

**UNIVERSITY OF GEORGIA RESEARCH
FOUNDATION, INC.**

FINANCIAL STATEMENTS

As of and for the Year Ended June 30, 2017

And Report of Independent Auditor

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.

TABLE OF CONTENTS

REPORT OF INDEPENDENT AUDITOR	1-2
MANAGEMENT’S DISCUSSION AND ANALYSIS	3-7
FINANCIAL STATEMENTS	
Statement of Net Position	8-9
Statement of Revenues, Expenses, and Changes in Net Position.....	10
Statement of Cash Flows.....	11-12
Notes to the Financial Statements.....	13-34
REPORT OF INDEPENDENT AUDITOR ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	35-36

Report of Independent Auditor

The Audit Committee of the Board of Directors
University of Georgia Research Foundation, Inc.
Athens, Georgia

We have audited the accompanying financial statements of the business-type activities of the University of Georgia Research Foundation, Inc. (the "Research Foundation"), an affiliate of the University of Georgia, which is a unit of the University System of Georgia, which is an organizational unit of the state of Georgia, which comprise the statement of net position as of June 30, 2017, and the related statements of revenues, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Research Foundation, as of June 30, 2017, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2 to the financial statements, during the year ended June 30, 2017, the Research Foundation adopted new accounting guidance, Statement of Governmental Accounting Standard (“SGAS”) No. 80, *Blending Requirements for Certain Component Units – an amendment of GASB Statement No. 14*. Our opinion is not modified with respect to this matter.

Other Matters***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management’s discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management’s responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 14, 2017, on our consideration of the Research Foundation’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Research Foundation’s internal control over financial reporting and compliance.



Augusta, Georgia
September 14, 2017

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Introduction

In compliance with reporting standards the University of Georgia Research Foundation, Inc. (the "Research Foundation") and the UGA Real Estate Foundation, Inc. (the "Real Estate Foundation") are treated as a single entity and financial information is shown using a blended presentation. The Research Foundation and the Real Estate Foundation are referred to collectively as the "Foundations".

The Research Foundation was incorporated under the laws of the state of Georgia as a nonprofit corporation on November 17, 1978. The Research Foundation qualifies as a tax-exempt corporation under Section 501(c)(3) of the Internal Revenue Code.

The Research Foundation is organized to fulfill broad scientific, literary, educational, and charitable purposes and operates to enhance the three-pronged mission of the University of Georgia (the "University") of teaching, research, and public service. The Research Foundation contributes to the research function of the University by securing research contracts, grants, and awards from individuals, institutions, private organizations, and government agencies for the performance of sponsored research in the various University colleges, schools, departments, and other units.

In the Intellectual Property Administration Agreement dated November 8, 1995, the Board of Regents of the University System of Georgia (the "Board of Regents") authorized the Research Foundation to serve as the official recipient of all research contracts, grants, and awards for the conduct of sponsored research at the University. The Intellectual Property Administration Agreement also assigned to the Research Foundation all of the Board of Regents' rights, title, and interest in intellectual property developed by University personnel. In addition, the Research Foundation administers, protects, and licenses this intellectual property.

The Research Foundation is the sole member of the Real Estate Foundation which was incorporated under the laws of the state of Georgia as a nonprofit corporation in 1999 and qualifies as a tax-exempt corporation under Section 501(c)(3) of the Internal Revenue Code. The Real Estate Foundation was incorporated for the purpose of managing and improving various real estate assets for the benefit of the University, governed by the Board of Regents. The Real Estate Foundation may also provide support to the Board of Regents and colleges and universities of the University System of Georgia. The Real Estate Foundation has created multiple limited liability companies of which it is the sole member. These entities are set up in order to construct, finance, own, and lease real estate projects.

Description of the Financial Statements

The *Statement of Net Position*, *Statement of Revenues, Expenses, and Changes in Net Position*, and the *Statement of Cash Flows* are designed to provide information which will assist in understanding the financial condition and performance of the Foundations. The Foundations' net position is one indicator of the Foundations' financial health. Over time, increases or decreases in net position are one indicator of the changes in financial condition when considered with other non-financial facts.

The *Statement of Net Position* presents information on the Foundations' assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net position.

The *Statement of Revenues, Expenses, and Changes in Net Position* presents the revenues earned and the expenses incurred during the year. Activities are reported as either operating or non-operating. The financial reporting model classifies investment earnings and changes in the fair value of investments as non-operating revenues. As a result, the financial statements may show operating losses that are then offset by non-operating revenues from a total financial perspective.

The *Statement of Cash Flows* presents information in the form of cash inflows and outflows summarized by operating, capital and noncapital financing, and investing activities.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Financial Highlights

Condensed financial statements are presented for the year ended June 30, 2017, and one prior fiscal year. In the following discussion, Fiscal 2017 and Fiscal 2016 refer to the years ended June 30, 2017 and 2016, respectively.

University of Georgia Research Foundation, Inc.
Condensed Statements of Net Position
June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>	<u>Change</u>	<u>% Change</u>
Assets:				
Current assets	\$ 101,796,445	\$ 85,090,126	\$ 16,706,319	20%
Capital assets, net	19,523,537	19,629,439	(105,902)	-1%
Other noncurrent assets	<u>315,873,263</u>	<u>324,537,525</u>	<u>(8,664,262)</u>	-3%
Total assets	<u>437,193,245</u>	<u>429,257,090</u>	<u>7,936,155</u>	2%
Deferred Outflows of Resources:				
Deferred loss on refundings	<u>16,534,037</u>	<u>12,908,125</u>	<u>3,625,912</u>	28%
Liabilities:				
Current liabilities	76,454,391	66,363,686	10,090,705	15%
Noncurrent liabilities	<u>283,918,259</u>	<u>288,660,411</u>	<u>(4,742,152)</u>	-2%
Total liabilities	<u>360,372,650</u>	<u>355,024,097</u>	<u>5,348,553</u>	2%
Net Position:				
Net investment in capital assets	11,007,315	11,113,217	(105,902)	-1%
Restricted	2,063,519	1,717,920	345,599	20%
Unrestricted	<u>80,283,798</u>	<u>74,309,981</u>	<u>5,973,817</u>	8%
Total net position	<u>\$ 93,354,632</u>	<u>\$ 87,141,118</u>	<u>\$ 6,213,514</u>	7%

Current assets increased by \$16,706,319 from Fiscal 2016 to Fiscal 2017 due to increases in cash and accounts receivable related to sponsored research activity and a net increase in cash related to net project activity, and capital lease operations and restructuring in Fiscal 2017.

Capital assets, which include land, construction in progress, an easement, buildings and improvements, and furniture and fixtures (net of accumulated depreciation) decreased by \$105,902 due primarily to amortization of depreciable capital assets.

Other noncurrent assets primarily include restricted bond proceeds, trustee held funds, capital leases receivable, investments held by investment managers, and other investments. The \$8,664,262 decrease in other noncurrent assets is primarily attributable to the Real Estate Foundation's principal reduction in accordance with the capital lease amortization schedules, and a slight decrease in the market value of investments held by the Research Foundation.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Deferred outflows of resources include deferred loss on refundings that result from the advanced refunding of bond series. Deferred outflows of resources increased \$3,625,912 from Fiscal 2016 to Fiscal 2017 due to the loss on refunding of Real Estate Foundation bonds offset by normal deferred loss amortization.

Current liabilities increased by \$10,090,705 due to increases in accounts payable to the University, accounts payable related to sponsored research, and short-term bond principal.

Noncurrent liabilities decreased by \$4,742,152 from Fiscal 2016 to Fiscal 2017. This decrease is largely due to the annual payments of principal on noncurrent debt. This decrease is offset by an increase in the Real Estate Foundation's bond debt plus premiums due to the issuance of refunding bonds during Fiscal 2017.

Net position represents the difference between the Foundations' assets, liabilities, and deferred outflows/inflows of resources. Total net position at June 30, 2017 and 2016, was \$93,354,632 and \$87,141,118, respectively, which represents an increase of \$6,213,514.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

University of Georgia Research Foundation, Inc.
Condensed Statements of Revenues, Expenses, and Changes in Net Position
Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>	<u>Change</u>	<u>% Change</u>
Operating Revenues:				
Sponsored research	\$ 182,409,293	\$ 160,445,433	\$ 21,963,860	14%
Licensing and royalties and other	8,733,292	9,166,453	(433,161)	-5%
Rental income	4,224,882	4,384,952	(160,070)	-4%
Capital lease interest income	14,616,362	17,050,125	(2,433,763)	-14%
Total operating revenues	<u>209,983,829</u>	<u>191,046,963</u>	<u>18,936,866</u>	10%
Operating Expenses:				
Research subcontracted to UGA	177,729,229	156,356,506	21,372,723	14%
Intellectual property	7,926,373	8,218,165	(291,792)	-4%
Support to UGA	4,463,889	3,665,118	798,771	22%
Project expenses	3,386,626	3,657,679	(271,053)	-7%
Management and general	909,389	1,227,394	(318,005)	-26%
Total operating expenses	<u>194,415,506</u>	<u>173,124,862</u>	<u>21,290,644</u>	12%
Operating income	15,568,323	17,922,101	(2,353,778)	13%
Non-operating Revenues (Expenses)	<u>(9,354,809)</u>	<u>(15,290,558)</u>	<u>5,935,749</u>	-39%
Change in Net Position	6,213,514	2,631,543	3,581,971	136%
Net position – beginning of year	<u>87,141,118</u>	<u>84,509,575</u>	<u>2,631,543</u>	3%
Net position – end of year	<u>\$ 93,354,632</u>	<u>\$ 87,141,118</u>	<u>\$ 6,213,514</u>	7%

Operating revenues consist primarily of sponsored research, licensing and royalties, interest earned on capital leases, and rental income. During Fiscal 2017, operating revenues increased \$18,936,866 due to increases in sponsored research revenue offset by decreases in revenue following capital and operating lease restructures.

