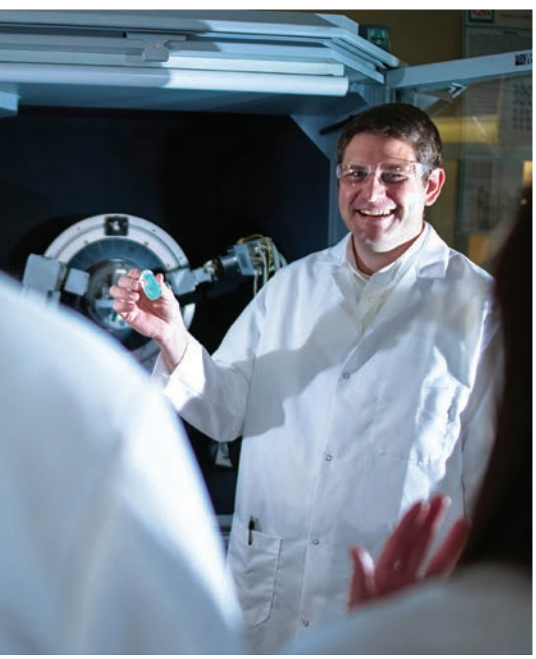


UNIVERSITY OF SOUTH ALABAMA

2018 FINANCIAL REPORT


CISCO

UNIVERSITY OF SOUTH ALABAMA BOARD OF TRUSTEES

PICTURED FROM LEFT:

The mission of the University of South Alabama is to make a difference in the lives of those we serve through promoting discovery, health and learning. At South, we strive to achieve this mission through the establishment of, and adherence to, five institutional strategic priorities:

- Student access and success
- Enhancement of research and graduate education
- Global engagement
- Excellence in healthcare
- University-community engagement

Everything we do at South, including management of financial resources, is with these priorities in mind.

As the University continues to grow, it is through a sound financial position that our priorities can be accomplished. Despite the economic challenges of the past several years, the financial position of the University of South Alabama, as demonstrated in this financial report, remains strong. This financial strength allows us to continue to serve the citizens of the state of Alabama and beyond by providing top quality academic, research, healthcare and public service programs.

With a Fall 2017 enrollment of 14,834, the academic profile of our students continues to improve and has never been stronger than it is right now. This continued improvement is a testament to the strength of our programs, the quality and dedication of our faculty and staff and the loyalty and spirit of our alumni. Similarly, USA Health continues its growth and dedication to the wellbeing of our patients.

Along with the growth in our academic programs, campus life is constantly being enhanced and improved as evidenced by an ever-increasing demand for on-campus student housing. More than 200 diverse student clubs and organizations engage students in campus life. Student leadership development is a continued area of focus in all areas of student life at the University, and the Office of Multicultural Student Affairs actively engages students in conversation and activities that encourage dialog among all students. Our student-athletes continue to excel both on the field and in the classroom.

USA students also give back to the community. Hundreds participate in community-service activities throughout the year, such as the annual MLK Day of Service, which offers numerous opportunities to help.

This is an exciting time for the University of South Alabama. Our future is bright and our vision remains true. As we continue to strive to make South more vibrant, more involved and more global, I affirm to you that my focus and the focus of the entire University will be solidly fixed on these objectives and on our students.

Tony G. Waldrop, Ph.D.
President

MESSAGE FROM THE CHAIR PRO TEMPORE OF THE BOARD OF TRUSTEES

Your Board of Trustees is committed to enhancing and sustaining the success of the University of South Alabama and to ensuring that our core values and priorities are met and maintained. We are committed to the successful achievement of the mission of the University as well as to the success of our students, faculty and staff.

The Board of Trustees takes its responsibility for the stewardship of our financial resources and academic programs very seriously. We constantly strive to improve all aspects of the University and seek to ensure that USA is an intellectual, economic and service leader in the state of Alabama and the region for years to come.

I am privileged to work alongside my colleagues on the Board as well as with President Waldrop and our University's dedicated and outstanding leadership team as we continue to move USA forward.

Together, we are the University of South Alabama. We are South!

Kenneth O. Simon
Chair Pro Tempore, Board of Trustees
University of South Alabama


Race

I am pleased to present this annual financial report for the University of South Alabama at and for the year ended September 30, 2018. I am confident that the accompanying financial statements fairly present the financial position and results of operations of the University including its Health System. It is the responsibility of University management to ensure that these financial statements, including management's discussion and analysis and the accompanying notes to the financial statements, are complete and fairly presented in accordance with U.S. generally accepted accounting principles.

The management of the University of South Alabama is responsible for the integrity and objectivity of the financial information presented in these statements. We believe that the University's system of internal accounting controls provides reasonable assurance that assets are protected and that all transactions and events are properly recorded. The Board of Trustees of the University, through the Audit Committee, monitors the financial and accounting operations of the University.

G. Scott Weldon
Vice President for Finance and Administration
University of South Alabama

KPMG

UNIVERSITY OF SOUTH ALABAMA

(A Component Unit of the State of Alabama)

Basic Financial Statements

September 30, 2018

(With Independent Auditors' Report Thereon)

UNIVERSITY OF SOUTH ALABAMA

(A Component Unit of the State of Alabama)

Basic Financial Statements

September 30, 2018

Table of Contents

Introduction

The following discussion presents an overview of the financial position and financial activities of the University of South Alabama (the University), including the University of South Alabama Health System (USA Health), a division of the University, at September 30, 2018 and 2017, and for the years then ended. This discussion has been prepared by University management and should be read in conjunction with the financial statements and notes thereto, which follow.

The basic financial statements of the University consist of the University and its component units. The financial position and results of operations of the component units either are blended with the University's financial position and results of operations or are discretely presented. The treatment of each component unit is governed by pronouncements issued by the Governmental Accounting Standards Board (GASB). As more fully described in note 1 to the basic financial statements, the University of South Alabama Professional Liability Trust Fund, the University of South Alabama General Liability Trust Fund and the USA HealthCare Management, LLC are reported as blended component units. The University of South Alabama Foundation, the USA Research and Technology Corporation and the University of South Alabama Health Care Authority (HCA) are discretely presented.

HCA was formed in May 2017 by the University as an Alabama public corporation pursuant to the University Authority Act of 2016. Operations commenced on August 1, 2017. HCA enhances the University's provision of patient care by providing it with a corporate structure which allows for greater flexibility and options to achieve goals consistent with the public health mission of the University. HCA provides group medical practices for physicians who strive to make a difference in the lives of those they serve through promoting excellent health care.

Due to the implementation of GASB No. 75 *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* in 2018, the University only presented financial statements for 2018 and management's discussion and analysis for 2018 and 2017. Management's discussion and analysis for 2017 does not reflect the impact of the adoption of GASB No. 75 and, therefore, is not comparative to 2018.

Financial Highlights

At September 30, 2018 and 2017, the University had total assets and deferred outflows of $1,298,365,000 and $1,282,492,000, respectively; total liabilities and deferred inflows of $1,262,967,000 and $1,016,673,000, respectively; and net position of $35,398,000 and $265,819,000, respectively. The significant reduction in net position at September 30, 2018 is due to the implementation of GASB No. 75, which required the recognition of the University's proportionate share of the net other postemployment benefits liability (OPEB) and related expenses in the basic financial statements (see note 1 for further discussion).

An overview of each statement is presented herein along with financial analysis of the transactions impacting each statement. Where appropriate, comparative financial information is presented to assist in the understanding of this analysis.

(CONTINUED)

Analysis of Financial Position and Results of Operations

Statement of Net Position

The statement of net position presents the assets, deferred outflows, liabilities, deferred inflows and net position of the University at September 30, 2018. Net position is displayed in three parts: net investment in capital assets, restricted and unrestricted. Restricted net position may be either expendable or nonexpendable and is the net position that is restricted by law or external donors. Unrestricted net position is generally designated by management for specific purposes, and is available for use by the University to meet current expenses for any purpose. The statement of net position, along with all of the University's basic financial statements, are prepared under the economic resources measurement focus and the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred by the University, regardless of when cash is exchanged.

Assets included in the statement of net position are classified as current or noncurrent. Current assets consist primarily of cash and cash equivalents, investments, and net patient receivables. Of these amounts, cash and cash equivalents, net patient receivables and investments comprise approximately 44%, 24% and 14%, respectively, of current assets at September 30, 2018. Noncurrent assets consist primarily of restricted cash and cash equivalents, restricted investments and capital assets.

(CONTINUED)

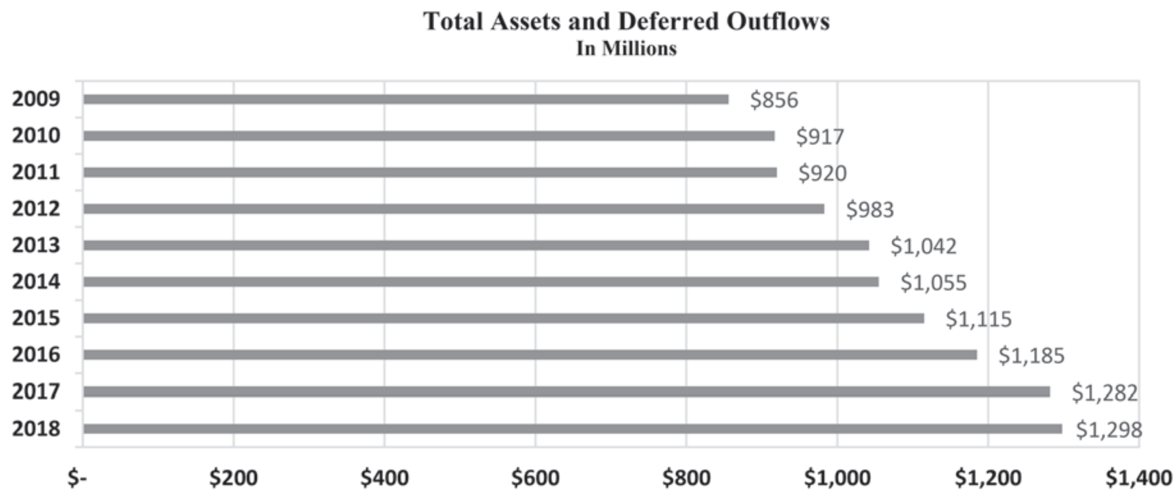
The condensed schedules of net position at September 30, 2018 and 2017 follow (in thousands):

Condensed Schedules of Net Position

		2018	2017
Assets:			
Current	$	182,139	261,407
Capital assets, net		719,816	693,968
Other noncurrent		308,941	268,116
Total assets		1,210,896	1,223,491
Deferred outflows		87,469	59,001
Total assets and deferred outflows		1,298,365	1,282,492
Liabilities:			
Current		157,059	157,803
Noncurrent		1,006,862	818,105
Total liabilities		1,163,921	975,908
Deferred inflows		99,046	40,765
Total liabilities and deferred inflows		1,262,967	1,016,673
Net position:			
Net investment in capital assets		337,303	305,898
Restricted, nonexpendable		58,078	54,961
Restricted, expendable		68,311	62,676
Unrestricted		(428,294)	(157,716)
Total net position	$	35,398	265,819

(CONTINUED)

Total assets and deferred outflows of the University as of September 30 is as follows:



Net position represents the residual interest in the University's assets after liabilities are deducted. Net position is classified into one of four categories:

Net investment in capital assets represents the University's capital assets less accumulated depreciation and outstanding principal balances of the debt attributable to the acquisition, construction, or improvement of those assets.

