

# **Kansas Athletics, Incorporated and Subsidiary**

Auditor's Report and Consolidated Financial Statements

June 30, 2017 and 2016



**Kansas Athletics, Incorporated and Subsidiary**  
**June 30, 2017 and 2016**

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## Independent Auditor's Report

Board of Directors, Audit Committee  
and Management  
Kansas Athletics, Incorporated and Subsidiary  
Lawrence, Kansas

We have audited the accompanying consolidated financial statements of Kansas Athletics, Incorporated and Subsidiary (the Corporation), which comprise the consolidated statements of financial position as of June 30, 2017 and 2016, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

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

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

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Board of Directors, Audit Committee  
and Management  
Kansas Athletics, Incorporated and Subsidiary  
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*Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kansas Athletics, Incorporated and Subsidiary as of June 30, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*BKD, LLP*

Kansas City, Missouri  
September 20, 2017

**Kansas Athletics, Incorporated and Subsidiary**  
**Consolidated Statements of Financial Position**  
**June 30, 2017 and 2016**

**Assets**

	<b>2017</b>	<b>2016</b>
<b>Current Assets</b>		
Cash	\$ 8,042,438	\$ 9,527,994
Tickets and accounts receivable, net of allowance; 2017 - \$85,813; 2016 - \$132,841	3,890,314	5,062,785
Contributions receivable, net of allowance; 2017 - \$733,983; 2016 - \$719,727	15,394,931	16,025,790
Investments held by Kansas University Endowment Association	14,751,955	16,895,301
Prepaid expenses and other current assets	1,393,735	1,033,833
Total current assets	43,473,373	48,545,703
 <b>Property and Equipment, at Cost</b>		
Buildings	6,822,022	6,889,544
Improvements to State property	155,332,844	152,522,627
Furniture and fixtures	15,076,237	14,172,969
Construction in progress	579,211	1,111,575
	177,810,314	174,696,715
Less accumulated depreciation and amortization	(83,179,637)	(75,334,610)
	94,630,677	99,362,105
 <b>Contributions Receivable</b>	3,612,390	3,340,228
 <b>Investments</b>		
Held by Kansas University Endowment Association	34,444,300	32,076,614
Held by trustee under bond indenture	2,986,841	2,986,401
	37,431,141	35,063,015
 <b>Other Assets</b>	334,464	445,759
 Total assets	<b>\$ 179,482,045</b>	<b>\$ 186,756,810</b>

## Liabilities and Net Assets

	<u>2017</u>	<u>2016</u>
<b>Current Liabilities</b>		
Accounts payable	\$ 3,685,243	\$ 3,104,722
Advance ticket sales	10,209,308	14,988,403
Current portion of long-term debt	2,036,480	4,210,479
Other accrued expenses and current liabilities	<u>11,209,902</u>	<u>6,262,735</u>
Total current liabilities	27,140,933	28,566,339
<b>Deferred Revenue</b>	2,511,226	3,025,892
<b>Long-term Debt</b>	33,975,736	36,094,238
<b>Other Non-current Liabilities</b>	<u>841,512</u>	<u>4,801,541</u>
Total liabilities	<u>64,469,407</u>	<u>72,488,010</u>
<b>Net Assets</b>		
Unrestricted	53,502,450	54,112,900
Temporarily restricted	43,787,705	42,647,001
Permanently restricted	<u>17,722,483</u>	<u>17,508,899</u>
Total net assets	<u>115,012,638</u>	<u>114,268,800</u>
Total liabilities and net assets	<u>\$ 179,482,045</u>	<u>\$ 186,756,810</u>

**Kansas Athletics, Incorporated and Subsidiary**  
**Consolidated Statement of Activities**  
**Year Ended June 30, 2017**