Operating expenses increased by \$21,290,644 primarily due to an increase in sponsored research.

Non-operating revenues and expenses consist mostly of investment income, the change in fair value of investments, and interest expense. For Fiscal 2017, non-operating expenses decreased \$5,935,749 due to decreased investment income, interest expense, and loss on the disposition of assets and liabilities incurred in Fiscal 2016. These decreases are offset by an increase in the fair market value of investments.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

University of Georgia Research Foundation, Inc.
Condensed Statements of Cash Flows
Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>	<u>Change</u>	<u>% Change</u>
Cash flows from operating activities	\$ 26,864,975	\$ 17,309,645	\$ 9,555,330	55%
Cash flows from capital and related financing activities	(20,957,640)	(23,120,848)	2,163,208	9%
Cash flows from investing activities	<u>3,587,139</u>	<u>(5,033,045)</u>	<u>8,620,184</u>	171%
Net change in cash and cash equivalents	9,494,474	(10,844,248)	20,338,722	188%
Cash and cash equivalents – beginning of year	<u>35,061,328</u>	<u>45,905,576</u>	<u>(10,844,248)</u>	-24%
Cash and cash equivalents – end of year	<u>\$ 44,555,802</u>	<u>\$ 35,061,328</u>	<u>\$ 9,494,474</u>	27%

Cash flows from operations primarily include receipts from research sponsors and licensees (net of disbursements for operations), rental income, principal and interest payments on capital leases receivable, and receipts on reimbursable project costs. The increase in net cash flows from operating activities in Fiscal 2017 is largely due to the timing of increased payments for sponsored research offset by decreased cash provided as a result of various lease restructures.

Cash flows from capital and related financing activities are related to capital expenditures, proceeds from new bond issuances, payments on the revolving credit agreement, proceeds from the transfer of assets, and bond debt payments of principal and interest. The decrease in cash used from Fiscal 2016 to Fiscal 2017 was due primarily to decreased cash used by debt and interest payments, and the partial repayment of the revolving credit agreement.

Cash flows from investing activities are comprised of proceeds from sales and maturities of investments, purchases of investments, and interest earned on investments. Significantly more cash was provided by these activities in Fiscal 2017 than in Fiscal 2016 as a result of investment sales exceeding investment purchases.

Economic Outlook

Nationally, research funding and specifically federal research funding remains competitive. The Research Foundation's sponsored research spending increased for the third consecutive year in Fiscal 2017 following a short downward trend in the preceding three years. University faculty are actively seeking new research award opportunities from a variety of funding sources and successfully compete for limited awards. Additionally, the Research Foundation continues to leverage commercialization opportunities with economic potential to provide new revenue streams.

The Real Estate Foundation ended Fiscal 2017 with a strong financial base and continues to support the real estate and facility needs of the University as evidenced in the number and broad spectrum focus of its construction and associated projects.

Questions concerning this report or requests for additional information should be directed to University of Georgia, University Business and Accounting Services at (706) 542-6860 or at 324 Business Services Building, 456 E. Broad Street, Athens, GA 30602.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
STATEMENT OF NET POSITION

JUNE 30, 2017

	Research Foundation	Component Unit Real Estate Foundation	Total
ASSETS			
Current Assets			
Cash and Cash Equivalents	\$ 17,571,113	\$ 19,156,122	\$ 36,727,235
Sponsored Research, Licensing, and Royalties Receivable	35,096,248	-	35,096,248
Accounts Receivable from the University and Affiliates	982,712	-	982,712
Funds Deposited with the University	20,382,914	-	20,382,914
Prepaid Expenses and Other Current Assets	14,676	212,573	227,249
Capital Lease Interest Receivable, Current Portion	-	389,746	389,746
Capital Leases Receivable, Current Portion	-	7,990,341	7,990,341
Total Current Assets	<u>74,047,663</u>	<u>27,748,782</u>	<u>101,796,445</u>
Noncurrent Assets			
Bond Proceeds Restricted for Construction, Debt Service, and Reserves	-	5,765,025	5,765,025
Operating Funds Held by Trustee Investments	38,673,811	-	38,673,811
Investments Held by UGAF	-	11,501,003	11,501,003
Investment in GRA Venture Fund	754,033	-	754,033
Capital Lease Receivable, Noncurrent Portion	-	257,115,849	257,115,849
Capital Assets not being Depreciated			
Land	110,000	15,724,224	15,834,224
Construction in Progress	-	21,884	21,884
Easement	-	1,835,296	1,835,296
Capital Assets, net of Accumulated Depreciation	-	1,832,133	1,832,133
Total Noncurrent Assets	<u>39,537,844</u>	<u>295,858,956</u>	<u>335,396,800</u>
Total Assets	<u>\$ 113,585,507</u>	<u>\$ 323,607,738</u>	<u>\$ 437,193,245</u>
Deferred Outflows of Resources			
Deferred Loss on Refundings	<u>\$ -</u>	<u>\$ 16,534,037</u>	<u>\$ 16,534,037</u>

The accompanying notes to the financial statements are an integral part of this statement.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
STATEMENT OF NET POSITION (CONTINUED)

JUNE 30, 2017

	Research Foundation	Component Unit Real Estate Foundation	Total
LIABILITIES			
Current Liabilities			
Accounts Payable to the University and Affiliates	\$ 40,224,832	\$ 9,337	\$ 40,234,169
Funds Received for Sponsored Research	22,540,419	-	22,540,419
Accounts Payable and Accrued Liabilities	1,296,742	-	1,296,742
Unearned Revenue	6,275	-	6,275
Accrued Interest Payable	-	591,779	591,779
Advance Rent and Lease Payment Receipts	-	2,154,508	2,154,508
Lease Rent Liability, Current Portion	-	25,499	25,499
Bonds Payable, Current Portion	-	9,605,000	9,605,000
Total Current Liabilities	<u>64,068,268</u>	<u>12,386,123</u>	<u>76,454,391</u>
Noncurrent Liabilities			
Lease Rent Liability, Noncurrent Portion	-	1,769,494	1,769,494
Revolving Credit Agreement, Noncurrent Portion	-	8,516,222	8,516,222
Bonds Payable, Noncurrent Portion	-	273,632,543	273,632,543
Total Noncurrent Liabilities	<u>-</u>	<u>283,918,259</u>	<u>283,918,259</u>
Total Liabilities	<u>64,068,268</u>	<u>296,304,382</u>	<u>360,372,650</u>
NET POSITION			
Net Investment in Capital Assets	110,000	10,897,315	11,007,315
Restricted for:			
Future Repairs and Replacements of Real Property	-	2,063,519	2,063,519
Unrestricted	49,407,239	30,876,559	80,283,798
Total Net Position	<u>\$ 49,517,239</u>	<u>\$ 43,837,393</u>	<u>\$ 93,354,632</u>

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

YEAR ENDED JUNE 30, 2017

	<u>Component Unit</u>		<u>Total</u>
	<u>Research Foundation</u>	<u>Real Estate Foundation</u>	
Operating Revenues			
Sponsored Research	\$ 182,409,293	\$ -	\$ 182,409,293
Licensing and Royalties	8,733,292	-	8,733,292
Rental Income	598,259	3,626,623	4,224,882
Capital Lease Interest Income	-	14,616,362	14,616,362
Total Operating Revenues	<u>191,740,844</u>	<u>18,242,985</u>	<u>209,983,829</u>
Operating Expenses			
Research Subcontracted to the University (including facilities and administrative cost reimbursements)	177,729,229	-	177,729,229
Licensing and Royalty Distributions	6,649,123	-	6,649,123
Licenses and Intellectual Property	1,277,250	-	1,277,250
Support to the University	4,463,889	-	4,463,889
Project Expenses	-	3,386,626	3,386,626
Management and General	427,558	481,831	909,389
Total Operating Expenses	<u>190,547,049</u>	<u>3,868,457</u>	<u>194,415,506</u>
Total Operating Income	<u>1,193,795</u>	<u>14,374,528</u>	<u>15,568,323</u>
Non-operating Revenue (Expenses)			
Investment Income	756,197	324,849	1,081,046
Change in Fair Value of Investments	2,150,263	-	2,150,263
Interest Expense, Net	-	(12,388,604)	(12,388,604)
Loss on Investment in GRA Venture Fund	(205,249)	-	(205,249)
Other	-	7,735	7,735
Total Non-operating Revenue (Expenses)	<u>2,701,211</u>	<u>(12,056,020)</u>	<u>(9,354,809)</u>
Change in Net Position	3,895,006	2,318,508	6,213,514
Net Position			
Beginning of Year	<u>45,622,233</u>	<u>41,518,885</u>	<u>87,141,118</u>
End of Year	<u>\$ 49,517,239</u>	<u>\$ 43,837,393</u>	<u>\$ 93,354,632</u>

