain non-readily marketable securities at cost (as described in Note 1) does not apply to UAHF.

**Investment in Unconsolidated Entities and Trust Receivable** - UAHF is one of several beneficiaries of a trust established upon the death in 1974 of one of the University's benefactors. The sole assets of the trust consist of ownership interests in two closely-held Huntsville, Alabama businesses named Big Springs, Inc. ("Big Springs") and Chambers Bottling Company, LLC ("Chambers"). The trust holds a 70% interest in the common stock of Big Springs and a 65% interest in Chambers. The trust was established with both lead and remainder beneficiaries. The lead interest in the trust (that is, the rights to the income generated by the trust assets) is divided equally among three sets of beneficiaries who hold a lifetime interest in those rights. As each lead interest terminates, a proportionate

amount of the underlying assets in the trust is distributed among two residual beneficiaries, UAHF and another unrelated charitable organization. UAHF's share of the residual interest of the trust assets is 90 percent. UAHF accounts for its residual interest in the trust as an unconditional promise to give noncash assets, consistent with generally accepted accounting principles for situations where a donee has the eventual right to noncash assets held by a charitable trust but not the cash flows generated by them while they are held by the trust. UAHF recorded this interest at fair value as of the date it was awarded in 1974, and currently carries this interest in the Trust receivable line on UAHF's accompanying Statements of Financial Position.

During 2008, one of the income interests terminated, and a pro-rata distribution of the ownership interests held by the trust were transferred to UAHF. As a result of the satisfaction of a pro-rata share of the pledge, UAHF recognized a gain of \$4,375,835 representing the increase in fair value of the noncash assets between the date the assets were promised in 1974 and their values upon actual receipt in 2008. As a result of the receipt of these equity interests, UAHF currently holds approximately 21% and 19.5% of Big Springs and Chambers, respectively. These equity interests allow UAHF to exercise significant influence over Big Springs and Chambers, and accordingly, UAHF accounts for these interests in under the equity method of accounting. During the years ended September 30, 2014 and 2013, UAHF recorded its proportionate share of earnings of each company (on a combined basis) of \$348,360 and \$594,251, respectively. In addition, UAHF received distributions from Chambers of \$532,935 and \$550,485 in 2014 and 2013, respectively. Big Springs did not make any distributions in either 2014 or 2013.

Eventually, all of the assets in the trust will be distributed upon the termination of the remaining lead interests, and the trust will terminate. At such time, UAHF will hold controlling interests of 63% and 58.5% in Big Springs and Chambers, respectively, and will consolidate these entities. UAHF will account for these interests under the equity method until the last lead interest is terminated, including the period after the termination of the second lead interest.

The following summarizes the combined financial position and results of operations of Big Springs and Chambers (on a consolidated basis) for the years ended September 30, 2014 and 2013:

	2014	2013
Current Assets	\$ 17,791,276	\$ 18,093,689
Noncurrent Assets	10,224,257	11,794,572
Current Liabilities	(2,999,249)	(3,502,034)
Noncurrent Liabilities	-	(257,493)
Equity	<u>\$ 25,016,284</u>	<u>\$ 26,128,734</u>
Net Sales	\$ 37,223,680	\$ 36,080,676
Operating Income	\$ 2,377,082	\$ 1,768,001
Net Income	\$ 1,628,070	\$ 3,052,625

**Income Taxes**-The Foundation is a nonprofit corporation that is exempt from federal income taxes under Section 501 (c)(3) of the Internal Revenue code for activities related to its exempt purpose. Certain of the Foundation's activities are considered by the Internal Revenue Service to provide unrelated business income and, accordingly, income from these activities is subject to federal income tax. The Foundation's income tax expense totaled \$211,131 and \$306,200 for the years ended September 30, 2014 and 2013, respectively.

**Endowments**-The Alabama Uniform Prudent Management of Institutional Funds Act (UPMIFA) was enacted by the State Legislature and signed into law effective January 1, 2009. UPMIFA prescribes new guidelines for the expenditure of a donor-restricted endowment funds in the absence of overriding, explicit donor stipulations. Its predecessor, UMIFA, focused on the prudent spending of the net appreciation of the fund. UPMIFA instead focuses on the entirety of a donor-restricted endowment fund, that is, both the original gift amount(s) and net appreciation. UPMIFA eliminates UMIFA's historic-dollar-value threshold, an amount below which an organization could not spend from the fund, in favor of a more robust set of guidelines about what constitutes prudent spending, explicitly requiring consideration of the duration and preservation of the fund. UAHF adopted guidance provided by the FASB relevant to endowments of not-for-profit organization and the related net asset classification of endowment funds subject to an enacted version of UPMIFA and enhanced disclosures for all endowment funds. The impact of this guidance on the classification of net assets for UAHF was not material to UAHF and is disclosed in UAHF's financial statements. The earnings distributions are appropriated for expenditure by the governing Boards of Trustees of UAHF in a manner consistent with the standard of prudence prescribed by UPMIFA. In order to conform to the standards for prudent fiduciary management of investments, UAHF's Board of Trustees has adopted endowment investment and spending policies that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of endowment assets.