Restricted nonexpendable net position consists primarily of the University's permanent endowment funds. In accordance with the policies of the University, the earnings from these funds may be expended, but the corpus may not be expended and must remain intact with the University in perpetuity.

Restricted expendable net position is subject to externally imposed restrictions governing their use. The funds are restricted primarily for debt service, capital projects, student loans, and scholarship purposes.

Unrestricted net position represents amounts not subject to externally imposed stipulations. Even though these funds are not legally restricted, the majority of the University's unrestricted net position has been internally designated for various projects, all supporting the mission of the University. Unrestricted net position includes funds for various academic and research programs, auxiliary operations (including student housing and dining services), student programs, capital projects and general operations. Also included in unrestricted net position at September 30, 2018 is the impact of the net pension liability recorded pursuant to the requirements of GASB Statement No. 68 and the impact of the net OPEB liability recorded pursuant to the requirements of GASB Statement No. 75.

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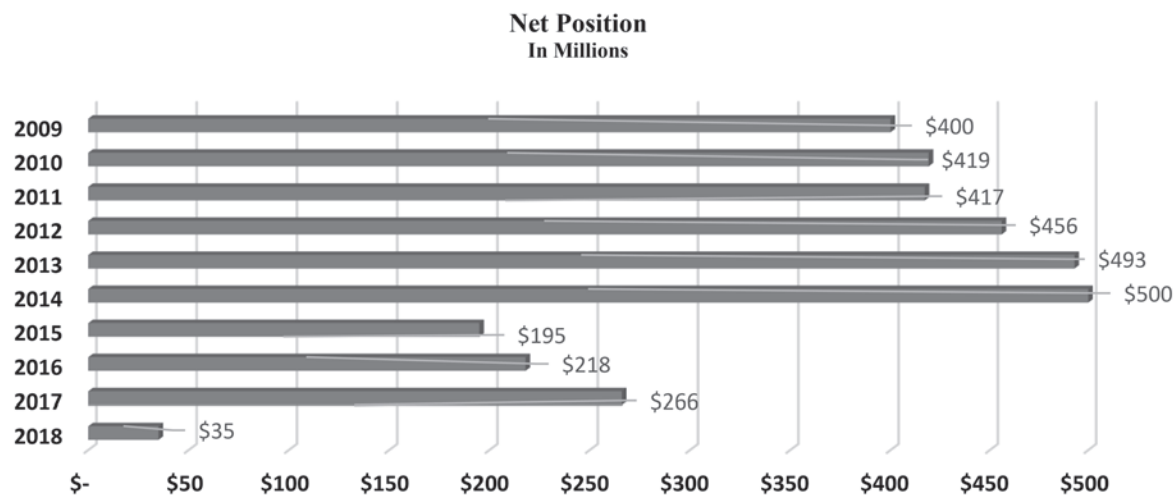
Net position of the University as of September 30 is as follows:



All categories of restricted net position collectively increased by approximately 7% between September 30, 2018 and 2017, primarily due to the addition of restricted gifts to the University. Unrestricted net position decreased from $(157,716,000) to $(428,294,000) between September 30, 2018 and 2017 primarily due to the implementation of GASB Statement No. 75. A summary of unrestricted net position at September 30, 2018 is summarized as follows (in thousands):

Unrestricted net position related to net pension liability	$	(296,654)
Unrestricted net position related to net OPEB liability		(256,178)
Unrestricted net position related to other activity		124,538
Unrestricted net position	$	(428,294)

Statement of Revenues, Expenses, and Changes in Net Position

Changes in total University net position are based on the activity presented in the statement of revenues, expenses, and changes in net position. The purpose of this statement is to present the changes in net position resulting from operating and nonoperating revenues earned by the University, and operating and nonoperating expenses incurred by the University, as well as any other revenues, expenses, gains, and losses earned or incurred by the University.

Generally, operating revenues have the characteristics of exchange transactions and are received or accrued for providing goods and services to the various customers and constituencies of the University. These include patient service revenues (net of provision for bad debts), tuition and fees (net of scholarship allowances), most noncapital

(CONTINUED)

athletic activities). Operating expenses are those expenses paid or incurred to acquire or produce the goods and services provided in return for the operating revenues, and to carry out the mission of the University.

Nonoperating revenues have the characteristics of nonexchange transactions because generally no goods or services are provided. Such transactions include investment income, state appropriations, gifts and other contributions. State appropriations are required by GASB to be classified as nonoperating revenues. Nonoperating expenses are those expenses required in the operation and administration of the University, but not directly incurred to acquire or produce the goods and services provided in return for operating revenues. Such nonoperating expenses include interest on the University's indebtedness, losses related to the disposition of capital assets, transfers to affiliates to fund operations, and transfers to intergovernmental agencies related to medical expenditures.

The condensed schedules of revenues, expenses, and changes in net position for the years ended September 30, 2018 and 2017 follow (in thousands):

Condensed Schedules of Revenues, Expenses, and Changes in Net Position

		2018	2017
Operating revenues:			
Tuition and fees, net	$	136,222	142,024
Patient service revenues, net		416,034	390,931
Federal, state and private grants and contracts		34,093	36,853
Other		66,730	92,674
		653,079	662,482
Operating expenses:			
Salaries and benefits		486,156	483,113
Supplies and other services		255,145	219,362
Other		78,081	64,942
		819,382	767,417
Operating loss		(166,303)	(104,935)
Nonoperating revenues and expenses:			
State appropriations		108,268	107,332
Net investment income		17,857	18,398
Other, net		22,674	20,613
Net nonoperating revenues		148,799	146,343
Income (loss) before capital contributions and grants and additions to endowment		(17,504)	41,408
Capital contributions and grants and additions to endowment		16,770	6,417
Increase (decrease) in net position	$	(734)	47,825

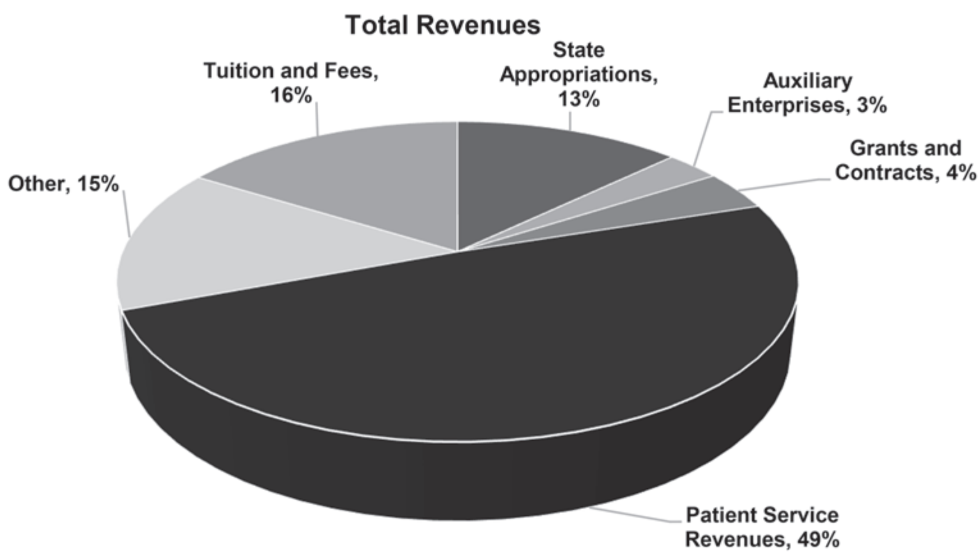
(CONTINUED)

Condensed Schedules of Revenues, Expenses, and Changes in Net Position

		2018	2017
Beginning net position, before cumulative effect of change in accounting principle	$	265,819	217,994
Cumulative effect of change in accounting principle		(229,687)	—
Beginning net position – as adjusted		36,132	217,994
Ending net position	$	35,398	265,819

Approximately 49% and 47% of total revenues of the University were patient service revenues in 2018 and 2017, respectively. Excluding patient service revenues, tuition and fees charged to students represent the largest component of total University revenues, approximately 16% and 17% of total revenues in 2018 and 2017, respectively. Also in 2018 and 2017, state appropriations and grants and contracts (federal, state and private) represented approximately 17% of total revenues.

A summary of University revenues for the year ended September 30, 2018 is presented as follows:



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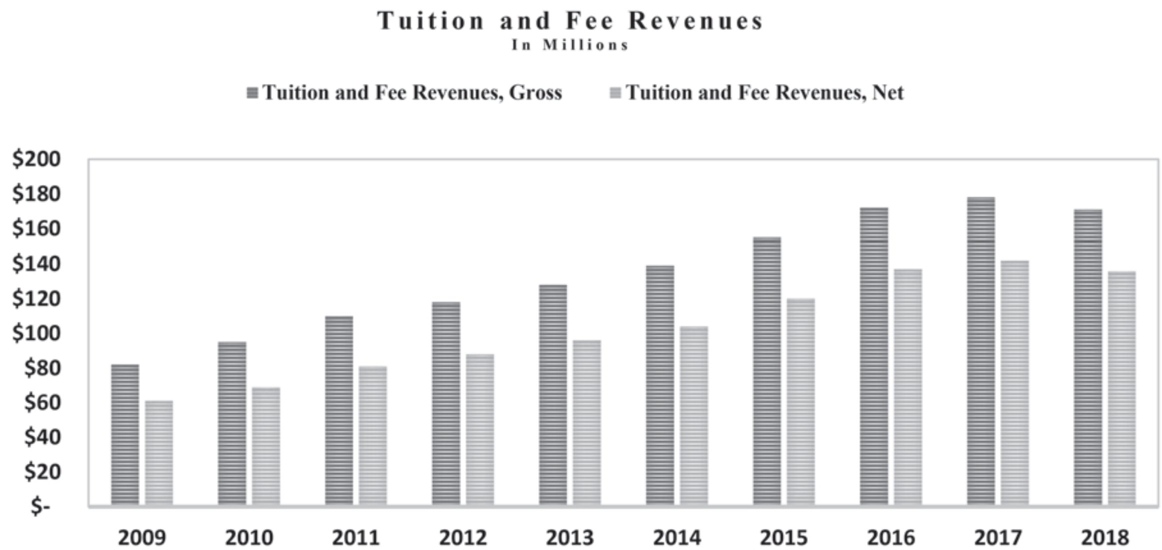
Tuition revenues and enrollment have generally increased in recent years. These increases are primarily due to increases in tuition and fee rates charged to students, the number of enrolled students and credit hours taken by those students. Additionally, tuition and fees as a percent of total operating revenues continue to increase, from 15% of operating revenues in 2009 to 21% in 2018. However, the University experienced a decrease in tuition revenues in the current year of approximately 4%, primarily due to a decline in international student enrollment. Tuition and fees, gross and net of scholarship allowances, for the past ten fiscal years are as follows:



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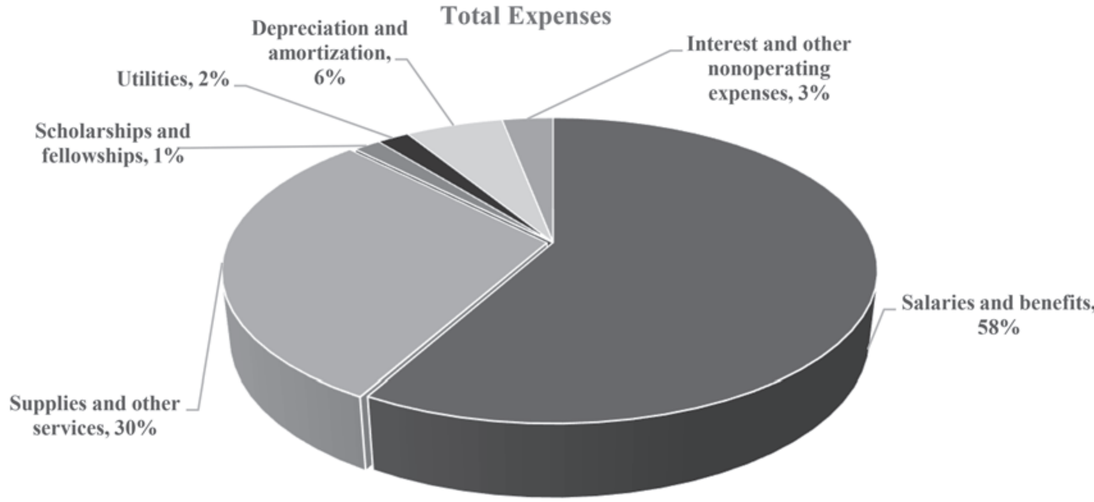
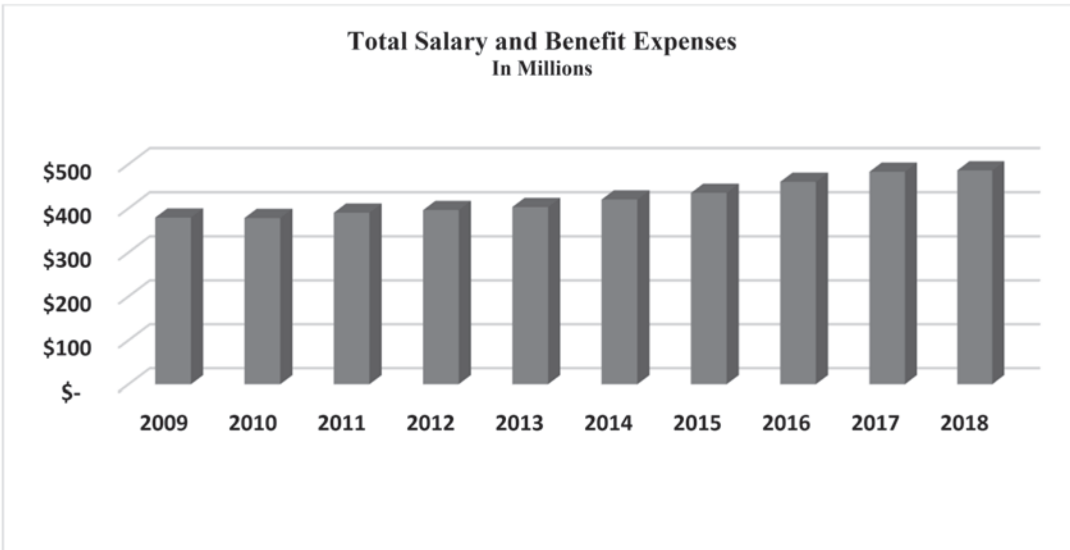
University expenses are presented using their natural expense classifications. A summary of University expenses for the year ended September 30, 2018 is presented as follows:



Functional classifications represent expenses categorized based on the function within the University. Such University functions include instruction, research, public service, academic support, student services, institutional support, operation and maintenance of plant and scholarships. Expenses related to auxiliary enterprise activities, USA Health and depreciation and amortization are presented separately. Functional expense information is presented in note 17 to the basic financial statements.

In 2018 and 2017, approximately 59% and 62%, respectively, of the University's total operating expenses were salaries and benefits.



For the years ended September 30, 2018 and 2017, the University reported operating losses of approximately $166,303,000 and $104,935,000, respectively. Operating losses are offset partially by state appropriations, which, as mentioned earlier, are reported as nonoperating revenues. After adding state appropriations and other nonoperating revenues and expenses, the total change in net position was approximately ($734,000) and $47,825,000, for the years ended September 30, 2018 and 2017, respectively.

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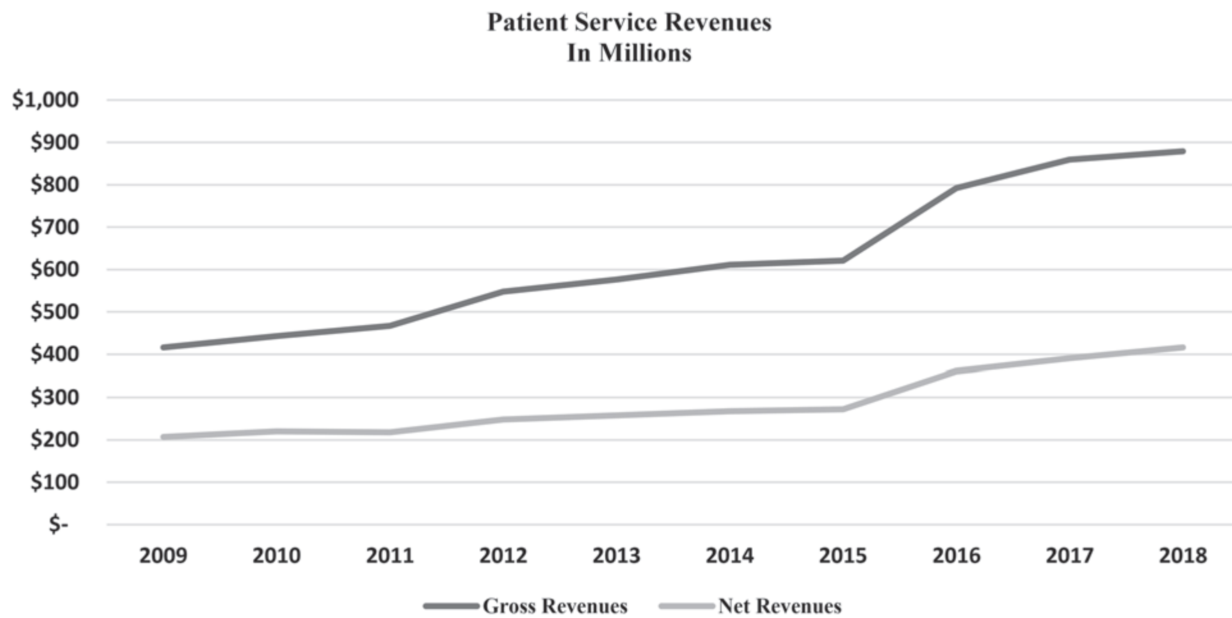
USA Health represents a significant portion of total University revenues. Operating patient service revenues, gross and net, for the last ten fiscal years are presented as follows:



Statement of Cash Flows

The statement of cash flows presents information related to cash flows of the University. The statement presents cash flows by category: operating activities, noncapital financing activities, capital and related financing activities and investing activities. The net cash provided to, or used by, the University is presented by category.

Capital Assets and Debt Administration

Total capital asset additions for the University were approximately $76,087,000 in 2018. Significant construction projects that remain in progress at September 30, 2018 include a new residence hall and major upgrades of infrastructure on the University's main campus. Major projects completed and placed into service in fiscal 2018 and 2017 included an electronic health record system, an addition to the Mitchell Cancer Institute, a professional medical office building near USA Children's and Women's Hospital, a professional medical office building in Fairhope, Alabama and major renovations to the Student Center Food Court. At September 30, 2018, the University had outstanding commitments of approximately $15,174,000 for various capital projects.

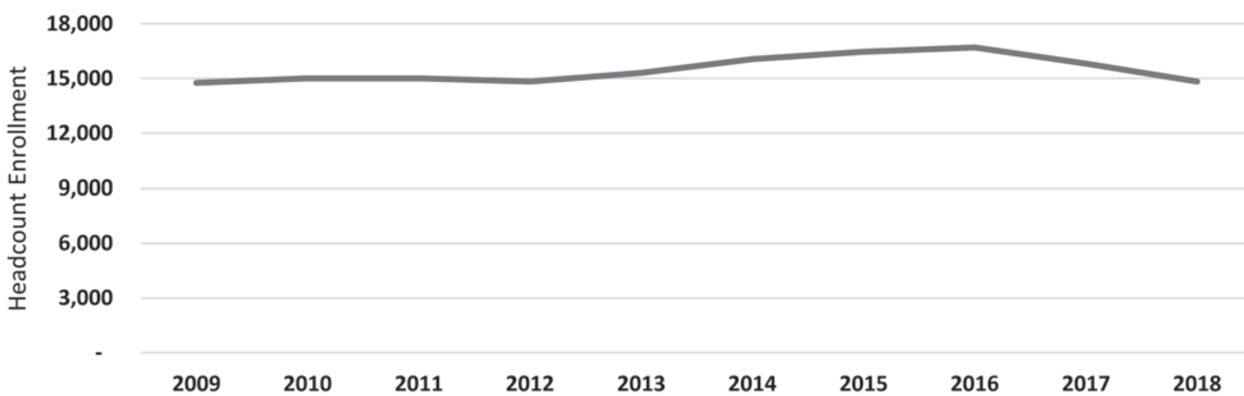
In June 2017, the University issued its University Facilities Revenue Bonds, Series 2017, with a face value of $38,105,000. The proceeds from the Series 2017 Bonds are being expended to construct a new residence hall on the campus of the University and to support ongoing infrastructure improvement projects.

(CONTINUED)

Economic Outlook

Tuition and fee rates have increased over the past ten years and, until the previous two years, student enrollment has generally increased. The University did experience a decline in enrollment of approximately 5% from Fall 2016 to Fall 2017 and an additional decline of 6% between Fall 2017 and Fall 2018, with both declines primarily resulting from a decrease in international student enrollment. The enrollment trend for the University between 2009 and 2018 is as follows:

Enrollment Growth Summary



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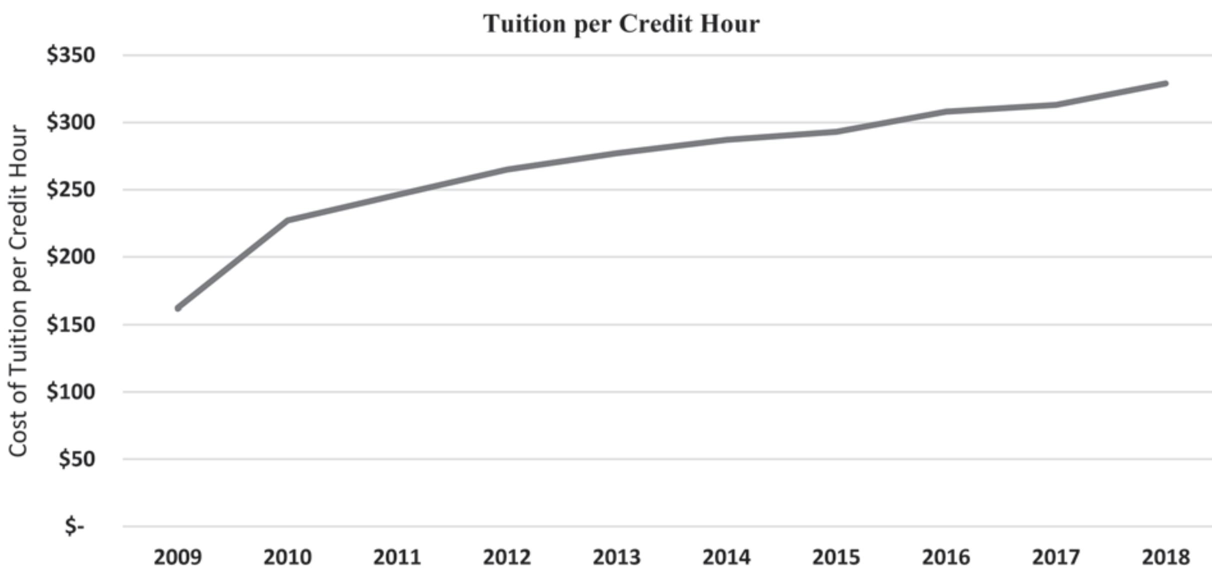
During the same period, in-state tuition per credit hour has increased by approximately 103%. The large increase in 2010 is the result of the University's bundling of tuition and required fees into a single per-hour charge. Similar increases have been experienced in out-of-state tuition and College of Medicine tuition. The trend of in-state tuition per credit hour between 2009 and 2018 is as follows:



A state appropriation in the amount of approximately $108,268,000 and $107,332,000 was authorized and received for the years ended September 30, 2018 and 2017, respectively. A state appropriation in the amount of $111,074,000, representing an increase of approximately 3%, has been authorized for the year ended September 30, 2019. While no announcement has been made, the University is aware that reductions in the 2019 appropriation are possible.