The accompanying notes to the financial statements are an integral part of this statement.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2017

	Research Foundation	Component Unit Real Estate Foundation	Total
Cash flows from operating activities			
Receipts from research sponsors	\$ 179,257,362	\$ -	\$ 179,257,362
Receipts from licensing, royalties, and other	8,733,291	-	8,733,291
Receipts from the University	8,654,781	-	8,654,781
Receipts from rental income	598,260	3,625,139	4,223,399
Receipts of principal on capital leases	-	6,500,191	6,500,191
Receipts of interest on capital leases	-	15,993,436	15,993,436
Receipts for payments reimbursable by the University and affiliates	-	761,237	761,237
Sponsored research payments to the University	(180,331,063)	-	(180,331,063)
Payments for licensing and royalty distributions and other	(5,024,639)	-	(5,024,639)
Payments to the University	(7,331,644)	-	(7,331,644)
Payments to suppliers	(416,527)	(3,392,718)	(3,809,245)
Payments reimbursable by the University and affiliates	-	(761,237)	(761,237)
Other operating payments	-	(894)	(894)
Net cash from operating activities	<u>4,139,821</u>	<u>22,725,154</u>	<u>26,864,975</u>
Cash flows from capital and related financing activities:			
Capital expenditures	-	(9,175)	(9,175)
Proceeds from sale of bonds	-	625,425	625,425
Payments for bond issuance costs	-	(621,100)	(621,100)
Interest payments on long-term debt	-	(11,382,790)	(11,382,790)
Principal repayment on bonds payable	-	(9,570,000)	(9,570,000)
Net cash from capital and related financing activities	<u>-</u>	<u>(20,957,640)</u>	<u>(20,957,640)</u>
Cash flows from investing activities			
Proceeds from sales and maturities of investments	23,992,645	-	23,992,645
Purchases of investments	(20,491,140)	(262,348)	(20,753,488)
Investment in GRA Venture Fund, net of distributions	(10,201)	-	(10,201)
Net payments for foreign currency fluctuations	-	7,735	7,735
Investment income	-	350,448	350,448
Net cash from investing activities	<u>3,491,304</u>	<u>95,835</u>	<u>3,587,139</u>
Net increase in cash and cash equivalents	7,631,125	1,863,349	9,494,474
Cash and cash equivalents			
Beginning of year	9,939,988	25,121,340	35,061,328
End of year	<u>\$ 17,571,113</u>	<u>\$ 26,984,689</u>	<u>\$ 44,555,802</u>

The accompanying notes to the financial statements are an integral part of this statement.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
STATEMENT OF CASH FLOWS (CONTINUED)

YEAR ENDED JUNE 30, 2017

	Research Foundation	Component Unit Real Estate Foundation	Total
Reconciliation of operating income to net cash from operating activities			
Operating income	\$ 1,193,795	\$ 14,374,528	\$ 15,568,323
Adjustments to reconcile operating income to net cash from operating activities			
Depreciation	-	115,077	115,077
Straight-line rent expense adjustment	-	423,737	423,737
Receipts of principal on capital leases	-	6,500,191	6,500,191
Changes in assets and liabilities			
Accounts receivable	(3,151,930)	1,472	(3,150,458)
Capital lease interest receivable	-	1,438,732	1,438,732
Prepaid expenses and other current assets	38,899	8,426	47,325
Accounts payable to the University and affiliates	5,894,503	(29,538)	5,864,965
Accounts payable and accrued liabilities	164,554	(44,329)	120,225
Advance rent least payment receipts	-	(63,142)	(63,142)
Net cash from operating activities	<u>\$ 4,139,821</u>	<u>\$ 22,725,154</u>	<u>\$ 26,864,975</u>
Reconciliation of cash and cash equivalents to the statement of net position			
Cash and cash equivalents, per the statement of net position	\$ 17,571,113	\$ 19,156,122	\$ 36,727,235
Cash and cash equivalents included in bond proceeds restricted for construction, debt service, and reserves	-	5,765,025	5,765,025
Cash and cash equivalents included in operating funds held by trustee	-	2,063,542	2,063,542
Total cash and cash equivalents	<u>\$ 17,571,113</u>	<u>\$ 26,984,689</u>	<u>\$ 44,555,802</u>
Schedule of noncash investing activity			
Increase in fair value of investments	\$ 2,150,263	\$ -	\$ 2,150,263
Investment income, reinvested	\$ 756,197	\$ -	\$ 756,197
Loss on investment in GRA Venture Fund	\$ (205,249)	\$ -	\$ (205,249)
Bonds payable refunded through new bond issue and related cost of issuance	\$ -	\$ 60,969,117	\$ 60,969,117

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 1—Organization

The University of Georgia Research Foundation, Inc. (the “Research Foundation”) was established in November 1978 to contribute to the educational, research, and service functions of the University of Georgia (the “University”) in securing gifts, contributions, and grants from individuals, private organizations, and public agencies and in obtaining contracts with such individuals or entities for the performance of sponsored research, development, education, or other programs by the various colleges, schools, departments, or other units of the University.

All research grants awarded to the Research Foundation are subcontracted to the University, which is responsible for the fiscal administration of the grants on behalf of the Research Foundation and the University.

Effective July 1, 2007, the Research Foundation became the sole member of the UGA Real Estate Foundation, Inc. (the “Real Estate Foundation”). The Real Estate Foundation is a not-for-profit foundation that was chartered in 1999 and manages and improves various real estate assets for the benefit of the University, governed by the Board of Regents of the University System of Georgia (the “Board of Regents”). The Real Estate Foundation may also provide support to the Board of Regents and colleges and universities of the University System of Georgia. The Real Estate Foundation has created several limited liability companies of which it is the sole member for various purposes including constructing, financing, owning, and leasing real estate projects.

The Real Estate Foundation is presented as a blended component unit. The Research Foundation and the Real Estate Foundation are collectively referred to as the “Foundations”.

Note 2—Summary of significant accounting policies

Basis of Presentation – The Foundations’ financial statements have been prepared in accordance with the accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (“GASB”).

The financial statement presentation provides a comprehensive, entity-wide perspective of the Foundations’ assets, liabilities, deferred inflows/outflows of resources, net position, revenues, expenses, changes in net position, and cash flows. As required by accounting principles generally accepted in the United States of America as prescribed by GASB, the financial position and activities of component units are shown using a blended presentation in the government-wide financial statements, which consist of the *Statement of Net Position*, the *Statement of Revenues, Expenses, and Changes in Net Position* and the *Statement of Cash Flows*. In addition, these standards require the presentation of Management’s Discussion and Analysis (“MD&A”). The MD&A is considered to be required supplemental information and precedes the financial statements.

Reporting Entity – In accordance with the criteria in Statement of Governmental Accounting Standard (“SGAS”) No. 61, *The Financial Reporting Entity*, the Research Foundation is a legally separate tax exempt organization whose activities primarily support the University, a unit of the University System of Georgia (an organizational unit of the state of Georgia). The Research Foundation is considered an affiliated organization of the University and due to its financial significance, its financial activities are included in the University and University System of Georgia’s reports. The State Accounting Office determined component units of the state of Georgia, as required by SGAS No. 61, should not be assessed in relation to their significance to the University. Accordingly, the Research Foundation qualifies for treatment as a component unit of the State of Georgia.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies (continued)

The Real Estate Foundation qualifies as a component unit of the Research Foundation. The *Statement of Net Position*, the *Statement of Revenues, Expenses, and Changes in Net Position*, and the *Statement of Cash Flows* of the Real Estate Foundation are shown using a blended presentation with the Research Foundation as required by government accounting standards.

These statements are the primary financial statements of the Research Foundation. Separately issued comparative financial statements for the Real Estate Foundation may be obtained at the following address: UGA Real Estate Foundation, Inc., c/o University Business and Accounting Services, 324 Business Services Building, 456 E. Broad Street, Athens, GA 30602.

Basis of Accounting – For financial reporting purposes, the Foundations are considered special-purpose government entities engaged only in business-type activities. Accordingly, the Foundations' financial statements have been presented using the economic resources 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.

Cash and Cash Equivalents – The Foundations consider all short-term investments with an original maturity of three months or less to be cash equivalents. Investments in the Board of Regents Short-term Fund are carried at fair value. Short-term investments, which consist of money markets, certificates of deposit, and non-participating repurchase agreements, are carried at cost.

Operating Funds Held by Trustee – Amounts transferred in from cash accounts are held by an independent trustee for the purpose of paying operating expenses and funding reserves for future obligations. From time to time, investments are made by the trustee in accordance with the trust indenture.