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
<b>Revenue, Gains and Other Support</b>				
Contributions and grants, excluding capital-restricted	\$ 18,919,409	\$ 3,964,965	\$ 213,584	\$ 23,097,958
NCAA and conference distributions	32,353,799			32,353,799
Ticket sales and handling fees	19,397,411			19,397,411
Broadcast and television	6,708,077			6,708,077
Apparel sponsorship	4,032,143			4,032,143
Concessions and merchandise	1,160,618			1,160,618
Licensing royalties	1,128,310			1,128,310
Direct institutional support	1,537,591			1,537,591
Student activity fees	304,801			304,801
Investment income	142,387	3,232,080		3,374,467
Jayhawk Tennis Center	395,667			395,667
Other revenue	2,225,988			2,225,988
Net assets released from restrictions	<u>12,150,079</u>	<u>(12,150,079)</u>		<u>-</u>
Operating revenue, gains and other support	100,456,280	(4,953,034)	213,584	95,716,830
Contributions restricted for capital projects	<u>-</u>	<u>6,093,738</u>	<u>-</u>	<u>6,093,738</u>
Total revenue, gains and other support	<u>100,456,280</u>	<u>1,140,704</u>	<u>213,584</u>	<u>101,810,568</u>
<b>Expenses and Losses</b>				
Salaries and benefits	32,331,443			32,331,443
Grants-in-aid	13,841,984			13,841,984
Depreciation and amortization	9,453,667			9,453,667
Contractual services	8,714,280			8,714,280
Facilities and maintenance	5,809,714			5,809,714
Team travel	6,276,074			6,276,074
Equipment, uniforms and supplies	5,390,659			5,390,659
Game expenses	2,977,065			2,977,065
Interest expense	1,400,678			1,400,678
Guarantees paid to visiting teams	1,526,125			1,526,125
Recruiting expenses	2,032,033			2,032,033
Marketing and promotions	2,854,773			2,854,773
Loss on disposal of property and equipment	1,126,286			1,126,286
Other operating expenses	<u>6,839,271</u>			<u>6,839,271</u>
Total expenses and losses	<u>100,574,052</u>			<u>100,574,052</u>
<b>Increase (Decrease) in Net Assets Before</b>				
Transfer of Assets to the University	(117,772)	1,140,704	213,584	1,236,516
Transfer of Assets to the University	<u>(492,678)</u>	<u>-</u>	<u>-</u>	<u>(492,678)</u>
<b>Increase (Decrease) in Net Assets</b>	(610,450)	1,140,704	213,584	743,838
<b>Net Assets, Beginning of Year</b>	<u>54,112,900</u>	<u>42,647,001</u>	<u>17,508,899</u>	<u>114,268,800</u>
<b>Net Assets, End of Year</b>	<u>\$ 53,502,450</u>	<u>\$ 43,787,705</u>	<u>\$ 17,722,483</u>	<u>\$ 115,012,638</u>

**Kansas Athletics, Incorporated and Subsidiary**  
**Consolidated Statement of Activities**  
**Year Ended June 30, 2016**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<b>Revenue, Gains and Other Support</b>				
Contributions and grants, excluding capital-restricted	\$ 18,167,967	\$ 5,226,842	\$ 222,122	\$ 23,616,931
NCAA and conference distributions	29,762,417			29,762,417
Ticket sales and handling fees	19,679,107			19,679,107
Broadcast and television	7,284,077			7,284,077
Apparel sponsorship	4,034,513			4,034,513
Concessions and merchandise	1,430,827			1,430,827
Licensing royalties	1,111,033			1,111,033
Direct institutional support	1,489,711			1,489,711
Student activity fees	319,852			319,852
Investment income (loss)	165,155	(424,958)		(259,803)
Jayhawk Tennis Center	428,069			428,069
Other revenue	2,266,806			2,266,806
Net assets released from restrictions	<u>13,125,307</u>	<u>(12,784,807)</u>	<u>(340,500)</u>	<u>-</u>
Operating revenue, gains and other support	99,264,841	(7,982,923)	(118,378)	91,163,540
Contributions restricted for capital projects	<u>-</u>	<u>4,038,588</u>	<u>-</u>	<u>4,038,588</u>
Total revenue, gains and other support	<u>99,264,841</u>	<u>(3,944,335)</u>	<u>(118,378)</u>	<u>95,202,128</u>
<b>Expenses and Losses</b>				
Salaries and benefits	30,412,796			30,412,796
Grants-in-aid	12,727,405			12,727,405
Depreciation and amortization	9,667,810			9,667,810
Contractual services	7,663,230			7,663,230
Facilities and maintenance	6,248,096			6,248,096
Team travel	5,492,341			5,492,341
Equipment, uniforms and supplies	4,637,242			4,637,242
Game expenses	2,993,832			2,993,832
Interest expense	1,622,552			1,622,552
Guarantees paid to visiting teams	1,569,629			1,569,629
Recruiting expenses	1,666,037			1,666,037
Marketing and promotions	2,556,605			2,556,605
Other operating expenses	<u>6,507,574</u>			<u>6,507,574</u>
Total expenses and losses	<u>93,765,149</u>			<u>93,765,149</u>
<b>Increase (Decrease) in Net Assets Before Transfer of Assets to the University</b>	5,499,692	(3,944,335)	(118,378)	1,436,979
<b>Transfers of Assets to the University</b>	<u>(9,254,733)</u>	<u>-</u>	<u>-</u>	<u>(9,254,733)</u>
<b>Decrease in Net Assets</b>	(3,755,041)	(3,944,335)	(118,378)	(7,817,754)
<b>Net Assets, Beginning of Year</b>	<u>57,867,941</u>	<u>46,591,336</u>	<u>17,627,277</u>	<u>122,086,554</u>
<b>Net Assets, End of Year</b>	<u>\$ 54,112,900</u>	<u>\$ 42,647,001</u>	<u>\$ 17,508,899</u>	<u>\$ 114,268,800</u>