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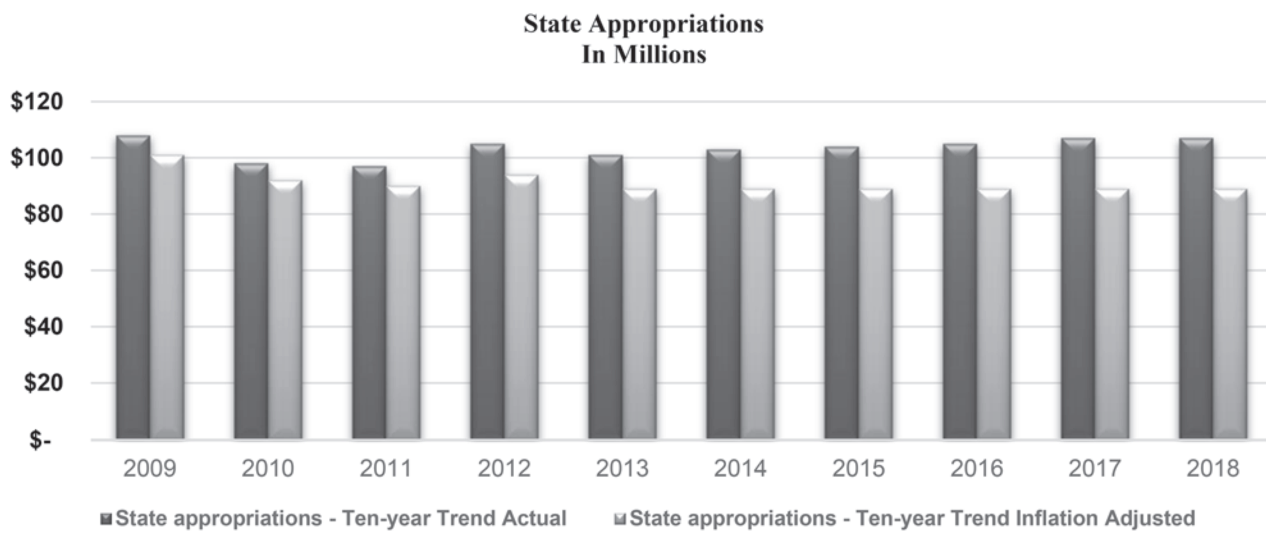
The ten-year trend of state appropriations for the University is as follows:



In addition to state appropriations, the University is subject to declines in general economic and political conditions in the United States and, specifically, the State of Alabama. Weakening of the economy, as well as changes in federal and state funding policies, could potentially have a negative impact on the University's enrollment, extramural funding, endowment performance and health care operations.

Other than the issues presented above, University administration is not aware of any other currently known facts, decisions, or conditions that are expected to have a significant effect on the University's financial position or results of operations during fiscal year 2019 beyond those unknown variables having a global effect on virtually all types of business operations.

Requests for Information

These basic financial statements are designed to provide a general overview of the University of South Alabama and its component units' financial activities and to demonstrate the University's accountability. Questions concerning any of the information provided in this report or requests for additional information should be addressed to G. Scott Weldon; Vice President for Finance and Administration; University of South Alabama Administration Building Room 170; Mobile, Alabama 36688. These basic financial statements can be obtained from our website at http:www.southalabama.edu/departments/financialaffairs/businessoffice/statements.html.

KPMG LLP
Suite 1100
One Jackson Place
188 East Capitol Street
Jackson, MS 39201-2127

Independent Auditors' Report

The Board of Trustees
University of South Alabama:

Report on the Financial Statements

We have audited the accompanying financial statements of the University of South Alabama, a component unit of the State of Alabama, (the University) and its aggregate discretely presented component units, as of and for the year ended September 30, 2018, and the related notes to the financial statements, which collectively comprise the University's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; 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.

Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the consolidated financial statements of the University of South Alabama Foundation, which represent 94% and 99%, respectively, of the total assets and net assets or net position as of June 30, 2018 and 56% of revenues, gains and other support for the year then ended of the aggregate discretely presented component units. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the University of South Alabama Foundation, is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial 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. The financial statements of the University of South Alabama Foundation and the USA Research and Technology Corporation were not audited in accordance with *Government Auditing Standards*.

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

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

KPMG

Opinions

In our opinion, based on our audit and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the University and its aggregate discretely presented component units as of September 30, 2018, and the respective changes in financial position, and where applicable, cash flows thereof for the year then ended in accordance with U.S. generally accepted accounting principles.

Emphasis Matter

As discussed in note 1(bb) to the basic financial statements, in 2018, the University adopted Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

Other Matters

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 1-14, the schedule of the University's proportionate share of the net pension liability, schedule of University's pension contributions, schedule of the University's proportionate share of the net other postemployment benefit liability, and schedule of the University's OPEB contributions on pages 71 - 74 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 November 20, 2018, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the University's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the University's internal control over financial reporting and compliance.

KPMG LLP

Jackson, Mississippi
November 20, 2018

UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Statement of Net Position

September 30, 2018

(In thousands)

Current assets:	
Cash and cash equivalents	$ 79,955
Investments	24,889
Patient receivables (net of allowance for doubtful accounts of $87,653)	43,841
Accounts receivable, other	16,604
Notes receivable, net	7,800
Prepaid expenses, inventories, and other	9,050
Total current assets	182,139
Noncurrent assets:	
Restricted cash and cash equivalents	16,381
Restricted investments	245,068
Investments	43,207
Accounts receivable	3,299
Other noncurrent assets	986
Capital assets, net	719,816
Total noncurrent assets	1,028,757
Total assets	1,210,896
Deferred outflows	87,469
Total assets and deferred outflows	1,298,365
Current liabilities:	
Accounts payable and accrued liabilities	65,012
Unrecognized revenues	58,355
Deposits	2,926
Current portion of other long-term liabilities	6,669
Current portion of long-term debt	24,097
Total current liabilities	157,059
Noncurrent liabilities:	
Long-term debt, less current portion	369,534
Net pension liability	296,654
Net other postemployment benefits liability	256,178
Other long-term liabilities, less current portion	84,496
Total noncurrent liabilities	1,006,862
Total liabilities	1,163,921
Deferred inflows	99,046
Total liabilities and deferred inflows	1,262,967
Net position:	
Net investment in capital assets	337,303
Restricted, nonexpendable:	
Scholarships	28,470
Other	29,608
Restricted, expendable:	
Scholarships	17,127
Other	51,184
Unrestricted	(428,294)
Total net position	$ 35,398

UNIVERSITY OF SOUTH ALABAMA FOUNDATION

(Discretely Presented Component Unit of the University of South Alabama)

Consolidated Statement of Financial Position

June 30, 2018

(In thousands)

Assets

Cash and cash equivalents	$	1,099
Investments:		
Equity securities		137,722
Timber and mineral properties		160,949
Real estate		69,163
Other		5,805
Other assets		450
Total assets	$	375,188

Liabilities and Net Assets

Liabilities:		
Accounts payable	$	184
Other liabilities		794
Total liabilities		978
Net assets:		
Unrestricted		97,487
Temporarily restricted		105,955
Permanently restricted		170,768
Total net assets		374,210
Total liabilities and net assets	$	375,188

See accompanying notes to basic financial statements.

USA RESEARCH AND TECHNOLOGY CORPORATION

(Discretely Presented Component Unit of the University of South Alabama)

Statement of Net Position

September 30, 2018

(In thousands)

Assets:		
Current assets:		
Unrestricted cash and cash equivalents	$	435
Rent receivable		235
Prepaid expenses and other current assets		5
Total current assets		675
Noncurrent assets:		
Intangible assets, net		94
Capital assets, net		21,430
Total noncurrent assets		21,524
Deferred outflows		1,442
Total assets and deferred outflows		23,641
Liabilities:		
Current liabilities:		
Deposits, other current liabilities, and accrued expenses		207
Unrecognized rent revenue		384
Current portion of notes payable		727
Total current liabilities		1,318
Noncurrent liabilities:		
Notes payable, excluding current portion		20,058
Payable to University of South Alabama		1,461
Total noncurrent liabilities		21,519
Total liabilities		22,837
Net position:		
Net investment in capital assets		627
Unrestricted		177
Total net position	$	804

See accompanying notes to basic financial statements.

UNIVERSITY OF SOUTH ALABAMA HEALTH CARE AUTHORITY

(Discretely Presented Component Unit of the University of South Alabama)

Statement of Net Position

September 30, 2018

(In thousands)

Assets:		
Current assets:		
Cash and cash equivalents	$	393
Patient receivables (net of allowance for doubtful accounts of $36)		1,827
Inventories		228
Other current assets		349
Total current assets		2,797
Noncurrent assets:		
Capital assets		731
Total assets		3,528
Liabilities:		
Current liabilities:		
Accounts payable and accrued liabilities		620
Accrued salaries and wages		890
Other current liabilities		798
Total current liabilities		2,308
Total liabilities		2,308
Net position:		
Net investment in capital assets		731
Unrestricted		489
Total net position	$	1,220

See accompanying notes to basic financial statements.