**Restricted Net Assets**-Restricted net assets are classified as either temporarily restricted net assets and available for the following purposes, or permanently restricted net assets, which are restricted to investment in perpetuity, the income from which is expendable for the following purposes at September 30, 2014 and 2013:

	Temporarily Restricted		Permanently Restricted	
	2014	2013	2014	2013
Student support	\$ 4,526,056	\$ 4,148,249	\$ 10,963,560	\$ 10,758,833
Faculty support	2,627,112	2,417,674	5,990,607	5,959,331
Academic support	2,856,105	2,621,331	3,312,293	3,312,293
Facilities renovation	134,059	116,229	-	-
Research	208,627	123,587	-	-
Library	58,805	56,047	50,427	50,428
Total	<u>\$ 10,410,764</u>	<u>\$ 9,483,117</u>	<u>\$ 20,316,887</u>	<u>\$ 20,080,885</u>

**Note 17 - Legal Settlement Receivable**

In July 2006, Nektar Therapeutics (Nektar) and the University announced the settlement of the University's litigation against Nektar and Dr. Milton Harris, in exchange for a total cash payment of \$25,000,000. Under the terms of the agreement, Nektar and Dr. Harris jointly made an upfront payment totaling \$15,000,000 to the University during fiscal year 2006 with remaining payments due through 2016. Included in the statements of net position is the net present value of the remaining payments owed to the University of \$1,855,729 and \$2,716,120 as of FY 2014 and 2013, respectively.

**Note 18 - Segment Information**

The University constructed Southeast Housing and issued bonds in 1980 and 1982. The bonds were payable from revenues received by the University for the use and occupancy of the facility. Condensed financial information of the University's segment for FY 2014 and 2013, is as follows:

<b>Condensed Statements of Position</b>				
	Dorm Revenue Bonds 1980		Dorm Revenue Bonds 1981	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
<b>Assets</b>				
Current assets	\$ 179,193	\$ 179,193	\$ 154,895	\$ 154,891
Capital assets, net of accumulated depreciation	856,483	980,148	846,809	976,938
<b>Total assets</b>	<b>\$ 1,035,676</b>	<b>\$ 1,159,341</b>	<b>\$ 1,001,704</b>	<b>\$ 1,131,829</b>
<b>Liabilities</b>				
Current liabilities	\$ 546,344	\$ 483,737	\$ 1,422,104	\$ 1,200,910
Noncurrent liabilities	445,000	525,000	819,603	892,125
<b>Total liabilities</b>	<b>\$ 991,344</b>	<b>\$ 1,008,737</b>	<b>\$ 2,241,707</b>	<b>\$ 2,093,035</b>
<b>Net assets</b>				
Invested in capital assets, net of related debt	\$ 331,483	\$ 375,148	\$ 160,809	\$ 200,938
Restricted				
Expendable	172,000	152,000	280,000	280,000
Unrestricted	(459,151)	(376,544)	(1,680,812)	(1,442,144)
<b>Total net position</b>	<b>44,332</b>	<b>150,604</b>	<b>(1,240,003)</b>	<b>(961,206)</b>
<b>Total liabilities and net position</b>	<b>\$ 1,035,676</b>	<b>\$ 1,159,341</b>	<b>\$ 1,001,704</b>	<b>\$ 1,131,829</b>

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

	Dorm Revenue Bonds 1980		Dorm Revenue Bonds 1981	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Operating revenues	\$ 526,933	\$ 383,869	\$ 736,974	\$ 308,609
Operating expenses	(512,072)	(793,870)	(863,385)	(902,318)
Depreciation expense	(123,665)	(123,665)	(130,129)	(130,129)
<b>Operating income (loss)</b>	<b>(108,804)</b>	<b>(533,666)</b>	<b>(256,540)</b>	<b>(723,838)</b>
Nonoperating expenses	2,532	(1,315)	(22,257)	(26,180)
Transfers from general fund	-	-	-	-
<b>Changes in net position</b>	<b>(106,272)</b>	<b>(534,981)</b>	<b>(278,797)</b>	<b>(750,018)</b>
Net position, beginning of year	150,604	685,585	(961,206)	(211,188)
<b>Net position, end of year</b>	<b>\$ 44,332</b>	<b>\$ 150,604</b>	<b>\$ (1,240,003)</b>	<b>\$ (961,206)</b>

**Condensed Statements of Cash Flows**

	Dorm Revenue Bonds 1980		Dorm Revenue Bonds 1981	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
<b>Cash flows from</b>				
Operating activities	\$ 33,868	\$ (390,937)	\$ (105,048)	\$ (983,754)
Capital and related financing activities	(33,868)	298,287	105,048	983,754
<b>Net increase (decrease) in cash</b>	<b>-</b>	<b>(92,650)</b>	<b>-</b>	<b>-</b>
Cash, beginning of year	-	92,650	-	-
<b>Cash, end of year</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>

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