Bond Proceeds Restricted for Construction, Debt Service, and Reserves – Proceeds from bond issuances are held by an independent trustee and are restricted for the purpose of funding construction costs, interest, administrative fees, debt service reserves, and costs of issuance associated with the bond offerings. From time to time, investments are made by the trustee in accordance with the trust indenture.

Investments – In accordance with SGAS No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, the Foundations are required to present certain investments at their fair value if the investment has a readily determined market value. Investments are carried at market value. Realized gains and losses are computed using the specific identification method.

Investments in Affiliated Companies and Partnerships – The Research Foundation accounts for its interest in a limited liability company for which the Research Foundation does not have significant ownership or control, using the cost method. Contributions are shown at cost less distributions of return of initial investment. Revenue is recognized for dividends received that are distributed from net accumulated earnings of the company since the date of acquisition by the Research Foundation. Losses are recognized if losses incurred by the company are determined to be other than a temporary decrease in value of the investment. Investments in startup companies are deemed to have a readily determinable fair market value when the stock becomes publicly traded.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies (continued)

Capital Leases Receivable – The Real Estate Foundation enters into lease contracts of real property as a lessor. The terms and conditions of these contracts are assessed and the leases are classified as operating leases or capital leases according to their economic substance. When making such an assessment, the Real Estate Foundation focuses on the following aspects: a) transfer of ownership of the asset to the lessee at the end of the lease term; b) existence of a bargain purchase option held by the lessee; c) whether the lease term is for the major part of the economic life of the asset; and d) whether the present value of the minimum lease payments is substantially equal to the fair value of the leased asset at inception of the lease term. If one or more of the conditions are met, the lease is generally classified as a capital lease. The initial recording of the capital lease receivable is made on the day the real property is placed in service, with a corresponding entry to remove the capital asset using the lesser of the net present value of the lease payments or the fair value of the leased property. Capital leases are amortized over the term of the lease using the effective interest rate – the implicit rate that exactly discounts estimated future cash receipts through the expected life of the lease. Lease payments are allocated between the principal and interest components. Capital leases receivable consist of capital lease payments due for real property owned by the University. Collectability of these lease payments is reasonably assured and no allowance for uncollectible amounts has been established.

Capital Assets – Expenditures for maintenance and repairs are charged to operations as incurred, while renewals and betterments are capitalized.

Furniture and equipment are stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets of seven years.

Real property includes buildings and improvements stated at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the lesser of the estimated useful life of the related asset of 10 to 30 years or the remaining term on the related ground or air rights leases. Land and easements are stated at cost and are not depreciated.

Construction in progress is stated at cost and includes planning, development, and construction costs, as well as capitalized interest. When construction is complete and the asset is placed in use, assets are transferred at cost to real property or transferred to lessees as part of a capital lease agreement.

Capitalized Interest – Interest incurred during construction of real estate projects is capitalized until the underlying assets are ready for their intended use. Interest related to projects financed by tax-exempt borrowings, including periodic amortization of any related discount or premium, is capitalized after reduction for interest earned on temporary investment of the proceeds of those borrowings from the date of borrowing until the specified qualifying assets acquired with those borrowings are ready for their intended use. Interest related to projects financed by taxable borrowings, including periodic amortization of any related discount or premium, does not include a reduction for interest earned on the temporary investment of the proceeds of those borrowings. At the time the qualifying assets are placed in service, amortization of the capitalized interest begins, straight-line, over the estimated useful lives of the related assets.

If a project is determined to be placed in service under a capital lease agreement, the asset, including capitalized interest, is transferred to lessees under a capital lease agreement.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies (continued)

Deferred Outflows/Inflows of Resources – In accordance with SGAS No. 65, *Items Previously Reported as Assets and Liabilities*, the statement of net position reports a separate financial statement element, deferred outflows of resources, which represents a consumption of net position that applies to a future period and will not be recognized as an outflow of resources until that time. The Real Estate Foundation's deferred loss on refundings qualifies for reporting in this category. The deferred loss on refundings results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt using the straight-line method. In addition to liabilities, the statement of net position will at times report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period and will not be recognized as revenue until that time. The Real Estate Foundation does not have any item that qualifies for reporting in this category.

Bonds Payable – The Real Estate Foundation records the net proceeds of tax-exempt and taxable bond financing as a liability upon issuance. Bond proceeds consist of the par value of the bonds issued plus premiums or minus discounts. Bond premiums and discounts are amortized to interest expense using the effective interest method.

Net Position – Net position is classified in three components. Net investment in capital assets consists of capital assets net of accumulated depreciation and is reduced by the outstanding balances of any borrowings used to finance the purchase or construction of those assets. Restricted net position includes amounts restricted by bond indentures for debt service, operating costs, and repair and replacements reserves. Unrestricted net position is not subject to donor or other stipulations imposed by outside sources. The Real Estate Foundation considers several factors in determining whether to use restricted or unrestricted resources when restrictions are met.

Revenue Recognition – Revenue from sponsored research is recognized as expenditures are made for approved research activities, or the Research Foundation has been notified of approved research activities related to the funds received.

A sponsored research receivable is recorded for amounts expended for authorized purposes but not yet reimbursed by research sponsors. Payments by research sponsors in advance of research expenditures are recorded and classified as funds received for sponsored research in the statement of net position. Accounts receivable included amounts due from the University and affiliates. Management believes the amounts due are fully collectible.

Licensing revenues and royalties are derived from licensing of the Research Foundation's intellectual property rights and are generally computed as a royalty based upon a percentage of the licensee's sales of products incorporating the rights licensed from the Research Foundation. Such licensing and royalties are recognized when received except that payments of royalties received in advance of actual sales are initially deferred and subsequently recognized on a straight-line basis over the expected royalty period.

The unrecognized portion of such advance payments is classified as unearned revenues in the statement of net position. The Research Foundation is obligated to distribute a portion of the licensing revenues and royalties pursuant to the University of Georgia Intellectual Property Policy. Such distributions are recorded as expenses when the related revenues are recognized.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies (continued)

Rental income is recognized when earned and collectability of the associated receivable is reasonably assured. Rental income consists of the repair and replacement portion of the total capital lease payment and is recognized on a monthly basis in accordance with the related lease agreement. Advance rent receipts represent rental payments received but not yet earned.

Capital lease interest income is recorded per the related capital lease amortization schedule simultaneously with the rental income described above. Amounts are offset by rebates to the University related to savings realized by the Real Estate Foundation due to advance refunding of bonds payable and the early extinguishment of certain bonds payable for projects transferred to the University. Advance lease payment receipts represent both the interest and principal components of capital lease payments received but not yet earned.

Operating and Non-Operating Revenues – The financial statements distinguish between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with sponsored research, and licensing and royalty agreements (the Research Foundation’s principal activities), and maintaining and leasing real property (the Real Estate Foundation’s principal activities). Non-exchange revenues, including investment income and net unrealized and realized gains and losses on investments, are reported as non-operating revenues. Interest and financing costs are reported as non-operating expenses. Operating expenses are all expenses incurred in the course of obtaining sponsored research grants, licensing and royalty agreements, providing support to the University, and to maintain and lease real property.

Income Taxes – The Foundations are exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (the “Code”), whereby only unrelated business income, as defined by Section 512(a)(1) of the Code, is subject to federal income tax. In addition, they are not classified as a private foundation under Section 509(a) of the Code based on determinations received from the Internal Revenue Service.

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

Implementation of New Accounting Pronouncement – During the year ended June 30, 2017, the Foundations implemented SGAS No. 80, *Blending Requirements for Certain Component Units – an amendment of GASB Statement No. 14*, which amends the blending requirements for the financial statement presentation of component units. SGAS No. 80 establishes an additional criterion which requires blending of a component unit that is incorporated as a not-for-profit corporation in which the primary government is the sole corporate member.

As a result of implementing SGAS No. 80, the Real Estate Foundation is presented as a blended component unit instead of as a discretely presented component unit.

The July 1, 2016 beginning net position in the statement of revenues, expenditures, and changes in net position was restated from \$45,622,233 to retroactively add the net position of the Real Estate Foundation in the amount of \$41,518,885. The resulting restated beginning net position is \$87,141,118.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 3—Deposits and investments

A. Deposits

At June 30, 2017, the bank and investment account values of the Foundations' deposits, including interest bearing checking accounts, cash held in managed investment accounts, and cash equivalents held by trustees, were \$8,764,740.

Custodial credit risk

The custodial credit risk for deposits is the risk that in the event of a bank failure, the Foundations' deposits may not be recovered. The Foundations do not have a deposit policy for custodial credit risk. The Foundations place their cash and cash equivalents on deposit with financial institutions in the United States and Italy. For deposits with financial institutions in the United States, the Federal Deposit Insurance Corporation ("FDIC") covers \$250,000 for substantially all depository accounts. The Foundations from time to time may have amounts on deposit in excess of these insured limits.

As of June 30, 2017, the bank balance of the Foundations' deposits is presented below by category of risk.