**Kansas Athletics, Incorporated and Subsidiary**  
**Consolidated Statements of Cash Flows**  
**Years Ended June 30, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
<b>Operating Activities</b>		
Change in net assets	\$ 743,838	\$ (7,817,754)
Items not requiring (providing) operating activities cash flows		
Net realized and unrealized (gains) losses on investments	(2,958,101)	805,848
Depreciation and amortization	9,372,550	9,615,254
Transfer of assets to the University	492,678	9,254,733
Loss (gain) on disposition of property and equipment	1,126,286	(78,455)
Contributions received restricted for capital projects	(6,093,738)	(4,038,588)
Contributions received restricted for long-term investment	(213,584)	(222,122)
Changes in		
Accounts receivable	1,172,471	(1,118,447)
Contributions receivable	512,981	(502,251)
Prepaid expenses and other assets	(248,607)	(71,049)
Accounts payable, accrued expenses and other liabilities	1,497,829	1,572,098
Advance ticket sales	(4,779,095)	4,051,044
Deferred revenue	(514,666)	(773,574)
	<u>110,842</u>	<u>10,676,737</u>
<b>Investing Activities</b>		
Contributions to investments held by Kansas University		
Endowment Association	(28,733,504)	(29,076,677)
Withdrawals from investments held by Kansas University		
Endowment Association	31,467,265	26,825,110
Deposits to investments held by trustee under bond indenture	(2,943,552)	(2,872,950)
Withdrawals from investments held by trustee under bond indenture	2,943,112	2,872,551
Proceeds from disposition of property and equipment	6,000	2,433,000
Purchase of property and equipment	(6,278,278)	(11,283,142)
	<u>(3,538,957)</u>	<u>(11,102,108)</u>
<b>Financing Activities</b>		
Proceeds from contributions restricted for capital projects	5,845,279	8,403,598
Proceeds from contributions restricted for long-term investments	307,759	282,140
Proceeds from long-term debt	-	245,477
Principal payments on athletic facilities revenue bonds	(1,555,000)	(1,495,000)
Principal payments on capital lease obligation	(580,184)	(559,185)
Principal payments on long-term debt	(2,075,295)	(2,394,163)
	<u>1,942,559</u>	<u>4,482,867</u>
<b>Increase (Decrease) in Cash</b>	(1,485,556)	4,057,496
<b>Cash, Beginning of Year</b>	<u>9,527,994</u>	<u>5,470,498</u>
<b>Cash, End of Year</b>	<u>\$ 8,042,438</u>	<u>\$ 9,527,994</u>
<b>Supplemental Cash Flows Information</b>		
Interest paid	\$ 1,482,705	\$ 1,528,155
Property and equipment purchases in accounts payable	186,980	117,150
Capital lease obligation incurred for equipment	-	31,194

# **Kansas Athletics, Incorporated and Subsidiary**

## **Notes to Consolidated Financial Statements**

### **June 30, 2017 and 2016**

#### **Note 1: Nature of Operations and Summary of Significant Accounting Policies**

##### ***Nature of Operations***

Kansas Athletics, Incorporated and Subsidiary (the Corporation) a Kansas not-for-profit corporation, operates under the administrative jurisdiction of the University of Kansas (the University) and is subject to all regulations and administrative policies of the University. The Corporation operates the varsity intercollegiate athletic program at the University in facilities that are owned by the University. The primary source of revenues and support for the program are athletic event ticket sales, conference revenue distributions and contributions.

Jayhawk Tennis Center, LLC (Jayhawk Tennis Center), a Kansas limited liability corporation, operates to manage the indoor and outdoor tennis facility utilized by the student athletes of the University of Kansas and the community of the city of Lawrence, Kansas. The primary sources of revenues for the facility are member dues, court time, lessons, clinics, facility rental and pro shop revenue.

##### ***Principles of Consolidation***

The consolidated financial statements include the accounts of Kansas Athletics, Incorporated and its wholly owned subsidiary, Jayhawk Tennis Center, LLC (collectively, the Corporation). All intercompany balances and transactions have been eliminated in consolidation.

##### ***Use of Estimates***

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

##### ***Accounts Receivable***

Accounts receivable are stated at the amount the Corporation expects to collect from balances outstanding. The Corporation provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. Accounts receivable are ordinarily due 30 days after the issuance of the invoice. Accounts past due more than 90 days are considered delinquent. Delinquent receivables are written off based on individual credit evaluation and specific circumstances of the customer.

**Kansas Athletics, Incorporated and Subsidiary**  
**Notes to Consolidated Financial Statements**  
**June 30, 2017 and 2016**

***Contributions Receivable***

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are initially reported at fair value determined using the discounted present value of estimated future cash flows technique. The resulting discount is amortized using the level-yield method and is reported as contribution revenue. The Corporation provides an allowance for uncollectible contributions, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Conditional gifts depend on the occurrence of a specified future and uncertain event to bind the potential donor and are recognized as assets and revenue when the conditions are substantially met and the gift becomes unconditional.

***Investments Held by Kansas University Endowment Association***

Investments in pooled funds held by Kansas University Endowment Association (KU Endowment) are valued at the proportional value of the overall fund which estimates fair value. Investment earnings are allocated monthly on a prorated basis representative of the Corporation's overall percentage of ownership in the applicable pooled funds. Investments in cash and real estate held by KU Endowment are recorded at the lower of cost or fair value.

The Corporation classifies funds that are available for immediate expenditure as current assets and funds invested in KU Endowment's long-term investment program and other investment funds as noncurrent assets.