UNIVERSITY OF SOUTH ALABAMA

(A Component Unit of the State of Alabama)

Statement of Revenues, Expenses, and Changes in Net Position

Year ended September 30, 2018

(In thousands)

Operating revenues:		
Tuition and fees (net of scholarship allowances of $35,207)	$	136,222
Patient service revenues (net of provision for bad debts of $99,436)		416,034
Federal grants and contracts		16,411
State grants and contracts		7,790
Private grants and contracts		9,892
Auxiliary enterprises (net of scholarship allowances of $1,089)		25,907
Other operating revenues		40,823
Total operating revenues		653,079
Operating expenses:		
Salaries and benefits		486,156
Supplies and other services		255,145
Scholarships and fellowships		13,394
Utilities		16,076
Depreciation and amortization		48,611
Total operating expenses		819,382
Operating loss		(166,303)
Nonoperating revenues (expenses):		
State appropriations		108,268
Net investment income		17,857
Interest expense		(12,119)
Other nonoperating revenues		48,044
Other nonoperating expenses		(13,251)
Net nonoperating revenues		148,799
Loss before capital contributions and grants and additions to endowment		(17,504)
Capital contributions and grants		8,612
Additions to endowment		8,158
Decrease in net position		(734)
Net position:		
Beginning of year, before cumulative effect of change in accounting principle		265,819
Cumulative effect of change in accounting principle (note 1 (bb))		(229,687)
Beginning balance, as adjusted		36,132
End of year	$	35,398

See accompanying notes to basic financial statements.

UNIVERSITY OF SOUTH ALABAMA FOUNDATION
(Discretely Presented Component Unit of the University of South Alabama)

Consolidated Statement of Activities and Changes in Net Assets

Year ended June 30, 2018

(In thousands)

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Revenues, gains, losses and other support:					
Net realized and unrealized gains on investments	$	4,059	15,887	—	19,946
Rents, royalties and timber sales		3,499	145	12	3,656
Interest and dividends		743	1,377	4	2,124
Gifts		75	3	1,039	1,117
Required match of donor contributions		(6)	2	4	—
Interfund interest		(367)	367	—	—
Other income		31	—	—	31
Net assets released from program restrictions		7,682	(7,682)	—	—
Total revenues, gains, losses and other support		15,716	10,099	1,059	26,874
Expenditures:					
Program services:					
Faculty support		2,242	—	—	2,242
Scholarships		1,139	—	—	1,139
Other academic programs		6,507	—	—	6,507
Total program service expenditures		9,888	—	—	9,888
Management and general		2,118	—	—	2,118
Other investment expense		1,752	—	—	1,752
Depletion expense		4,072	—	—	4,072
Depreciation expense		77	—	—	77
Total expenditures		17,907	—	—	17,907
Change in net assets		(2,191)	10,099	1,059	8,967
Net assets – beginning of year		99,678	95,856	169,709	365,243
Net assets – end of year	$	97,487	105,955	170,768	374,210

See accompanying notes to basic financial statements.

USA RESEARCH AND TECHNOLOGY CORPORATION

(Discretely Presented Component Unit of the University of South Alabama)

Statement of Revenues, Expenses, and Changes in Net Position

Year ended September 30, 2018

(In thousands)

Operating revenues	$	3,510
Operating expenses:		
Building management and operating expenses		1,096
Depreciation and amortization		1,074
Legal and administrative fees		185
Insurance		35
Total operating expenses		2,390
Operating income		1,120
Nonoperating revenues (expenses):		
Donations		107
Interest expense		(1,069)
Debt issuance expense		(82)
Other		(3)
Net nonoperating expenses		(1,047)
Change in net position		73
Net position:		
Beginning of year		731
End of year	$	804

See accompanying notes to basic financial statements.

UNIVERSITY OF SOUTH ALABAMA HEALTH CARE AUTHORITY

(Discretely Presented Component Unit of the University of South Alabama)

Statement of Revenues, Expenses, and Changes in Net Position

Period August 1, 2017 (inception) through September 30, 2018

(In thousands)

Operating revenues:		
Patient service revenues (net of provision for bad debts of $77)	$	16,863
Other operating revenues		651
Total operating revenues		17,514
Operating expenses:		
Salaries and benefits		13,592
Building and equipment expenses		1,537
Medical and surgical supplies		6,791
Other expenses		3,205
Depreciation and amortization		134
Total operating expenses		25,259
Operating loss		(7,745)
Nonoperating revenues:		
Support from University of South Alabama		8,953
Other nonoperating revenues		12
Total nonoperating revenues		8,965
Increase in net position		1,220
Net position at inception		—
Net position at end of year	$	1,220

See accompanying notes to basic financial statements.

UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Statement of Cash Flows

Year ended September 30, 2018

(In thousands)

Cash flows from operating activities:		
Receipts related to tuition and fees	$	139,852
Receipts from and on behalf of patients and third-party payers		429,955
Receipts from grants and contracts		32,812
Receipts related to auxiliary enterprises		25,615
Payments to suppliers and vendors		(262,895)
Payments to employees and related benefits		(464,167)
Payments for scholarships and fellowships		(13,006)
Other operating receipts		32,069
Net cash used in operating activities		(79,765)
Cash flows from noncapital financing activities:		
State appropriations		108,268
Endowment gifts		8,158
Agency funds received		1,645
Agency funds disbursed		(747)
Student loan program receipts		151,313
Student loan program disbursements		(152,448)
Other nonoperating revenues		19,730
Other nonoperating expenses		(13,251)
Net cash provided by noncapital financing activities		122,668
Cash flows from capital and related financing activities:		
Capital contributions and grants		8,612
Purchases of capital assets		(68,345)
Proceeds from sales of capital assets		153
Principal payments on capital debt		(23,088)
Interest payments on capital debt		(11,931)
Net cash used in capital and related financing activities		(94,599)
Cash flows from investing activities:		
Interest and dividends on investments		14,950
Purchases of investments		(29,599)
Proceeds from sales of investments		26,817
Net cash provided by investing activities		12,168
Net decrease in cash and cash equivalents		(39,528)
Cash and cash equivalents (unrestricted and restricted):		
Beginning of year		135,864
End of year	$	96,336

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UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Statement of Cash Flows

Year ended September 30, 2018

(In thousands)

Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$	(166,303)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization expense		48,611
Changes in assets and liabilities, net:		
Student receivables		2,198
Net patient receivables		5,897
Grants and contracts receivables		661
Other receivables		(8,794)
Prepaid expenses, inventories, and other		9,647
Accounts payable and accrued liabilities		29,793
Unrecognized revenues		(1,475)
Net cash used in operating activities	$	(79,765)
Noncash investing, noncapital financing, and capital and related financing transactions:		
Net increase in fair value of investments recognized as a component of investment income	$	10,424
Addition of capital leases		4,940
Additional maturity on capital appreciation on bonds payable and other borrowings recorded as interest expense		427
Gifts of capital and other assets		1,697
Capitalization of construction period interest		1,105
Decrease in accounts payable related to capital assets		(4,666)

See accompanying notes to basic financial statements.

(1) Summary of Significant Accounting Policies

(a) Reporting Entity

On May 3, 1963, the Governor of Alabama signed enabling legislation creating the University of South Alabama (the University). The accompanying basic financial statements present the financial position and activities of the University, which is a component unit of the State of Alabama. The financial statements of the University present the financial position, changes in financial position and, where applicable, cash flows of only that portion of the basic financial statements and the aggregate discretely presented component units of the State of Alabama that is attributable to the transactions of the University.

The financial reporting entity, as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, and amended by GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, GASB Statement No. 61, *The Financial Reporting Entity: Omnibus,* and GASB Statement No. 80*, Blending Requirements for Certain Component Units,* consists of the primary government and all of its component units. Component units are legally separate organizations for which the primary government is financially accountable. In addition, the primary government may determine, through exercise of management's professional judgment, that the inclusion of an organization that does not meet the financial accountability criteria is necessary in order to prevent the reporting entity's financial statements from being misleading. In such instances, that organization is included as a component unit. Accordingly, the basic financial statements include the accounts of the University, as the primary government, and the accounts of the entities discussed below as component units.

GASB Statement No. 61 amends GASB Statements No. 14 and No. 39, and provides criteria for determining whether certain organizations should be reported as component units based on the nature and significance of their relationship with the primary government. Such criteria include the appointment of a voting majority of the board of the organization, the ability to impose the will of the primary government on the organization and the financial benefits/burden between the primary government and the potential component unit. The statement also clarifies reporting and disclosure requirements for those organizations. Based on these criteria as of September 30, 2018, the University reports the University of South Alabama Foundation (USA Foundation), the USA Research and Technology Corporation (the Corporation) and the University of South Alabama Health Care Authority (HCA) as discretely presented component units.

The University is also affiliated with the South Alabama Medical Science Foundation (SAMSF), Gulf Coast TotalCare (Gulf Coast) and the University of South Alabama Foundation for Research and Commercialization (FRAC). These entities are considered component units of the University under the provisions of GASB Statements No. 14, 39 and 61. However, these entities are not discretely presented in the accompanying financial statements as the University does not consider them significant enough to warrant inclusion in the University's reporting entity.

GASB Statement No. 61 and GASB Statement No. 80 require the University, as the primary government, to include in its basic financial statements, as a blended component unit, organizations that, even though they are legally separate entities, meet certain requirements as defined by GASB Statement No. 61 and No. 80. Based on these requirements, the University reports the Professional Liability Trust Fund (PLTF),

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General Liability Trust Fund (GLTF) and USA HealthCare Management, LLC (HCM) as blended component units. All significant transactions among the University and its blended component units have been eliminated in consolidation.

(b) Professional Liability and General Liability Trust Funds

The medical malpractice liability of the University is maintained and managed in its separate Professional Liability Trust Fund in which the University, HCM, SAMSF and HCA are the only participants. In accordance with the bylaws of the PLTF, the president of the University is responsible for appointing members of the PLTF policy committee. Additionally, the general liability of the University, HCM, SAMSF, the Corporation and HCA is maintained and managed in its General Liability Trust Fund for which the University, as defined by GASB Statement No. 14, is responsible. The PLTF and GLTF are separate legal entities, which are governed by the University Board of Trustees through the University president. As such, PLTF and GLTF are reported as blended component units (see note 18 for further discussion of, and disclosure for, these entities).

(c) USA HealthCare Management, LLC

In June 2010, the University's Board of Trustees approved the formation of USA HealthCare Management, LLC. HCM was organized for the purpose of managing and operating on behalf of, and as agent for, substantially all of the health care clinical enterprise of the University. The University is the sole member of HCM. HCM commenced operations in October 2010, and is reported as a blended component unit (see note 18 for further discussion of, and disclosure for, this entity).

(d) University of South Alabama Health Care Authority

In May 2017, the University's Board of Trustees approved the formation of the University of South Alabama Health Care Authority. The HCA is a public corporation created under and pursuant to the provisions of the State of Alabama University Authority Act of 2016. The HCA employs physicians and staff of certain physician practice groups as determined appropriate by the University. Operations commenced on August 1, 2017. Since inception, HCA's operations have been partially funded by the University, with total support amounting to $8,953,000 during the period August 1, 2017 (inception) through September 30, 2018. This support is reported in fiscal 2018 in nonoperating expenses on the University's statement of revenues, expenses, and changes in net position. Due to the significance of the relationship between the University and HCA, the HCA is considered a component unit of the University. The accompanying statement of net position and statement of revenues, expenses, and changes in net position for HCA as of and for the period August 1, 2017 (inception) through September 30, 2018 are discretely presented.