	FDIC Insured	Collateralized by U.S. Securities	Uninsured and Uncollateralized	Total
Checking Accounts	\$ 943	\$ -	\$ 37,832	\$ 38,775
Cash Held in Investments	-	-	6,662,423	6,662,423
Funds Held by Trustee	-	-	2,063,542	2,063,542
Total Deposits	\$ 943	\$ -	\$ 8,763,797	\$ 8,764,740

The uninsured and uncollateralized deposits classified as "Funds Held by Trustee" are primarily invested in Fidelity Institutional Money Market Treasury Portfolio, a short-term money market fund.

Foreign currency risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect a deposit. During the year ended June 30, 2017, the Foundations' deposits increased by \$7,735, due to foreign currency fluctuations between the Euro and the dollar on cash balances held in banks related to Real Estate Foundation operations in Italy. Amounts held in foreign currency denominations are valued at \$37,832 as of June 30, 2017.

B. Investments

The Foundations maintain separate investment policies. The Research Foundation's policy describes its investment objectives and risk posture, identifies a spending rate, establishes asset allocation and investment guidelines, and specifies investment performance criteria. The Real Estate Foundation's policy establishes objectives, specifies allowable investments, sets target investment mixes, and provides investment guidelines.

During the year ended June 30, 2016, the Real Estate Foundation entered into an agreement with the University of Georgia Foundation ("UGAF") in order to establish the UGA Real Estate Short-Term Holding Fund (the "UGAF Fund") to be managed and held by UGAF. The UGAF Fund serves as a depository account and is separately managed and accounted for by UGAF. The Real Estate Foundation's Board of Trustees (the "Real Estate Board") is responsible for investing decisions. As of June 30, 2017, investments held by UGAF included fixed-income mutual funds in the amount of \$11,501,003.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 3—Deposits and investments (continued)

B. Investments (continued)

The Foundations' investments at June 30, 2017, are presented below. All investments are presented by investment type and debt securities are presented by maturity.

<u>Investment Type</u>	<u>Total</u>	<u>Investment Maturity</u>			<u>More Than 10 Years</u>
		<u>Less Than 1 Year</u>	<u>1-5 Years</u>	<u>6-10 Years</u>	
Debt Securities					
U.S. Treasuries	\$ 3,481,919	\$ 825,792	\$ 1,612,444	\$ 562,569	\$ 481,114
U.S. Agencies - Implicitly Guaranteed	75,177	75,177	-	-	-
Corporate Debt	6,472,625	2,712,153	2,323,224	915,435	521,813
Municipal Debt	388,260	52,237	118,966	18,854	198,203
Foreign Government Debt	128,550	-	128,550	-	-
Repurchase Agreements	21,998,762	21,998,762	-	-	-
Repurchase Agreements Held by Trustee	5,765,025	-	-	-	5,765,025
	<u>38,310,318</u>	<u>\$ 25,664,121</u>	<u>\$ 4,183,184</u>	<u>\$ 1,496,858</u>	<u>\$ 6,966,155</u>
Other Investments					
Equity Mutual Funds - Domestic	5,145,925				
Equity Mutual Funds - International	5,422,155				
Equity Mutual Funds - Global	5,399,653				
Bond Mutual Funds - Domestic	1,953,142				
Equity Securities - Domestic	720,353				
Equity ETF	1,956,826				
Managed Futures / Hedge Funds	7,529,226				
Mutual Funds Held by UGAF	11,501,003				
Board of Regents - Short-term Fund	8,523,598				
Total Investments	<u>\$ 86,462,199</u>				

Repurchase agreements of \$11,404,000 held by the Research Foundation are included in cash and cash equivalents on the statement of net position. Repurchase agreements held by the Real Estate Foundation of \$10,594,762 and the Board of Regents – Short-term Fund are included in cash and cash equivalents on the statement of net position. Repurchase agreements held by the Real Estate Foundation of \$5,765,025 are included in bond proceeds restricted for construction, debt service, and reserves on the statement of net position.

Interest rate risk

Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. The Research Foundation's policy for managing interest rate risk is to evaluate investments in light of their ability to provide needed cash flow while still preserving long-term earning and investment potential. The Real Estate Foundation's policy for managing interest rate risk is to invest primarily in short-term or intermediate-term investments.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 3—Deposits and investments (continued)

B. Investments (continued)

Custodial credit risk

Custodial credit risk for investments is the risk that, in the event of a failure of the counterparty to a transaction, the Foundations will not be able to recover the value of the investment. The Foundations do not have a formal policy for managing custodial credit risk for investments. At June 30, 2017, \$39,030,670 of the Foundations' applicable investments were uninsured and held by the investment's counterparty in the Foundations' name.

Credit quality risk

Credit quality risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Research Foundation's investment policy specifies acceptable categories of fixed income securities, the overall rating of bond portfolios, and specifies an investment limit for foreign securities. The Real Estate Foundation's policy is to invest primarily in a diversified portfolio of investment grade debt securities and fixed income mutual funds.

The Foundations' investments at June 30, 2017, are presented below. All investments are presented by investment type and fixed income securities are presented by credit quality ratings.

Quality Ratings	Total	Rated Investments			
		U.S. Agencies	Corporate, Municipal, and Foreign Government Bonds	Mutual Funds	Repurchase Agreements
Moody's					
Aaa	\$ 5,961,183	\$ 75,177	\$ 120,981	\$ -	\$ 5,765,025
Aa1	209,037	-	209,037	-	-
Aa2	215,261	-	215,261	-	-
Aa3	303,783	-	303,783	-	-
A1	921,079	-	921,079	-	-
A2	278,947	-	278,947	-	-
A3	1,647,712	-	1,647,712	-	-
Baa1	976,856	-	976,856	-	-
Baa2	1,047,938	-	1,047,938	-	-
Baa3	661,075	-	661,075	-	-
Ba2	522,875	-	522,875	-	-
Standard & Poor's					
BBB	31,379	-	31,379	-	-
Morningstar					
5-Star	3,711,297	-	-	3,711,297	-
4-Star	16,000,530	-	-	16,000,530	-
3-Star	1,953,142	-	-	1,953,142	-
Unrated	29,808,183	-	52,512	7,756,909	21,998,762
	<u>64,250,277</u>	<u>\$ 75,177</u>	<u>\$ 6,989,435</u>	<u>\$ 29,421,878</u>	<u>\$ 27,763,787</u>
Exempt Investments					
U. S. Treasuries	3,481,919				
Equity Securities - Domestic	720,353				
Equity ETF	1,956,826				
Managed Futures/Hedge Funds	7,529,226				
Board of Regents - Short-term Fund	8,523,598				
	<u>\$ 86,462,199</u>				

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 3—Deposits and investments (continued)

B. Investments (continued)

The Board of Regents Short-term Fund is part of the Board of Regents Investment Pool which is not registered with the Securities and Exchange Commission as an investment company. The fair value of investments is determined daily. The pool does not issue shares. Each participant is allocated a pro rata share of each investment at fair value along with a pro rata share of the interest that it earns. Participation in the Board of Regents Investment Pool is voluntary. The Board of Regents Investment Pool is not rated. Additional information on the Board of Regents Investment Pool is disclosed in the audited Financial Statements of the Board of Regents of the University System of Georgia - System Office (oversight unit). This audit can be obtained from the Georgia Department of Audits - Education Audit Division or on their web site at <http://www.audits.ga.gov>.

Concentration of credit risk

Concentration of credit risk is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. The Research Foundation manages concentration of credit risk by including limits in its investment policy on holdings of individual classes of investments, holdings with a single manager, and the diversity of individual portfolios. For short-term investments, the investment security mix is driven by the management of investments to meet cash needs. For long-term investments, equities comprise 30-70%, bonds 20-70%, and alternative investments can range 0-40%.

The Real Estate Foundation's policy for managing concentration of credit risk is to invest primarily in a diversified portfolio of investment grade debt securities and fixed income mutual funds.

As of June 30, 2017, investments and repurchase agreement-underlying securities in a single issuer where those investments are 5% or more of total investments were as follows:

Federal National Mortgage Association	13%
Federal Home Loan Mortgage Corporation	9%
Federal Home Loan Bank	7%

Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds and external investment pools are exempt from concentration of credit risk disclosure.

Foreign currency risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The Foundations do not have a formal policy for managing foreign currency risk; however, investments do not include securities denominated in currencies other than the U.S. dollar.

Note 4—Other investments – cost method

During 2009, the Research Foundation made a commitment to invest \$1,000,000 in GRA Venture Fund (T. E.), LLC, (the "GRA Fund"). The GRA Fund was created by the Georgia legislature whereby State funds and funds from profit and not-for-profit entities will be combined to provide seed and early stage venture financing for businesses formed around intellectual property resulting from Georgia Research Alliance (the "GRA") universities. In July 2015, the Research Foundation made an additional commitment to invest \$1,000,000.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 4—Other investments – cost method (continued)

During fiscal year 2017, the Research Foundation made total contributions of \$112,606 and received \$102,405 in distributions of return of initial investment.

A fair value is not estimated for the investment. At June 30, 2017, the Research Foundation recognized its share of losses incurred by the Fund amounting to \$205,249. The total investment by the Research Foundation is shown at cost less distributions of return of initial investment and other than temporary losses.