***Investments Held by Trustee under Bond Indenture***

Investments held under bond indenture consist of money market funds, which are carried at fair value, and a guaranteed investment contract, which is recorded at the lower of cost or fair value.

***Property and Equipment***

Property and equipment are stated at cost less accumulated depreciation. Depreciation is charged to expense using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives.

The estimated useful lives for each major depreciable classification of property and equipment are as follows:

Land improvements	39 years
Buildings	39 years
Improvements to State property	25 years
Furniture and fixtures	5-7 years

# **Kansas Athletics, Incorporated and Subsidiary**

## **Notes to Consolidated Financial Statements**

**June 30, 2017 and 2016**

### ***Long-lived Asset Impairment***

The Corporation evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized for the years ended June 30, 2017 or 2016.

### ***Advance Ticket Sales***

Advance ticket sales represent tickets sold for future athletic events. Revenue is recognized in the year the athletic event is held.

### ***Deferred Revenue***

Revenue from fees for merchandise and multimedia is deferred and recognized over the periods to which the fees relate.

### ***Temporarily and Permanently Restricted Net Assets***

Temporarily restricted net assets are those whose use by the Corporation has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Corporation in perpetuity.

### ***Contributions***

Gifts of cash and other assets received without donor stipulations are reported as unrestricted revenue and net assets. Gifts received with a donor stipulation that limits their use are reported as temporarily or permanently restricted revenue and net assets. When a donor stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Gifts and investment income that are originally restricted by the donor and for which the restriction is met in the same time period are recorded as temporarily restricted and then released from restriction.

**Kansas Athletics, Incorporated and Subsidiary**  
**Notes to Consolidated Financial Statements**  
**June 30, 2017 and 2016**

***In-kind Contributions***

The Corporation receives in-kind contributions of supplies and services from donors and others. It is the policy of the Corporation to record, as contribution revenue in the consolidated financial statements, the estimated fair value of these supplies and services received, and also to record a like amount of expense to reflect the immediate consumption of these supplies and services. Revenue and expense related to in-kind services are only recorded when the services received create or enhance nonfinancial assets or require specialized skills possessed by the individuals providing the service and the service would typically need to be purchased if not donated. For the years ended June 30, 2017 and 2016, \$1,293,895 and \$1,216,960, respectively, of in-kind supplies and services was received and consumed by the Corporation.

***Broadcast and Television***

Broadcast and television revenues represent marketing and media production and distribution services rights relating to the Corporation's athletics programs. Revenues are recognized on a straight-line basis over the length of the contract period with the service provider.

***Functional Allocation of Expenses***

The costs of supporting the various programs and other activities have been summarized below on a functional basis. Certain costs have been allocated among the program, management and general and fundraising categories based on management's estimate of usage and other methods.

	<b>2017</b>	<b>2016</b>
Program	\$ 81,713,639	\$ 72,936,728
Management and general	15,660,678	17,431,928
Fundraising	3,199,735	3,396,493
	\$100,574,052	\$ 93,765,149

***Income Taxes***

The Corporation is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the Corporation is subject to federal income tax on any unrelated business taxable income. The Corporation is not subject to state income taxes.

The Corporation applies the provisions of ASC 740, *Income Taxes*, with respect to certain uncertain tax positions. ASC 740 requires that all tax positions be evaluated using a recognition threshold and measurement of a tax position taken in a tax return. Differences between positions taken in a tax return and amounts recognized in the consolidated financial statements are recorded as adjustments to income taxes payable or receivable, or adjustments to deferred taxes, or both. ASC 740 also requires expanded disclosures at the end of each annual reporting period. No amounts have been recorded at June 30, 2017 and 2016 with respect to uncertain tax positions.

**Kansas Athletics, Incorporated and Subsidiary**  
**Notes to Consolidated Financial Statements**  
**June 30, 2017 and 2016**

***Taxes Collected from Customers and Remitted to Governmental Authorities***

Taxes collected from customers and remitted to governmental authorities are presented in the accompanying consolidated statements of activities on a net basis.

***Transfers Between Fair Value Hierarchy Levels***

Transfers in and out of Level 1 (quoted market prices), Level 2 (other significant observable inputs) and Level 3 (significant unobservable inputs) are recognized on the period ending date.

***Reclassifications***

Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 financial statement presentation. These reclassifications had no effect on net earnings.

***Subsequent Events***

Subsequent events have been evaluated through the date of the Independent Auditor's Report, which is the date the consolidated financial statements were available to be issued.