(e) University of South Alabama Foundation

The University of South Alabama Foundation is a not-for-profit corporation that was organized for the purpose of promoting education, scientific research, and charitable purposes, and to assist in developing and advancing the University in furthering, improving, and expanding its properties, services, facilities, and activities. Because of the significance of the relationship between the University and the USA Foundation, the USA Foundation is considered a component unit of the University. The Board of Directors of the USA Foundation is not appointed or controlled by the University. The University receives distributions from the USA Foundation primarily for scholarship, faculty and other support. Total

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distributions received or accrued by the University for the year ended September 30, 2018 were $9,703,000, and are included primarily in other nonoperating revenues and capital contributions and grants in the University's statement of revenues, expenses, and changes in net position. The USA Foundation presents its financial statements in accordance with standards issued by the Financial Accounting Standards Board (FASB). The USA Foundation is reported in separate financial statements because of the difference in the financial reporting format since the USA Foundation follows FASB rather than GASB pronouncements. The USA Foundation has a June 30 fiscal year end, which differs from the University's September 30 fiscal year end. In accordance with GASB Statement No. 14 and GASB Statement No. 61, this discretely presented unit has been included with the most recent fiscal year. The accompanying consolidated statement of financial position and statement of activities and changes in net assets for the USA Foundation as of and for the year ended June 30, 2018 are discretely presented.

(f) USA Research and Technology Corporation

USA Research and Technology Corporation is a not-for-profit corporation that exists for the purpose of furthering the educational and scientific mission of the University by developing, attracting, and retaining technology and research industries in Alabama that will provide professional and career opportunities to the University's students and faculty. Because of the significance of the relationship between the University and the Corporation, the Corporation is considered a component unit of the University. The Corporation presents its financial statements in accordance with GASB. The accompanying statement of net position and statement of revenues, expenses, and changes in net position for the Corporation as of and for the year ended September 30, 2018 are discretely presented.

(g) Measurement Focus and Basis of Accounting

For financial reporting purposes, the University is considered a special purpose governmental agency engaged only in business type activities, as defined by GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*. Accordingly, the University's basic 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.

(h) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires that management make estimates and assumptions affecting the reported amounts of assets and liabilities, revenues and expenses, as well as disclosure of contingent assets and liabilities. Actual results could differ from those estimates.

In particular, laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates related to these programs could change by a material amount in the near term.

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(i) Cash and Cash Equivalents

Cash and cash equivalents are defined as petty cash, demand accounts, certificates of deposit, and any short-term investments that take on the character of cash. These investments have maturities of less than three months at the time of purchase and include repurchase agreements and money market accounts.

(j) Investments and Investment Income

The University reports the fair value of investments using the three-level hierarchy established under GASB Statement No. 72, *Fair Value Measurement and Application*. The fair value of alternative investments (low-volatility multi-strategy funds of funds) and certain private equity partnerships do not have readily ascertainable market values and the University values these investments in accordance with valuations provided by the general partners or fund managers of the underlying partnerships or companies, typically based on net asset value (NAV) of the partnership or commingled vehicle. Because some of these investments are not readily marketable, the estimated fair value is subject to uncertainty and, therefore, may differ from the fair value that would have been used had a ready market for the investment existed. Investments received by gift are recorded at fair value at the date of receipt. Changes in the fair value of investments are reported in net investment income.

(k) Derivatives

The University has adopted the provisions of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement No. 53 establishes a framework for accounting and financial reporting related to derivative instruments, requiring the fair value of derivatives to be recognized in the basic financial statements. At September 30, 2018, the University had two hedging derivative instruments, interest rate swaps, in effect. In accordance with hedge accounting, the changes in fair values of the interest rate swaps are reported as changes in deferred inflows and outflows and the fair values of the interest rate swaps are recognized in other long-term liabilities and deferred inflows and outflows on the statement of net position since the interest rate swaps were deemed effective.

(l) Deferred Outflows and Inflows of Resources

Deferred outflows of resources consist of employer contributions to the Teacher's Retirement System of Alabama and the Public Education Employees Health Insurance Plan subsequent to the plans' measurement dates, changes in proportion and differences between employer contributions and proportionate share of contributions related to the OPEB plan, changes in actuarial and other assumptions related to the pension plan and the loss on the defeasement of certain bond amounts.

Deferred inflows of resources consist of the proportionate share of the differences between expected and actual experience related to the pension plan, net difference between projected and actual earnings on pension and OPEB plan investments, changes of assumptions in OPEB plan, changes in proportion and differences between employer contributions and proportionate share of contributions in pension plan, fair values of interest rate swaps and gain on the refunding of certain bond amounts.

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(m) Bond Premiums, Discounts, and Debt Extinguishment Costs

Bond premiums, discounts, and debt extinguishment costs associated with the issuance of certain bond series are capitalized and amortized over the life of the respective bond series on a straight-line basis in accordance with generally accepted accounting principles.

(n) Accounts Receivable

Patient receivables primarily result from hospital and ambulatory patient service revenues. Accounts receivable – other includes amounts due from students, the federal government, state and local governments, or private sources in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts. Accounts and patient receivables are recorded net of estimated uncollectible amounts.

(o) Inventories

The University's inventories primarily consist of medical supplies and pharmaceuticals. Medical supplies and pharmaceuticals are stated at the lower of cost (first-in, first-out method) or market.

(p) Capital Assets

Capital assets are recorded at cost, if purchased, or, if donated, at acquisition value at the date of donation. Depreciation is provided over the estimated useful life of each class of depreciable assets using the straight-line method. Major renewals and renovations are capitalized. Costs for repairs and maintenance are expensed when incurred. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and the gain or loss, if any, is included in nonoperating revenues (expenses) in the statement of revenues, expenses, and changes in net position.

All capital assets other than land are depreciated using the following asset lives:

Buildings, infrastructure and certain building components	40 to 100 years
Fixed equipment	10 to 20 years
Land improvements	8 to 20 years
Library materials	10 years
Other equipment	4 to 15 years

Certain buildings are componentized for depreciation purposes.

Interest costs for certain constructed assets are capitalized as a component of the cost of acquiring those assets. The amount of interest capitalized for the year ended September 30, 2018 was approximately $1,105,000.

The University evaluates impairment in accordance with GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. For the year ended September 30, 2018, no impairments were recorded.

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(q) Unrecognized Revenues

Student tuition, fees, and dormitory rentals are initially recorded as unrecognized revenues and then recognized over the applicable portion of each school term.

(r) Cost Sharing Multiple-Employer Pension Plan

Employees of the University are covered by a cost sharing multiple-employer defined benefit pension plan (the Plan) administered by the Teachers' Retirement System of Alabama (TRS). The TRS financial statements are prepared using the economic resources measurement focus and accrual basis of accounting. Contributions are recognized as revenues when earned, pursuant to plan requirements. Benefits and refunds are recognized as expenses when due and payable in accordance with the terms of the Plan. Expenses are recognized when the corresponding liability is incurred, regardless of when the payment is made. Investments are reported at fair value. Financial statements are prepared in accordance with requirements of the GASB. Under these requirements, the Plan is considered a component unit of the State of Alabama and is included in the State's Comprehensive Annual Financial Report.

(s) Postemployment Benefits Other Than Pensions (OPEB)

Employees of the University are covered by a cost sharing multiple-employer other post employment benefit plan administered by the Alabama Retired Education Employees Health Care Trust (Trust). The Trust's financial statements are prepared using the economic resources measurement focus and accrual basis of accounting. This includes for purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the Trust and additions to/deductions from the Trust's fiduciary net position. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due pursuant to plan requirements. Benefits are recognized when due and payable in accordance with the terms of the plan. In accordance with GASB, the Trust is considered a component unit of the State of Alabama and is included in the State's Comprehensive Annual Financial Report.

(t) Classification of Net Position

The University's net position is classified as follows:

Net investment in capital assets reflects the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such debt is excluded from the calculation of *net investment in capital assets*.

Restricted, nonexpendable net position consists of endowment and similar type funds for which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

Restricted, expendable net position includes resources that the University is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

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Unrestricted net position represents resources derived from student tuition and fees, state appropriations, patient service revenues, sales and services of educational activities and auxiliary enterprises. Auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty and staff. While unrestricted net position may be designated for specific purposes by action of management or the Board of Trustees, they are available for use at the discretion of the governing board to meet current expenses for any purpose. Substantially all unrestricted net position is designated for academic and research programs and initiatives and capital programs.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the University addresses each situation on a case-by-case basis prior to determining the resources to be used to satisfy the obligation.

(u) Scholarship Allowances and Student Financial Aid

Student tuition and fees, and certain other revenues from students, are reported net of scholarship discounts and allowances in the statement of revenues, expenses, and changes in net position. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the University and the amount paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants and other federal, state, or nongovernmental programs are recorded as either operating or nonoperating revenues in the University's basic financial statements based on their classification as either an exchange or a nonexchange transaction. To the extent that revenues from such programs satisfy tuition and fees and certain other student charges, the University has recorded a scholarship discount and allowance.

(v) Donor Restricted Endowments

The University is subject to the "Uniform Prudent Management of Institutional Funds Act" (UPMIFA) of the Code of Alabama. This law allows the University, unless otherwise restricted by the donor, to spend net appreciation, realized and unrealized, of the endowment assets. The law also allows the University to appropriate for expenditure or accumulate to an endowment fund such amounts as the University determines to be prudent for the purposes for which the endowment fund was established. The University's endowment spending policy provides that 4.5% of the five-year invested net asset moving average value (inclusive of net realized and unrealized gains and losses), as measured at September 30, is available annually for spending. The University's policy is to retain the endowment net interest and dividend income and net realized and unrealized appreciation with the endowment after distributions allowed by the spending policy have been made. These amounts, unless otherwise directed by the donor, are included in restricted expendable net position.

(w) Classification of Revenues

The University has classified its revenues as either operating or nonoperating revenues.

Operating revenues include activities that have the characteristics of exchange transactions such as student tuition and fees, net of scholarship discounts and allowances; patient service revenues, net of provision for bad debts; most federal, state, and local grants and contracts; and sales and services of auxiliary enterprises, net of scholarship allowances.

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Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as state appropriations, investment income and gifts and contributions.

(x) Gifts and Pledges

Pledges of financial support from organizations and individuals representing an unconditional promise to give are recognized in the basic financial statements once all eligibility requirements, including time requirements, have been met. In the absence of such a promise, revenue is recognized when the gift is received. Endowment pledges generally do not meet eligibility requirements, as defined by GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, and are not recorded as assets until the related gift has been received. Unconditional promises that are expected to be collected in future years are recorded at the present value of the estimated future cash flows.

(y) Grants and Contracts

The University has been awarded grants and contracts for which funds have not been received or expenditures made for the purpose specified in the award. These awards have not been reflected in the basic financial statements, but represent commitments of sponsors to provide funds for specific research or training projects. For grants that have allowable cost provisions, the revenue will be recognized as the related expenditures are made. For grants with work completion requirements, the revenue is recognized as the work is completed. For grants without either of the above requirements, the revenue is recognized as it is received.

(z) Patient Service Revenues and Electronic Health Records Incentive Program

Patient service revenues are reported at estimated net realizable amounts due from patients, third-party payers and others for healthcare services rendered, including estimated retroactive revenue adjustments due to future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such amounts are adjusted in future periods, as adjustments become known or as years are no longer subject to such audits, reviews and investigations.