**GRA Venture Fund (T. E.), LLC –
capital contribution, at cost, net of
distributions and losses**

2009 commitment	\$	487,148
2015 commitment		266,885
	\$	<u>754,033</u>

Note 5—Fair value measurements of assets and liabilities

The Foundations have adopted SGAS No. 72, *Fair Value Measurements and Application*, which requires fair value measurement be classified and disclosed in one of the following three categories (“Fair Value Hierarchy”):

- Level 1 – Quoted prices are available in active markets for identical investments as of the reporting date. The types of investments which would generally be included in Level 1 include listed equity securities, mutual funds, and money market funds. As required by accounting principles generally accepted in the United States of America, the Foundations, to the extent that they hold such investments, does not adjust the quoted price for these investments, even in situations where the Foundations hold a large position and a sale could reasonably impact the quoted price.
- Level 2 – Pricing inputs are observable for the investments, either directly or indirectly, as of the reporting date, but are not the same as those used in Level 1; inputs include comparable market transactions, pricing of similar instruments, values reported by the administrator, and pricing expectations based on internal modeling. Fair value is determined through the use of models or other valuation methodologies. The types of investments which would generally be included in this category include publicly-traded securities with restrictions on disposition, corporate obligations, and U.S. Government and Agency Treasury Inflation Indices.
- Level 3 – Pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investments. The types of investments which would generally be included in this category include debt and equity securities issued by private entities and partnerships. The inputs into the determination of fair value require significant judgment or estimation. Inputs include recent transactions, earnings forecasts, market multiples, and future cash flows.

The table on the following page summarizes the valuation of the Foundations’ financial assets and liabilities measured at fair value on a recurring basis and at net asset value as of June 30, 2017.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 5—Fair value measurements of assets and liabilities (continued)

	Fair Value Measurement			Total
	Level 1	Level 2	Level 3	
Investments by Fair Value Level				
Equity Securities:				
Stocks (by sector)				
Health Care	\$ 720,353	\$ -	\$ -	\$ 720,353
Equity ETF	1,956,826	-	-	1,956,826
Mutual Funds				
Domestic	5,145,925	-	-	5,145,925
International	5,422,155	-	-	5,422,155
Global	5,399,653	-	-	5,399,653
Total Equities	18,644,912	-	-	18,644,912
Investment Pools				
Board of Regents-Short-term Fund	-	8,523,598	-	8,523,598
Total Investment Pools	-	8,523,598	-	8,523,598
Fixed Income:				
U. S. Treasury	-	3,481,919	-	3,481,919
U. S. Agencies - Implicitly Guaranteed		75,177		75,177
Bonds				
Corporate	-	6,472,625	-	6,472,625
Municipal	-	388,260	-	388,260
Foreign Government	-	128,550	-	128,550
Mutual Funds - Domestic	1,953,142	-	-	1,953,142
Mutual Funds Held by UGAF	11,501,003	-	-	11,501,003
Total Fixed Income	13,454,145	10,546,531	-	24,000,676
Investments Measured at Net Asset Value ^(a)				
Multi-Strategy Hedge Funds	-	-	-	4,008,654
Interval ILS Fund	-	-	-	2,006,055
Managed Futures	-	-	-	1,514,517
Total Investments Measured at Net Asset Value ^(a)	-	-	-	7,529,226
Total Investments, Recurring Basis	\$ 32,099,057	\$ 19,070,129	\$ -	\$ 58,698,412

^(a) Certain investments that are measured at fair value using the net asset value per share have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts on the statement of net position.

All assets have been valued using a market approach. There have been no changes in valuation techniques and related inputs.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 5—Fair value measurements of assets and liabilities (continued)

The Foundations' assets where fair value is measured by net asset value of the entity are as follows:

<u>Category</u>	<u>Fair Value</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Interval ILS Fund ^(a)	\$ 2,006,055	Quarterly	21 days
Managed Futures ^(b)	1,514,517	Daily	None
Multi-Strategy Hedge Funds ^(c)	574,040	Quarterly	65 days
Multi-Strategy Hedge Funds ^(c)	3,434,614	Quarterly	95 days
	<u>\$ 7,529,226</u>		

There were no unfunded commitments related to the investments above that calculate net asset value as of June 30, 2017.

- (a) *Interval ILS Fund* – This category includes investments in insurance-linked securities (“ILS”) especially reinsurance related securities. ILS funds invest in both liquid instruments as well as illiquid instruments such as catastrophe bonds, private reinsurance contracts, event-linked bonds, and shares or notes issued in connection with non-proportional reinsurance.
- (b) *Managed Futures* – This category includes investments in diversified hedge funds investing in equity and debt securities as well as currencies and commodities. The allocation strategy primarily is based on trend analysis including identification of emerging trends.
- (c) *Multi-Strategy Hedge Funds* – This category includes investments in multi-strategy off-shore funds. Strategies primarily focus on long/short credit strategies which generally take both long and short positions in credit related instruments, such as corporate bonds, bank loans, traded claims, emerging market debt and credit derivatives, and multi-strategy opportunistic strategies which generally involve portfolio managers exercising discretion in allocating capital among several types of arbitrage, event driven, and directional strategies.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 6—Restricted and Real Estate Board designated assets

Restricted and Real Estate Board designated assets included in Operating Funds Held by Trustee and Bond Proceeds Restricted for Construction, Debt Service, and Reserves are as follows:

Restricted for:	
Debt Service	\$ 5,765,025
Future Repairs and Replacements of Real Property	2,063,519
Total Restricted	<u>7,828,544</u>
Designated for:	
General Operations of the Real Estate Foundation	<u>23</u>
Total Restricted and Designated	<u>\$ 7,828,567</u>

The carrying values of the restricted and Real Estate Board designated cash and cash equivalents and investment balances above are included in the statement of net position as follows:

Operating Funds Held by Trustee	\$ 2,063,542
Bond Proceeds Restricted for Construction, Debt Service, and Reserves	<u>5,765,025</u>
Total Restricted and Designated	<u>\$ 7,828,567</u>

Cash and Cash Equivalents, which include Real Estate Board designated assets, are as follows:

	<u>Research Foundation</u>	<u>Real Estate Foundation</u>	<u>Total</u>
Designated for:			
Debt Service	\$ -	\$ 4,018,315	\$ 4,018,315
Future Repairs and Replacements of Real Property	-	8,778,318	8,778,318
General Operations of the Real Estate Foundation	<u>-</u>	<u>400,000</u>	<u>400,000</u>
Total Designated	-	13,196,633	13,196,633
Undesignated Cash and Cash Equivalents	<u>17,571,113</u>	<u>5,959,489</u>	<u>23,530,602</u>
Total Cash and Cash Equivalents	<u>\$ 17,571,113</u>	<u>\$ 19,156,122</u>	<u>\$ 36,727,235</u>

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 7—Capital leases receivable

The Real Estate Foundation has entered into multiple 20 to 30-year capital lease agreements (1-year leases with annual renewals) with the Board of Regents to occupy the facilities. Lease payments are due monthly. At the end of the lease term, ownership of the leased facilities will be transferred to the Board of Regents.

As of June 30, 2017, net capital leases receivable were \$265,106,190. These amounts include future minimum lease payments to be received of \$433,287,875 as of June 30, 2017, of which \$168,181,685 is unearned interest.

As of June 30, 2017, lease payments are receivable as follows:

2018	\$ 22,537,729
2019	22,390,921
2020	22,372,264
2021	22,352,200
2022	22,333,264
2023 - 2027	111,351,627
2028 - 2032	110,657,383
2033 - 2037	73,058,879
2038 - 2042	23,467,522
2043 - 2044	<u>2,766,086</u>
Total Payments to be Received	433,287,875
Less Amounts Representing Interest	<u>(168,181,685)</u>
Total Leases Receivable	265,106,190
Less Current Portion	<u>(7,990,341)</u>
Noncurrent Leases Receivable	<u><u>\$ 257,115,849</u></u>

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 8—Capital assets

Capital assets consisted of the following:

	<u>Balance at June 30, 2016</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at June 30, 2017</u>
Capital assets not being depreciated				
Land	\$ 15,834,224	\$ -	\$ -	\$ 15,834,224
Construction in-progress	12,709	9,175	-	21,884
Easement	1,835,296	-	-	1,835,296
Total capital assets not being depreciated	<u>17,682,229</u>	<u>9,175</u>	<u>-</u>	<u>17,691,404</u>
Capital assets being depreciated				
Furniture and equipment	197,392	-	-	197,392
Less accumulated depreciation	(196,638)	(754)	-	(197,392)
Library repository building	1,142,307	-	-	1,142,307
Less accumulated depreciation	(1,142,307)	-	-	(1,142,307)
Other buildings and improvements	3,179,498	-	-	3,179,498
Less accumulated depreciation	<u>(1,233,042)</u>	<u>(114,323)</u>	<u>-</u>	<u>(1,347,365)</u>
Total capital assets being depreciated, net	<u>1,947,210</u>	<u>(115,077)</u>	<u>-</u>	<u>1,832,133</u>
Capital assets - net	<u>\$ 19,629,439</u>	<u>\$ (105,902)</u>	<u>\$ -</u>	<u>\$ 19,523,537</u>

Note 9—Long-term debt

The Real Estate Foundation has entered into multiple loan agreements to borrow bond proceeds from the Development Authority of the Unified Government of Athens-Clarke County, Georgia (the Development Authority) or the Housing Authority of the City of Athens, Georgia (the Housing Authority). The Real Estate Foundation used the proceeds of these loans to fund construction, acquisition, renovation and the equipping of various facilities located on the University's campus. These properties are secured by certain real properties and by the Real Estate Foundation's interest in certain rents and leases derived from these facilities.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 9—Long-term debt (continued)

At June 30, 2017, borrowings under the Real Estate Foundation's loan agreements bear interest payable semi-annually in December and June at rates ranging from 1.25% to 6.30% with maturity dates through fiscal year 2044.