**Note 2: Contributions Receivable**

Contributions receivable at June 30, 2017 and 2016 consisted of the following unconditional promises to give discounted at a rate of 4%:

	<u>2017</u>	<u>2016</u>
Due within one year	\$ 16,128,914	\$ 16,745,517
Due in one to five years	3,674,262	3,388,825
Due in greater than five years	49,000	77,000
	<u>19,852,176</u>	<u>20,211,342</u>
Less unamortized discount	110,872	125,597
Less allowance for uncollectible accounts	733,983	719,727
	<u><u>\$ 19,007,321</u></u>	<u><u>\$ 19,366,018</u></u>

**Kansas Athletics, Incorporated and Subsidiary**  
**Notes to Consolidated Financial Statements**  
**June 30, 2017 and 2016**

Contributions receivable are classified within the consolidated statements of financial position as follows:

	<u>2017</u>	<u>2016</u>
Contributions receivable - current	\$ 15,394,931	\$ 16,025,790
Contributions receivable - non-current	3,612,390	3,340,228
	<u>\$ 19,007,321</u>	<u>\$ 19,366,018</u>

**Note 3: Investments**

Investments at June 30, 2017 and 2016 consisted of the following:

	<u>2017</u>	<u>2016</u>
Held by Kansas University Endowment Association		
Cash	\$ 14,751,042	\$ 16,881,896
Long-term investment pool	32,274,768	29,899,435
Bond fund	1,340,373	1,390,614
Real estate	830,072	799,970
	<u>49,196,255</u>	<u>48,971,915</u>
Held by Trustee Under Bond Indenture		
Money market mutual funds	1,567,364	1,566,924
Guaranteed investment contract	1,419,477	1,419,477
	<u>2,986,841</u>	<u>2,986,401</u>
Total investments	<u>\$ 52,183,096</u>	<u>\$ 51,958,316</u>

Investments are classified within the consolidated statements of financial position as follows:

	<u>2017</u>	<u>2016</u>
Investments held by Kansas University		
Endowment Association		
Current	\$ 14,751,955	\$ 16,895,301
Noncurrent	34,444,300	32,076,614
Investments held by trustee under bond indenture	2,986,841	2,986,401
	<u>\$ 52,183,096</u>	<u>\$ 51,958,316</u>

**Kansas Athletics, Incorporated and Subsidiary**  
**Notes to Consolidated Financial Statements**  
**June 30, 2017 and 2016**

Total investment return is comprised of the following:

	<b>2017</b>	<b>2016</b>
Interest and dividend income	\$ 416,366	\$ 546,045
Net realized and unrealized gains (losses)	2,958,101	(805,848)
	\$ 3,374,467	\$ (259,803)

***Investments Held by Kansas University Endowment Association***

The KU Endowment holds various investments for the Corporation. The majority of these investments originated from donor contributions and were given to KU Endowment for the benefit of the Corporation's operations and activities. In order to ensure observance of limitations and restrictions that donors may have placed on the use of these resources, KU Endowment manages the resources as separate fund accounts, according to their nature and purpose; however, these separate accounts have been combined into appropriate accounting classifications in the accompanying consolidated financial statements.

KU Endowment invests the funds in accordance with its investment policies and procedures. The following is a description of the investment funds held at KU Endowment:

Cash

The cash fund represents cash held at KU Endowment that is available for expenditure and operates similar to a noninterest-bearing checking account. KU Endowment commingles the Corporation's cash balance with other idle cash balances held for the benefit of the University, to produce a net investment yield in order to defray KU Endowment's administrative costs. The cash fund is recorded at cost.

Long-term Investment Pool

The majority of the Corporation's investments held at KU Endowment are managed in the Long-Term Investment Portfolio (LTIP). The LTIP invests in equity securities, mutual funds, common trust funds, fixed income securities and alternative investments. These investments are recorded at fair value and investment earnings are allocated on a market-value proportional basis.

Bond Fund

The bond fund is primarily invested in government bond index fund. Investments are recorded at fair value and investment earnings are allocated on a market-value unit basis.

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Real Estate

Real estate represents property that is held by KU Endowment on behalf of the Corporation and is recorded at the lower of cost or fair value.

***Investments Held by Trustee Under Bond Indenture***

In connection with the Athletic Facilities Revenue Bonds discussed in Note 4, the Corporation is required to maintain funds in certain debt service reserve accounts pursuant to the bond agreements.

***Recurring Fair Value Measurements***

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities

The determination of where an asset or a liability falls in the hierarchy requires significant judgment. The Corporation evaluates its hierarchy disclosures for each reporting period; based on various factors, it is possible that an asset or a liability may be classified differently from one reporting period to another. However, the Corporation expects that changes in classifications between different levels will be rare.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs. There have been no significant changes in the valuation techniques during the year ended June 30, 2017.

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The following table presents the fair value measurements of assets and liabilities recognized in the accompanying consolidated statements of financial position measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2017 and 2016:

	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>June 30, 2017</b>				
Investments held by the Kansas University Endowment Association				
Long-term investment pool	\$ 32,274,768	\$ -	\$ 32,274,768	\$ -
Bond fund	1,340,373	-	1,340,373	-
Investments held by trustee under bond indenture				
Money market mutual funds	1,567,364	1,567,364	-	-
<b>June 30, 2016</b>				
Investments held by the Kansas University Endowment Association				
Long-term investment pool	\$ 29,899,435	\$ -	\$ 29,899,435	\$ -
Bond fund	1,390,614	-	1,390,614	-
Investments held by trustee under bond indenture				
Money market mutual funds	1,566,924	1,566,924	-	-

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

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**Note 4: Long-term Debt**

Long-term debt at June 30, 2017 and 2016 consisted of the following:

	<b>2017</b>	<b>2016</b>
Revenue bonds, KDFA Series 2014F (A)	\$ 34,830,000	\$ 36,385,000
Note payable, donor (B)	-	2,000,000
Note payable, bank (C)	32,648	41,273
Note payable, bank (D)	77,778	144,444
Capital lease obligation (E)	343,770	923,955
	35,284,196	39,494,672
Add unamortized premium	1,319,785	1,468,484
Less unamortized debt issuance costs	(591,765)	(658,439)
Less current maturities	(2,036,480)	(4,210,479)
	\$ 33,975,736	\$ 36,094,238

(A) The Athletic Facilities Revenue Bonds, Series 2014F, were issued by the Kansas Development Finance Authority during the year ended June 30, 2014 in the original amount of \$39,430,000. These bonds were issued for the purpose of refinancing the Series 2004K bonds and Series 2008C bonds to take advantage of favorable interest rates and reduce the amount of debt outstanding. The entire amount of the unamortized premium and debt issuance costs included in the above schedule relate to the bonds.

The Corporation entered into a loan agreement with the Kansas Development Finance Authority for repayment of the Series 2014F bonds. These tax-exempt bonds are secured by future revenues of the Corporation. Principal payments are due annually, ending in 2033. Interest is payable at various rates ranging from 3.00% to 4.00% per annum.

The Corporation is required to continually maintain at least \$2,951,113 in a debt service reserve account for the period of time for which principal and interest payments are required to be made on outstanding indebtedness. At June 30, 2017, the Corporation had investments held by a trustee of \$2,986,665, which were designated as the debt service reserve. Funds in this reserve account are invested as permitted by the bond trust indenture, the earnings from which are transferred out of this account and applied towards the principal and interest payments.

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- (B) Note payable to donor, due on or before January 2017, bears no interest and is unsecured. The balance was paid in full in December 2016.
- (C) Note payable to financing company, payable in monthly installments, including interest at 3.39%, due December 2020, collateralized by property and equipment.
- (D) Note payable to vendor, payable in monthly installments, including interest at 3.34%, due August 2018, collateralized by property and equipment.
- (E) Capital lease obligation for equipment expiring July 2019. Cost and accumulated depreciation at June 30, 2017 was \$2,821,477 and \$2,456,566, respectively, and at June 30, 2016, \$2,821,477 and \$1,892,270, respectively.

Aggregate annual maturities of long-term debt and payments on capital lease obligations at June 30, 2017 are:

<b>Year Ending June 30,</b>	<b>Revenue Bonds</b>	<b>Notes Payable</b>	<b>Capital Lease Obligations</b>	<b>Total</b>
2018	\$ 1,620,000	\$ 75,597	\$ 340,883	\$ 2,036,480
2019	1,690,000	20,354	7,636	1,717,990
2020	1,755,000	9,566	-	1,764,566
2021	1,825,000	4,909	-	1,829,909
2022	1,900,000	-	-	1,900,000
Thereafter	26,040,000	-	-	26,040,000
	<u>\$ 34,830,000</u>	<u>\$ 110,426</u>	348,519	35,288,945
Less capital lease interest			<u>(4,749)</u>	<u>(4,749)</u>
			<u>\$ 343,770</u>	<u>\$ 35,284,196</u>

Subsequent to year end, the Corporation entered into a five year capital lease with US Bank totaling approximately \$1,600,000 for capital projects. As the agreements were not closed prior to June 30, 2017, this debt is not reflected in the consolidated statements of financial position or long-term debt maturity schedule above.

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**Note 5: Net Assets**

***Temporarily Restricted Net Assets***

Temporarily restricted net assets at June 30, 2017 and 2016 are available for the following purposes or periods:

	<u>2017</u>	<u>2016</u>
Scholarships	\$ 17,601,983	\$ 15,909,913
Capital projects	5,361,087	5,495,033
Hall of Athletics	411,653	484,613
Other	1,715,448	1,795,388
Time restricted	18,697,534	18,962,054
	<u>\$ 43,787,705</u>	<u>\$ 42,647,001</u>

***Permanently Restricted Net Assets***

Permanently restricted net assets at June 30, 2017 and 2016 are restricted to:

	<u>2017</u>	<u>2016</u>
James Davis, Jr. Scholarship Fund	\$ 5,286,986	\$ 5,286,986
Louis L. Ward Family Scholarship for Men's Basketball Fund	1,240,049	1,240,049
Harry and Clara Nielsen Scholarship Fund	1,203,877	1,203,877
Dr. Earl and Kathleen Merkel Athletic Scholarship Fund	978,950	928,850
Mike and Mary Nell Beatty Athletic Scholarship Fund	960,195	860,195
Jayhawk Track and Field Endowment Fund	736,736	736,736
Ed Hall Memorial Scholarship Fund	581,000	581,000
Richard C. King Athletic Scholarship Fund	480,329	480,329
Wilt Chamberlain Men's Basketball Scholarship Fund	342,895	342,895
Gladys and Dale Gordon Scholarship Fund	251,552	251,552
Elder Nancy Miller Memorial Scholarship Fund	249,560	223,060
Bower's Family Men's Basketball Scholarship	246,673	246,673
W.R. Murfin Memorial Athletic Scholarship Fund	238,000	238,000
Kenneth and Ruth Hamilton Athletic Scholarship Fund	219,601	219,601
Other funds under \$200,000 each	4,706,080	4,669,096
	<u>\$ 17,722,483</u>	<u>\$ 17,508,899</u>

**Kansas Athletics, Incorporated and Subsidiary**  
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**Net Assets Released from Restrictions**

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors.