The Centers for Medicare and Medicaid Services (CMS) has implemented provisions of the American Recovery and Reinvestment Act of 2009 that provide incentive payments for the meaningful use of certified electronic health record (EHR) technology. CMS has defined meaningful use as meeting certain objectives and clinical quality measures based on current and updated technology capabilities over predetermined reporting periods as established by CMS. The Medicare EHR incentive program provides annual incentive payments to eligible professionals, and hospitals, that are meaningful users of certified EHR technology. The Medicaid EHR incentive program provides annual incentive payments to eligible professionals and hospitals for efforts to adopt, implement, and meaningfully use certified EHR technology. USA Health, a division of the University, which includes two hospitals and a cancer treatment center, utilizes a grant accounting model to recognize EHR incentive revenues. EHR incentive revenue is recorded ratably throughout the incentive reporting period when it is reasonably assured that it will meet the meaningful use objectives for the required reporting period and that the grants will be received. The EHR reporting period for hospitals is based on the federal fiscal year, which runs from October 1 through September 30.

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University Hospital has met the Medicare and Medicaid meaningful use objectives for fiscal year 2017 and also expects to meet meaningful use objectives in fiscal 2018. No meaningful use payment is expected for fiscal year 2018 as a result of the transition to the Merit-Based Incentive Payment System, which is an ambulatory Eligible Professional attestation. While University Hospital is moving to Penalty Aversion, it is still in the Meaningful Use program for eligible hospitals. Any payment adjustments for fiscal year 2017 and 2018 will not be paid until 2019.

(aa) Compensated Absences

The University accrues annual leave for employees as incurred at rates based upon length of service and job classification.

(bb) Recently Adopted Accounting Pronouncements

In 2018, the University adopted the provisions of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* which updates the reporting guidance for governmental institutions that provide other postemployment benefits by requiring the recognition of the University's proportionate share of the net OPEB liability, based on an actuarial valuation, and the OPEB expense in the basic financial statements. The statement also enhances financial statement note disclosures. The adoption of the provisions of GASB No. 75 resulted in a restatement of beginning unrestricted net position at October 1, 2017 by decreasing unrestricted net position $229,687,000 (see note 13 for further discussion).

(2) Income Taxes

The University is classified as both a governmental entity under the laws of the State of Alabama and as a tax-exempt entity under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3). Consistent with these designations, no provision for income taxes has been made in the accompanying basic financial statements.

In addition, the University's discretely presented component units, except for HCA, are tax-exempt entities under Section 501(a) of the Internal Revenue Code as organizations described in Section 501(c)(3). The income of HCA is excluded from federal and state income taxation pursuant to the provisions of Section 115(1) of the Internal Revenue Code. Consistent with these designations, no provision for income taxes has been made in the accompanying discretely presented financial statements.

(3) Cash

Pursuant to the Security for Alabama Funds Enhancement Act, funds on deposit may be placed in an institution designated as a qualified public depository (QPD) by the State of Alabama. QPD institutions pledge securities to a statewide collateral pool administered by the State Treasurer's office. Such financial institutions contribute to this collateral pool in amounts proportionate to the total amount of public fund deposits at their respective institutions. The securities are held at the Federal Reserve Bank and are designated for the State of Alabama. Additional collateral was not required for University funds on deposit with QPD institutions. At September 30, 2018, the net public deposits subject to collateral requirements for all institutions participating in the pool totaled approximately $11.4 billion. The University had cash and cash equivalents, including restricted cash and cash equivalents, in the pool of $96,336,000 at September 30, 2018.

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At September 30, 2018, restricted cash and cash equivalents consist of $6,411,000 related to cash included in the PLTF and GLTF to pay insurance liability claims, $1,722,000 related to collateral requirements of HCM, $8,189,000 of unspent proceeds from the issuance of University bonds for capital purchases as outlined in the bond indenture, and $59,000 related to endowment funds.

(4) Investments

(a) University of South Alabama

The investments of the University are invested pursuant to the University of South Alabama "Nonendowment Cash Pool Investment Policies," the "Endowment Fund Investment Policy," and the "Derivatives Policy" (collectively referred to as the University Investment Policies) as adopted by the Board of Trustees. The purpose of the nonendowment cash pool investment policy is to provide guidelines by which commingled funds not otherwise needed to meet daily operational cash flows can be invested to earn a maximum return, yet still maintain sufficient liquidity to meet fluctuations in the inflows and outflows of University operational funds. Further, endowment fund investment policies exist to provide earnings to fund specific projects of the endowment fund, while preserving principal. The University Investment Policies require that management apply the "prudent person" standard in the context of managing its investment portfolio.

The investments of the blended component units of the University are invested pursuant to the separate investment policy shared by the PLTF and GLTF (the Trust Fund Investment Policy.) The objectives of the Trust Fund Investment Policy are to provide a source of funds to pay general and professional liability claims and to achieve long-term capital growth to help defray future funding requirements. Additionally, certain investments of the University's component units, both blended and discretely presented, are subject to UPMIFA as well as any requirements placed on them by contract or donor agreements.

Certain investments, primarily related to the University's endowment assets, are pooled. The University uses this pool to manage its investments and distribute investment income to individual endowment funds.

Investments of the University, by type, at fair value, are as follows at September 30, 2018 (in thousands):

U.S. Treasury securities	$	9,139
U.S. federal agency notes		103,119
Commingled equity funds		113,863
Commingled fixed income funds		38,184
Marketable equity securities		12,803
Real estate		275
Private equity		2,049
Managed income alternative investments (low-volatility multi-strategy funds of funds)		33,732
	$	313,164

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At September 30, 2018, restricted investments consist of endowment funds, funds held in the PLTF and GLTF to pay insurance liability claims and funds related to collateral requirements of the interest rate swaps.

At September 30, 2018, $19,120,000 of cumulative appreciation in fair value of investments of donor-restricted endowments was recognized and is included in restricted expendable net position in the accompanying statement of net position.

(i) Credit Risk and Concentration of Credit Risk

Nonendowment Cash Pool Investment Policy

The University Investment Policies limit investment in corporate bonds to securities with a minimum "A" rating, at the time of purchase, by both Moody's and Standard and Poor's. Investments in corporate paper are limited to issuers with a minimum quality rating of P-1 by Moody's, A-1 by Standard and Poor's or F-1 by Fitch.

Additionally, the University Investment Policies require that not more than 10% of the cash, cash equivalents and investments of the University be invested in the obligations of a single private corporation and not more than 35% of the cash, cash equivalents and investments of the University be invested in the obligations of a single government agency.

Endowment Fund Investment Policy

The University Investment Policies limit investment in fixed income securities to securities with a minimum "BAA" rating, at the time of purchase, by both Moody's and Standard and Poor's. Money Market Funds selected shall contain securities whose credit rating at the absolute minimum would be rated investment grade by Standard and Poor's, and/or Moody's. Investment in fixed income securities within the fixed income portfolio shall be restricted to only investment grade bonds rated "BAA" or higher. Any investment in below investment grade bonds shall be considered an equity or fixed income alternative investment.

Additionally, the University Investment Policies require that not more than 5% of the Endowment Fund assets of the University be allocated to an individual investment manager and no more than 25% of the Endowment Fund assets be allocated to a "Funds of Funds" or multi-manager fund.

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The University's exposure to credit risk and concentration of credit risk at September 30, 2018 is as follows:

	Credit rating	Percentage of total investments
Federal National Mortgage Association	AAA	9.1 %
Federal Home Loan Mortgage Corporation	AAA	4.6
Federal Farm Credit Banks Funding Corporation	AAA	9.9
Common Fund Bond Fund	AAA	10.4
Federal Farm Credit Banks Debenture	AAA/AA+	8.7
PIMCO Pooled Bond Fund	BAA+/AA/A	1.8
Federal Home Loan Banks Debenture	AAA/AA+	0.6
US Treasury securities	AAA/AA+	2.9

(ii) *Interest Rate Risk*

At September 30, 2018, the maturity dates of the University's fixed income investments are as follows (in thousands):

		Years to maturity			
	Fair value	Less than 1	1–5	6–10	More than 10
U.S. Treasury securities	$ 9,139	9,139	—	—	—
U.S. federal agency notes	103,119	23,819	79,300	—	—
Commingled fixed income funds	38,184	2,936	—	2,707	32,541
	$ 150,442	35,894	79,300	2,707	32,541

Commingled fixed income funds are classified based on the weighted average maturity of the individual investment instruments within each fund.

The University's Investment Policies do not specifically address the length to maturity on investments which the University must follow; however, they do require that the maturity range of investments be consistent with the liquidity requirements of the University.

(iii) *Mortgage-Backed Securities*

The University, from time to time, invests in mortgage-backed securities such as the Federal Home Loan Mortgage Corporation (FHLMC), the Federal National Mortgage Association (FNMA), and other government sponsored enterprises of the United States government. The University invests in these securities to increase the yield and return on its investment portfolio given the available alternative investment opportunities.

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(iv) Fair Value Measurement

Fair value measurements represent the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The University measures and records its investments using fair value measurement guidelines established by GASB Statement No. 72. These guidelines prioritize the inputs of valuation techniques used to measure fair value, as follows:

- Level 1: Quoted prices for identical investments in active markets;
- Level 2: Observable inputs other than quoted market prices; and,
- Level 3: Unobservable inputs

The level in the fair value hierarchy that determines the classification of an asset or liability depends on the lowest level input that is significant to the fair value measurement. Observable inputs are derived from quoted market prices for assets or liabilities traded on an active market where there is sufficient activity to determine a readily determinable market price. Investments that are not traded on an active exchange and do not have a quoted market price are classified as unobservable inputs. The University's assets that have unobservable inputs consist of the investment in real estate, with fair value based on an independent third party appraisal performed by qualified appraisers specializing in real estate investments, and of investments in private capital, with fair value determined by the investment managers and primarily utilizes management assumptions and best estimates after considering internal and external factors. Other assets included in the University's investment portfolio with unobservable inputs are the shares or units in certain partnerships or other commingled funds that do not have readily determinable fair values. For these funds, fair value is estimated using the net asset value reported by the investment managers as a practical expedient to fair value. Such investments have not been categorized within 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 presented in the statement of net position.

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The following tables summarize the fair value measurements for all investment assets and liabilities carried at fair value as of September 30, 2018 (in thousands):

Description		Asset fair value measurements at September 30, 2018			
		Level 1	Level 2	Level 3	Total
U.S. Treasury securities	$	9,139	—	—	9,139
U.S. federal agency notes		—	103,119	—	103,119
Commingled equity funds		66,895	46,968	—	113,863
Commingled fixed income funds		5,642	32,542	—	38,184
Marketable equity securities		12,803	—	—	12,803
Private equity		—	—	1,640	1,640
Real estate		—	—	275	275
Total investments at fair value	$	94,479	182,629	1,915	279,023
Investments measured at NAV:					
Private equity					409
Managed income alternative investments (low volatility multi-strategy funds of funds)					33,732
Total investments				$	313,164

Description		Liability fair value measurements at September 30, 2018			
		Level 1	Level 2	Level 3	Total
Interest rate exchange agreements	$	—	33,826	—	33,826

A rollforward schedule of amounts for Level 3 financial instruments for the fiscal year ended September 30, 2018 is as follows (in thousands):

Description		Private equity and real estate
Beginning balance	$	1,144
Purchases		665
Net realized/unrealized gains		303
Sales		(197)
Ending balance	$	1,915

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(b) University of South Alabama Foundation

Investments in securities consist primarily of equity securities totaling $137,722,000 at June 30, 2018.

Investment income was comprised of the following for the year ended June 30, 2018 (in thousands):

Unrealized gains	$	15,736
Realized gains		4,210
Timber sales		2,921
Interest and dividends		2,124
Rents		646
Royalties		89
	$	25,726

Investment related expenses in the amount of $347,000, are included in the USA Foundation's management and general expenses in the accompanying consolidated statement of activities and changes in net assets.