Revenue Bonds	Original Issue Amount	Interest Rates	Maturing Through Year	Outstanding Balance 2017
Bolton Entity, Series 2013	\$ 24,400,000	3.00% - 5.00%	2044	\$ 19,345,000
CCRC Entity, Series 2011	32,580,000	2.00% - 5.25%	2032	26,840,000
Central Precinct Entity, Series 2016	54,025,000	2.00% - 5.00%	2038	52,250,000
Coverdell Entity, Series 2013	21,100,000	2.00% - 5.00%	2034	18,780,000
EC Housing Entity, Series 2010	34,090,000	2.50% - 5.00%	2023	21,540,000
EC Housing Entity, Series 2011	48,250,000	2.00% - 5.00%	2033	46,550,000
EC Housing Phase II Entity, Series 2017	44,630,000	3.00% - 5.00%	2040	43,380,000
Fraternity Row Entity, Series 2017	12,665,000	1.05% - 4.45%	2039	12,215,000
PAC Entity, Series 2009	17,655,000	3.00% - 5.00%	2039	14,775,000
Rutherford Entity, Series 2012	21,910,000	2.00% - 5.00%	2033	13,240,000

Defeasance and refunding of revenue bonds

Real Estate Foundation – EC Housing Phase II Entity

On February 9, 2017, the Housing Authority issued \$44,630,000 in Revenue Refunding Bonds (UGAREF East Campus Housing Phase II, LLC Project), Series 2017 (the "2017 EC Housing Phase II Bonds") with interest rates ranging from 3.0% to 5.0% and entered into an agreement (the "2017 EC Housing Phase II Loan Agreement") with the EC Housing Phase II Entity to advance refund \$44,425,000 of outstanding 2009 EC Housing Phase II Bonds with interest rates ranging from 4.0% to 5.25%.

The net proceeds of \$48,384,818 were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent and will fund all future debt service payments on the refunded 2009 EC Housing Phase II Bonds. As a result, \$44,425,000 of outstanding 2009 EC Housing Phase II Bonds are considered to be defeased and the liability for those bonds has been removed from the statement of net position for the year ended June 30, 2017.

The advance refunding resulted in a loss, which consisted of the difference between the reacquisition price and the net carrying amount of the old debt, of \$3,298,186. This difference, reported in the accompanying statements of net position as a deferred outflow of resources, is being charged to operations as interest expense through June 15, 2040, using the straight-line method. The EC Housing Phase II Entity completed the advance refunding to reduce its total debt service payments through 2040 by \$4,540,769 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$3,195,287 at an effective interest rate of 3.2701%.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 9—Long-term debt (continued)

Defeasance and refunding of revenue bonds (continued)

Real Estate Foundation – Fraternity Row Entity

On March 15, 2017, the Housing Authority issued \$12,665,000 in Revenue Refunding Bonds (UGAREF Fraternity Row, LLC Project), Taxable Series 2017 (the "2017 Fraternity Row Bonds") with interest rates ranging from 1.05% to 4.45% and entered into an agreement (the "2017 Fraternity Row Loan Agreement") with the Fraternity Row Entity to advance refund \$11,070,000 of outstanding 2009 Fraternity Row Bonds with interest rates ranging from 4.4% to 6.3%.

The net proceeds of \$12,351,882 were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent and will fund all future debt service payments on the refunded 2009 Fraternity Row Bonds. As a result, \$11,070,000 of outstanding 2009 Fraternity Row Bonds are considered to be defeased and the liability for those bonds has been removed from the statement of net position for the year ended June 30, 2017.

The advance refunding resulted in a loss, which consisted of the difference between the reacquisition price and the net carrying amount of the old debt, of \$1,171,044. This difference, reported in the accompanying statements of net position as a deferred outflow of resources, is being charged to operations as interest expense through June 15, 2039, using the straight-line method. The Fraternity Row Entity completed the advance refunding to reduce its total debt service payments through 2039 by \$1,343,929 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$891,220 at an effective interest rate of 4.099%.

Real Estate Foundation – Bonds Payable

The bonds payable agreements require the Real Estate Foundation to meet certain covenants. At June 30, 2017, the Real Estate Foundation was not aware of any violations of the covenants.

Following is a summary as of June 30, 2017, of principal and interest payments for the face value of the bonds payable during each of the next five years ending June 30 and every five years thereafter:

	<u>Principal</u>	<u>Interest</u>
2018	\$ 9,605,000	\$ 11,170,224
2019	9,840,000	10,791,256
2020	10,215,000	10,404,919
2021	10,630,000	9,981,561
2022	10,980,000	9,574,274
2023 - 2027	62,195,000	40,233,606
2028 - 2032	76,380,000	25,374,588
2033 - 2037	57,210,000	10,147,379
2038 - 2042	19,525,000	2,228,668
2043 - 2044	2,335,000	158,850
	<u>\$ 268,915,000</u>	<u>\$ 130,065,325</u>

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 9—Long-term debt (continued)

Real Estate Foundation – Bonds Payable (continued)

Changes in long-term debt for the fiscal year ended June 30, 2017, are shown below:

	<u>Balance at June 30, 2016</u>	<u>Additions</u>	<u>Disposals and Reductions</u>	<u>Balance at June 30, 2017</u>	<u>Current Portion</u>
Bonds Payable	\$ 276,685,000	\$ 57,295,000	\$ (65,065,000)	\$ 268,915,000	\$ 9,605,000
Net Premium (Discount)	11,449,942	4,299,542	(1,426,941)	14,322,543	-
Total Long-Term Debt	<u>\$ 288,134,942</u>	<u>\$ 61,594,542</u>	<u>\$ (66,491,941)</u>	<u>\$ 283,237,543</u>	<u>\$ 9,605,000</u>

A summary of the components of interest cost for the year ended June 30, 2017, is as follows:

	<u>Interest Expensed 2017</u>
Interest Cost	
Interest Expense	\$ 11,876,826
Amortization of Premiums, Discounts, and Deferred Loss	(307,087)
Cost of Issuance	853,516
Fees	239,188
Interest Income	<u>(273,839)</u>
Total Interest Cost	<u>\$ 12,388,604</u>

Note 10—Line of credit

\$25,000,000 Revolving Credit Agreement – In November 2015, the Real Estate Foundation entered into a \$25 million revolving credit agreement with a bank, for a three-year term to expire on November 30, 2018. Credit available under the revolving credit agreement is reduced by outstanding borrowings. At June 30, 2017, amounts outstanding and issued under this agreement include borrowings of \$8,516,222 resulting in \$16,483,778 available as borrowing capacity under this line. Borrowings under the revolving credit agreement bear interest at the bank’s 30-day London Interbank Offered Rate plus 60.0 basis points (or 0.60%). At June 30, 2017, the rate applicable to the borrowings was 1.82%. Amounts available as borrowing capacity are subject to an unused commitment fee of 0.10%.

Under this revolving credit agreement, certain borrowings are subject to a guarantee requirement with the Research Foundation as guarantor. As of June 30, 2017, there are no borrowings subject to this guarantee requirement.

The revolving credit agreement requires the Real Estate Foundation to meet certain covenants. At June 30, 2017, the Real Estate Foundation was not aware of any violations of the covenants.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 11—Operating leases

The Real Estate Foundation is a lessee under an amended multiyear operating lease for University education facilities at One Live Oak Center, Atlanta, Georgia, that expires on August 31, 2024, with escalating rents. The Real Estate Foundation recognizes rent for this agreement on a straight-line basis. A straight-line lease liability of \$781,030, as of June 30, 2017, is included in liabilities. For the year ended June 30, 2017, rent expense was \$834,924, and includes additional rents to cover operating expenses of the education facility.

The Real Estate Foundation is a lessee under a multiyear operating lease for University education facilities at Gwinnett Intellicenter, Duluth, Georgia, that expires on April 30, 2027, with escalating rents. The Real Estate Foundation recognizes rent for this agreement on a straight-line basis. A straight-line lease liability of \$1,013,963, as of June 30, 2017, is included in liabilities. For the year ended June 30, 2017, rent expense was \$1,431,057, and includes additional rents to cover operating expenses of the education facility.