	<b>2017</b>	<b>2016</b>
Scholarships	\$ 5,316,152	\$ 4,873,361
Capital projects	5,485,000	7,315,471
Hall of Athletics	103,427	-
Other	1,245,500	936,475
	<b>\$ 12,150,079</b>	<b>\$ 13,125,307</b>

**Note 6: Endowment**

The Corporation's endowment consists of numerous individual donor-restricted funds established for a variety of purposes. As required by accounting principles generally accepted in the United States of America (GAAP), net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Corporation's management has interpreted the Uniform Prudent Management of Institutional Funds Act as adopted in the state of Kansas (UPMIFA) as requiring preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Corporation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Corporation in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Corporation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of the Corporation and the fund
3. General economic conditions
4. Possible effect of inflation and deflation
5. Expected total return from investment income and appreciation or depreciation of investments
6. Other resources of the Corporation
7. Investment policies of the Corporation

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The composition of donor-restricted endowment funds by net asset restriction and the changes in donor-restricted endowment net assets for the years ended June 30, 2017 and 2016 were:

	<b>2017</b>			<b>Total</b>
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	
Endowment net assets, beginning of year	\$ (25,728)	\$ 13,922,649	\$ 17,508,899	\$ 31,405,820
Investment return				
Investment income	-	337,227	-	337,227
Net appreciation	23,534	2,634,967	-	2,658,501
Total investment return	23,534	2,972,194	-	2,995,728
Contributions	-	147,624	213,584	361,208
Appropriation of endowment assets for expenditure	-	(1,289,036)	-	(1,289,036)
Endowment net assets, end of year	<u>\$ (2,194)</u>	<u>\$ 15,753,431</u>	<u>\$ 17,722,483</u>	<u>\$ 33,473,720</u>
	<b>2016</b>			
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, beginning of year	\$ (7,787)	\$ 15,029,761	\$ 17,627,277	\$ 32,649,251
Investment return (loss)				
Investment income	-	328,774	-	328,774
Net depreciation	(17,941)	(692,790)	-	(710,731)
Total investment loss	(17,941)	(364,016)	-	(381,957)
Contributions	-	150,234	222,122	372,356
Appropriation of endowment assets for expenditure	-	(1,233,830)	-	(1,233,830)
Change in donor designation	-	340,500	(340,500)	-
Endowment net assets, end of year	<u>\$ (25,728)</u>	<u>\$ 13,922,649</u>	<u>\$ 17,508,899</u>	<u>\$ 31,405,820</u>

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Amounts of donor-restricted endowment funds classified as permanently and temporarily restricted net assets at June 30, 2017 and 2016, was:

	<b>2017</b>	<b>2016</b>
Permanently restricted net assets - portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation or UPMIFA	\$ 17,722,483	\$ 17,508,899
Temporarily restricted net assets - portion of perpetual endowment funds subject to a time restriction under UPMIFA with purpose restrictions	\$ 15,753,431	\$ 13,922,649

KU Endowment has adopted investment and spending policies for the management of its Long-term Investment Portfolio (LTIP), which includes the endowment assets. The objective of these policies is to provide a predictable stream of funding to programs supported by the endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds the Corporation must hold in perpetuity or for donor-specified periods.

To preserve the endowment's value for future years, the LTIP is managed to achieve a total return that will cover both current spending and inflation. The objectives of the LTIP are to: 1) utilize an asset mix that will provide both diversification and long-term growth and 2) to provide a reasonable rate of spendable income to benefit University faculty members, staff and students. Actual returns in any given year may vary from this amount.

Funds participating in the LTIP receive regular distributions that are available for immediate spending to meet the Corporation's needs. In keeping with its objectives for the portfolio, KU Endowment has developed a calculation that determines the percentage of the portfolio that can be spent on a regular basis. The percentage, or spending rate, is reviewed annually by KU Endowment and is subject to modification to account for changes in market and economic conditions as well as the University needs.

Amounts that are available from the LTIP for the Corporation's needs are based on a constant growth spending policy, where spending is adjusted annually by inflation, as measured by the Consumer Price Index (CPI-U). Under the constant growth spending policy, the target rate from the LTIP for current expenditure by the Corporation is 4.6% of the market value. To avoid potential under-distributions or unsustainable over-distributions relative to the current market value in any given year, the constant growth spending policy is subject to a 3.76% floor and a 5.44% cap of the trailing four-quarter average market value.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the amount given by the donor. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. These deficiencies totaled \$2,194 and \$25,728 at June 30, 2017 and 2016, respectively. In accordance with UPMIFA, the Corporation and KU Endowment together consider whether to continue spending from accounts that are in a deficiency position, to ensure that the donor expectation for permanency of the funds is not jeopardized.