The following is a schedule by years of future minimum rental payments under operating leases as of June 30, 2017, that have initial or remaining noncancelable lease terms in excess of one year:

Years Ending June 30,

2018	\$ 2,304,331
2019	2,369,804
2020	2,437,201
2021	2,506,465
2022	2,577,876
2023 - 2027	<u>10,624,231</u>
	<u>\$ 22,819,908</u>

Note 12—Related party transactions

On July 23, 1991, the Research Foundation purchased a library storage facility and approximately four acres of land for approximately \$1.2 million and subsequently leased the 38,000 square-foot facility to the University. The lease is renewable annually, at the University's option, through June 30, 2020. The monthly rental for this lease agreement is \$6,275. The lease rental for the year ended June 30, 2017, was \$75,300. The library storage facility was being depreciated over 25 years and became fully depreciated during fiscal year 2016.

The Research Foundation receives reimbursement from research sponsors for facilities and administrative ("F&A") cost incurred. Of the total received, 78% is remitted to the University for reimbursement of F&A cost incurred by the University. Additionally, the Research Foundation remitted \$3,974,717 for the year ended June 30, 2017, to various departments of the University for F&A cost they incurred in the support of research.

In addition to the \$4,463,889 in support to the University shown on the statement of revenues, expenses, and changes in net position, the Research Foundation distributes a portion of license and royalties revenue on a quarterly basis. Distributions are made to parties according to the Intellectual Property Administration Agreement and other contractual provisions. During fiscal year 2017, \$6,649,123 of license and royalties revenue was distributed of which \$2,926,650 was paid to the University to support inventor's research and departmental research programs, and the Plant Cultivar and Animal Health Fund programs.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 12—Related party transactions (continued)

The Real Estate Foundation leases real property to the Board of Regents under both operating and capital leases, including space subleased under operating leases to the Board of Regents. The Real Estate Foundation also has one-year licensing agreements with the Board of Regents which provides for the operation of parking lots by the Board of Regents on the Real Estate Foundation's land located on Oconee Street in Athens, Georgia, in exchange for a fee adjusted at the end of the term to reflect actual costs incurred. For the year ended June 30, 2017, the amounts reported as Rental Income and Capital Lease Interest Income in the statement of revenues, expenses, and changes in net position consists of revenue earned through lease agreements. The lease agreements with the Board of Regents are the primary source of revenue for the Real Estate Foundation, which constitutes a concentration of credit risk.

Additionally, the lease agreements provide that certain amounts paid by the Real Estate Foundation be reimbursed by the Board of Regents. Amounts reimbursed are primarily insurance and property taxes. For the year ended June 30, 2017, the expenses which were paid by the Real Estate Foundation and reimbursed by the University are reported as Receipts for Payments Reimbursable by the University and Affiliates and Payments Reimbursable by the University and Affiliates in the statement of cash flows.

The Real Estate Foundation leases the use of land from the Board of Regents where it has constructed property on Board of Regents' land. These ground leases are for a period of up to 3 years during construction and continue for 30 years after construction is complete for a base rental of \$10 per year. Under the ground leases, the ownership of any building or structure constructed on the land passes to the Board of Regents at the end of the ground lease.

The Real Estate Foundation leases air rights from the Board of Regents where it has constructed property above the lower floors on the Board of Regents' land. The air rights lease is for a period of up to 3 years during construction and continues for 30 years after construction is complete for a base rental of \$10 per year. Under the air rights lease, the ownership of any building or structure constructed above the lower floors of the building passes to the Board of Regents at the end of the air rights lease.

The Real Estate Foundation has entered into an administrative services agreement with the University whereby the University provides project management, accounting, and other administrative services, as well as provisions for office space, maintenance, and utilities to be provided by the University to the Real Estate Foundation. During the year ended June 30, 2017, the Real Estate Foundation paid \$391,147 to the University under the terms of that agreement. The administrative services agreement is renewable on an annual basis.

On March 1, 2013, the Real Estate Foundation and UGAF entered into a Memorandum of Agreement (the "Terry Entity MOA") for the Real Estate Foundation to oversee the design and construction of the Terry Entity project, a new approximately 75,000 square foot building, on the campus of the University for the Terry College of Business. The Terry Entity MOA specifies that UGAF will reimburse the Real Estate Foundation for all project costs incurred by the Real Estate Foundation in connection with the completion of the Terry Entity project. During the year ended June 30, 2017, the Real Estate Foundation was reimbursed \$106,925 for project costs. Expenses paid by the Real Estate Foundation and reimbursed by UGAF are reported as Receipts for Payments Reimbursable by the University and Affiliates and Payments Reimbursable by the University and Affiliates in the statement of cash flows. The building was completed and placed in service in July 2015.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 13—Significant funding sources

For the fiscal year ended June 30, 2017, approximately \$114,000,000 (78%) of the Research Foundation's total federal expenditures and support were awarded by three (3) agencies of the United States government. Changes in governmental spending could have a significant impact on the operations of the Research Foundation.

Note 14—Commitments and contingencies

In the normal course of business, there may be legal actions pending against the Research Foundation. At this time there are no such actions pending, therefore, no legal actions are expected to have a material effect on the Research Foundation's financial position, results of operations, or liquidity.

The Research Foundation has the following contractual commitments, in whole or in part, with parties other than the University:

The Georgia legislature passed legislation establishing the GRA Venture Fund (T. E.), LLC (the "GRA Fund"). The fund provides seed and early stage venture financing for businesses formed around intellectual property resulting from GRA universities. The Research Foundation committed a total of \$1,000,000 at \$200,000 per year for five years beginning in fiscal year 2009. During fiscal year 2017, \$26,812 was requested and transferred to the GRA Fund. As of June 30, 2017, the Research Foundation's remaining commitment is \$163,137. In July 2015, the Research Foundation made an additional commitment of \$1,000,000 at \$200,000 per year for five years to the GRA Fund. During fiscal year 2017, \$85,794 was requested and transferred to the GRA Fund. As of June 30, 2017, the Research Foundation's remaining commitment is \$714,432.

As the sole member of the Real Estate Foundation, the Research Foundation is guarantor on up to \$25 million on a revolving credit agreement maintained by the Real Estate Foundation. As of June 30, 2017, there are no borrowings subject to this guarantee requirement.

The Research Foundation has committed to fund, in whole or in part, the following projects at the University:

In prior fiscal years, the Research Foundation made multi-year commitments to support programs and initiatives in infectious disease. The fiscal year 2018 commitment for these programs is approximately \$123,000.

The Research Foundation has an ongoing commitment to fund a portion of the Coverdell Center lease repayment. The current commitment is \$585,144 each fiscal year and continues through fiscal year 2035. This commitment will end in fiscal year 2018 upon the transfer of the facility to the University as discussed in Note 15.

Annual commitments totaling \$749,900 exist to support general operating costs of the Georgia Advanced Computing Resource Center, the Coverdell and Riverbend buildings, to provide access dues to research computing resources, and support for the Animal Health Research Center.

The Research Foundation established the Special Research Hiring Initiative in fiscal year 2014 and the President's Extraordinary Research Faculty Hiring Initiative in fiscal year 2015. The fiscal year 2018 commitment for these initiatives is budgeted at \$960,000.

UNIVERSITY OF GEORGIA RESEARCH FOUNDATION, INC.
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 15—Subsequent events

On August 2, 2017, the Research Foundation agreed to provide up to \$6,000,000 to the University to partially fund the early extinguishment of debt related to the Paul D. Coverdell Center for Biomedical and Health Sciences as described below.

On September 6, 2017, the Development Authority entered into an agreement with the Coverdell Entity to early extinguish \$18,780,000 of outstanding 2013 Coverdell Bonds with interest rates ranging from 3.0% to 5.0% pursuant to the transfer of the Coverdell Entity facility to the University. The Coverdell Entity received \$21,167,039 from the University to complete the extinguishment, transfer of the facility to the University, and early terminate the air rights lease and capital lease agreements related to the project.

On September 14, 2017, the Development Authority issued \$15,215,000 in Revenue Refunding Bonds (UGAREF PAC Parking Deck, LLC Project), Series 2017 (the "2017 PAC Bonds") with interest rates ranging from 2.0% to 5.0% and entered into a loan agreement with the PAC Entity to advance refund \$14,775,000 of outstanding 2009 Educational Facilities Revenue Bonds with interest rates ranging from 3.625% to 5.00%. Payment of principal and interest under the 2017 PAC Bonds is secured by certain real property constituting two parking decks, and by the PAC Entity's interest in certain rents and leases derived from these facilities.

**Report of Independent Auditor on Internal Control over Financial Reporting and
on Compliance and Other Matters Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards***

The Audit Committee of the Board of Directors
University of Georgia Research Foundation, Inc.
Athens, Georgia

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the University of Georgia Research Foundation, Inc. (the "Research Foundation"), an affiliate of the University of Georgia, which is a unit of the University System of Georgia, which is an organizational unit of the state of Georgia, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the Research Foundation's basic financial statements, and have issued our report thereon dated September 14, 2017.

Internal Control over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Research Foundation's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Purpose of this Report

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

A handwritten signature in black ink that reads "Cheryl Bekant LLP". The signature is written in a cursive, flowing style.

Augusta, Georgia
September 14, 2017