# **Kansas Athletics, Incorporated and Subsidiary**

## **Notes to Consolidated Financial Statements**

### **June 30, 2017 and 2016**

#### **Note 7: Related Party Transactions**

The Corporation conducts a significant portion of its business with the University and entities under the administrative jurisdiction of the University.

The Corporation utilizes facilities owned by the University in order to generate a portion of its revenues. Construction costs associated with University owned facilities that are incurred by the Corporation is accumulated as construction in progress and transferred to the University as determined by management. The Corporation transferred assets to the University totaling \$492,678 and \$9,254,733 during the years ended June 30, 2017 and 2016, respectively, related to construction of University facilities, most notably the McCarthy Scholarship Apartments and DeBruce Center.

The University has reported certain salaries, fringe benefits and other expenses paid for the benefit of the athletic program. Such amounts paid by the University for Intercollegiate Athletics as of June 30, 2017 and 2016 were \$1,537,591 and \$1,489,711, respectively, and are recorded as revenue and expense within the accompanying consolidated statements of activities.

The Corporation pays the University for tuition, meals and housing for student athletes. Amounts paid to the University for tuition, meals and housing were \$7,193,435, \$2,127,364 and \$1,604,362 in 2017, respectively, and \$6,848,335, \$1,474,072 and \$1,785,935 in 2016, respectively, and is included in the grants-in-aid expense on the consolidated statements of activities.

Total trade payables due to the University and related entities were \$2,592,781 and \$2,078,881 at June 30, 2017 and 2016, respectively, and are included in accounts payable. Total trade receivables due from the University and related entities were \$16,032 and \$4,387 at June 30, 2017 and 2016, respectively, and are included in accounts receivable.

The Corporation entered into an agreement in June 2016 which assigned, to KU Endowment, certain contributions receivable sufficient to satisfy 1) a McCarthy Scholarship Apartments construction period advance and 2) annual interest payments on this advance at a rate of prime plus 1% until the advance is fully paid off by collection of the assigned receivables. Total advances payable due to KU Endowment at June 30, 2017 and 2016 were \$1,541,114 and \$2,861,747, respectively, and are reflected between current and non-current liabilities on the consolidated statements of financial position based on management's estimates of when payments will be made. The Corporation paid KU Endowment principal and interest relating to this advance of \$1,514,890 and \$102,544 in 2017 and \$0 and \$97,157 in 2016, respectively.

Investment management fees paid to KU Endowment during 2017 and 2016 were \$279,792 and \$272,949, respectively.

**Kansas Athletics, Incorporated and Subsidiary**  
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**Note 8: Operating Leases**

Noncancellable operating leases for facilities and equipment expire in various years through 2044. Future minimum lease payments under operating leases are:

Year Ending June 30,	Amount
2018	\$ 2,466,929
2019	2,328,449
2020	2,232,918
2021	2,233,308
2022	2,230,703
Thereafter	49,261,356
	\$ 60,753,663

Rental expense for all operating leases was \$2,539,989 and \$2,493,746 for the years ended June 30, 2017 and 2016, respectively.

**Note 9: Retirement Benefit Plans**

The Corporation has a defined contribution pension plan for employees who meet certain length of service requirements. The Corporation contributes 8.50% and the employee contributes 5.50% of the employee's annual salary. The Corporation's expense related to this plan was \$1,490,196 and \$1,416,132 for the years ended June 30, 2017 and 2016, respectively.

**Note 10: Significant Estimates, Concentrations and Contingencies**

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

**Cash**

At June 30, 2017 and 2016, the Corporation's cash accounts exceeded federally insured limits by approximately \$8,200,000 and \$9,700,000, respectively.

# **Kansas Athletics, Incorporated and Subsidiary**

## **Notes to Consolidated Financial Statements**

### **June 30, 2017 and 2016**

#### ***Contributions Receivable***

Significant estimates for contributions receivable are described in Note 1. There were no concentration of contributions receivable as of June 30, 2017 and 2016.

#### ***Investments***

The Corporation invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying consolidated statements of financial position. Additional estimates and judgments relating to investments and fair value measurements are described in Note 3.

#### ***Property and Equipment***

Significant estimates relating to property and equipment are described in Note 1.

#### ***University Bond Obligation***

In July 2005, the Corporation entered into a contribution agreement with the University to fund certain expenses and bond obligations of the University in conjunction with renovations and additions to the University's student recreation center. The contribution agreement was pledged as security on the Kansas Development Finance Authority Revenue Bonds, Series 2007E issued by the Kansas Board of Regents on behalf of the University.

In 2014, the agreement was amended to relieve the Corporation of all future obligations. While the amendment does eliminate the Corporation's contractual obligation for future payments to the University, it does not modify the original security agreement on the Series 2007E bonds. Management believes that the possibility of future losses resulting from the security agreement is remote.

#### ***Litigation***

The Corporation may be subject to claims and lawsuits that have been brought directly against the University but that indirectly involve activities of the Corporation. The University and the Corporation evaluate such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of ultimate expected loss, if any, for each of these matters. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.