Real estate at June 30, 2018 consisted of the following property held (in thousands):

Land and land improvements – held for investment	$	68,071
Building and building improvements – held for investment		1,092
	$	69,163

Timber and mineral properties are stated at fair value. Depletion of mineral properties is recognized over the remaining producing lives of the properties based on total estimated production and current-period production. Depletion of timber properties is recognized on a specific identification basis as timber rights are sold or on a unit basis for sales made on that basis. Reforestation costs consisting of site preparation and planting of seedlings are capitalized.

Investments at June 30, 2018, include an equity interest in a timberland management company. The company's primary assets consist of timberland. The Foundation's proportionate share of the fair value of the company is based upon the valuation from the trustee responsible for the management of the company and the timber valuation.

The USA Foundation has adopted Accounting Standards Codification (ASC) 820, *Fair Value Measurement and Disclosures*. ASC 820 provides a single definition of fair value and a hierarchical framework for measuring it, as well as establishing additional disclosure requirements about the use of fair value to measure assets and liabilities. Fair value measurements are classified as either observable or unobservable in nature. Observable fair values are derived from quoted market prices for investments traded on an active exchange or in dealer markets where there is sufficient activity and liquidity to allow price discovery by substantially all market participants (Level 1). The USA Foundation's observable values consist of investments in exchange-traded equity securities with a readily determinable market

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price. Other observable values are fair value measurements derived either directly or indirectly from quoted market prices (Level 2). Investments that are not traded on an active exchange and do not have a quoted market price are classified as unobservable (Level 3). The USA Foundation's unobservable values consist of investments in timber and real estate with fair values based on independent third-party appraisals performed by qualified appraisers specializing in timber and real estate investments.

The USA Foundation's investment assets at June 30, 2018, are summarized based on the criteria of ASC 820 as follows (in thousands):

	Fair value measurements at June 30, 2018			
Description	**Level 1**	**Level 2**	**Level 3**	**Total**
Equity securities	$ 84,072	—	—	84,072
Timber and mineral properties	—	—	160,949	160,949
Real estate	—	—	69,163	69,163
Other investments	—	—	5,805	5,805
	$ 84,072	—	235,917	319,989
Investment in Commonfund measured at NAV				53,650
				$ 373,639

For the year ended June 30, 2018, activity in investment assets valued at fair value based on unobservable values is as follows (in thousands):

Description	**Timber and mineral properties**	**Real estate**	**Other investments**	**Total**
Beginning balance	$ 160,351	69,186	5,808	235,345
Net unrealized gains	4,533	10	(3)	4,540
Additions	25	7	—	32
Reforestation	112	—	—	112
Depreciation/depletion	(4,072)	(40)	—	(4,112)
Ending balance	$ 160,949	69,163	5,805	235,917

As of June 30, 2018, the USA Foundation has no outstanding commitments to purchase securities or other investments. Additionally, substantially all of the USA Foundation's equity securities at June 30, 2018 are considered readily liquid. Timber and mineral properties, real estate, and other investments are generally considered illiquid.

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(5) Capital Assets

(a) University of South Alabama

A summary of the University's capital asset activity for the year ended September 30, 2018 follows (in thousands):

	Beginning balance	Additions	Transfers	Reductions	Ending balance
Capital assets not being depreciated:					
Land and other	$ 22,840	266	—	—	23,106
Construction-in-progress	130,024	49,188	(94,218)	(1,522)	83,472
	152,864	49,454	(94,218)	(1,522)	106,578
Capital assets being depreciated:					
Land improvements	33,814	361	5,416	—	39,591
Buildings, fixed equipment, and infrastructure	751,117	3,472	32,031	—	786,620
Other equipment	175,916	18,912	56,771	(5,414)	246,185
Library materials	71,070	3,888	—	—	74,958
	1,031,917	26,633	94,218	(5,414)	1,147,354
Less accumulated depreciation for:					
Land improvements	(21,846)	(1,378)	—	—	(23,224)
Buildings, fixed equipment, and infrastructure	(278,953)	(22,645)	—	—	(301,598)
Other equipment	(135,026)	(21,400)	—	5,237	(151,189)
Library materials	(54,988)	(3,117)	—	—	(58,105)
	(490,813)	(48,540)	—	5,237	(534,116)
Capital assets being depreciated, net	541,104	(21,907)	94,218	(177)	613,238
Capital assets, net	$ 693,968	27,547	—	(1,699)	719,816

At September 30, 2018, the University had commitments of approximately $15,174,000 related to various construction projects.

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(b) USA Research and Technology Corporation

Changes in capital assets for the year ended September 30, 2018 are as follows (in thousands):

		Beginning balance	Additions	Transfers	Reductions	Ending balance
Land	$	223	—	—	—	223
Land improvements		1,976	—	—	—	1,976
Buildings		28,291	12	—	—	28,303
Tenant improvements		1,155	682	3	—	1,840
Other equipment		275	111	—	(13)	373
Construction in progress - nondepreciable		3	—	(3)	—	—
		31,923	805	—	(13)	32,715
Less accumulated depreciation for:						
Land improvements		(1,218)	(94)	—	—	(1,312)
Buildings		(8,037)	(732)	—	—	(8,769)
Tenant improvements		(759)	(195)	—	—	(954)
Other equipment		(220)	(30)	—	—	(250)
		(10,234)	(1,051)	—	—	(11,285)
Capital assets, net	$	21,689	(246)	—	(13)	21,430

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(6) Noncurrent Liabilities

A summary of the University's noncurrent liability activity for the year ended September 30, 2018 follows (in thousands):

		Beginning balance	Additions	Reductions	Ending balance	Less amounts due within one year	Noncurrent liabilities
Long-term debt:							
Bonds payable	$	389,424	427	(19,650)	370,201	18,262	351,939
Notes payable		5,542	—	(382)	5,160	867	4,293
Capital lease obligations		17,332	4,940	(4,002)	18,270	4,968	13,302
Total long-term debt		412,298	5,367	(24,034)	393,631	24,097	369,534
Other noncurrent liabilities:							
Net pension liability		336,477	—	(39,823)	296,654	—	296,654
Net OPEB liability		—	256,178	—	256,178	—	256,178
Other long-term liabilities		101,992	2,067	(12,894)	91,165	6,669	84,496
Total other noncurrent liabilities		438,469	258,245	(52,717)	643,997	6,669	637,328
Total noncurrent liabilities	$	850,767	263,612	(76,751)	1,037,628	30,766	1,006,862

Other long-term liabilities primarily consist of self-insurance liabilities, liabilities related to compensated absences, and the fair value of derivatives. Amounts due within one year are included in current portion of other long-term liabilities.

During 2017, the University entered into a note payable for a period of ten years payable monthly at $19,000. This agreement commenced in November 2016 to finance improvements of the HVAC system. The amount outstanding on the note at September 30, 2018 is $1,831,000, and is reported as long-term debt (and current portion thereof) in the statement of net position.

In March 2015, the University entered into a variable interest rate revolving line of credit with Compass Bank to, among other reasons, fund the acquisition of certain real property by USA Health. The total amount available under the line of credit was $5,000,000 and interest on the outstanding amounts accrued at the rate of the London InterBank Offered Rate (LIBOR) plus 1.00%. In July 2018, the University converted the line of credit into a term loan for a period of five years, with monthly payments of $63,000 and interest accruing at the fixed rate of 3.85% per annum. The amount outstanding at September 30, 2018 is $3,329,000, and is reported as long-term debt (and current portion thereof) in the statement of net position.

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(a) USA Research and Technology Corporation

(i) Notes Payable

Notes payable consisted of the following (in thousands):

PNC Bank promissory note, 4.38%, payable through 2028	$	13,066
PNC Bank promissory note, 4.50%, payable through 2021		7,719
	$	20,785

During 2018, a variable interest rate note payable to Wells Fargo Bank, N.A. was refunded with the proceeds of a loan from PNC Bank, N.A. The note payable to Wells Fargo Bank, N.A. was incurred by the Corporation to acquire Buildings II and III in the USA Technology & Research Park and to provide funds for renovations and tenant finishing costs. In addition to refunding the Wells Fargo note payable, the refunding proceeds were used to terminate an interest rate swap that was used to fix the interest rate on the Wells Fargo note. Over the term of each note payable, the cash flows required to service the PNC Bank note payable exceed the cash flows required to service the Wells Fargo note payable by $2,352,759. The economic loss due to the refunding was $587,552. The first promissory note payable to PNC Bank has a 10-year term and amortization is based on a 20-year term. The promissory note payable is secured by an interest in tenant leases for Buildings II and III, and an interest in income received from rental of Buildings II and III. The Corporation agreed to not transfer or encumber the buildings or its leasehold interest in the real estate on which the buildings stand.

The second promissory note payable to PNC Bank has a 10-year term and amortization is based on a 20-year term. The promissory note payable is secured by an interest in tenant leases for Building I and the dialysis services building, and an interest in income received from rental of Building I and the dialysis services building. The Corporation agreed to not transfer or encumber the buildings or its leasehold interest in the real estate on which the buildings stand.

In connection with each PNC note, the University entered into an agreement with the lender providing that for any year in which the Corporation's debt service coverage ratio is less than 1 to 1, the University will pay the Corporation rent equal to the amount necessary to bring the ratio to 1 to 1. The debt service coverage ratio is calculated by dividing the sum of unrestricted cash and cash equivalents at the beginning of the year (reduced by current year capital asset additions) and current year change in net position (determined without depreciation, amortization, and interest expenses) by current year debt service. For fiscal 2018, the Corporation's debt service coverage ratio was 1.13 to 1. Management believes the Corporation was in compliance with its debt covenants, including the debt service coverage ratio covenant, at September 30, 2018.

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(ii) Debt Service on Long-Term Obligations

At September 30, 2018, total future debt service by fiscal year is as follows (in thousands):

		Debt service on notes		
		Principal	Interest	Total
2019	$	727	905	1,632
2020		760	872	1,632
2021		7,568	631	8,199
2022		485	504	989
2023		507	482	989
2024–2028		10,738	1,964	12,702
Total	$	20,785	5,358	26,143

(iii) Derivative Transaction

The Corporation was a party to a derivative with Wells Fargo Bank, N.A., the counterparty (successor to Wachovia Bank, N.A. the original counterparty). The derivative was a "receive-variable, pay-fixed" interest rate swap entered into in connection with the promissory note to Wells Fargo Bank, N.A.

Under the swap, the Corporation paid Wells Fargo a fixed payment of 6.10% and received a variable payment of the one-month LIBOR rate plus 0.85%. Conversely, the Wells Fargo loan bore interest at the one-month LIBOR rate plus 0.85%. The Corporation paid $329,600 under the interest rate swap agreement for the year ended September 30, 2018, which is reflected as an increase in interest expense.

The swap terminated on June 20, 2018 as part of a transaction refunding the Wells Fargo loan with the proceeds of a loan from PNC Bank. The fee paid by the Corporation to Wells Fargo to terminate the swap was $1,478,000. Pursuant to GASB Statement No. 65, the fee is reported in deferred outflows on the statement of net position and amortized to interest expense according to the percentage of annual interest paid on the loan from PNC Bank to the total interest to be paid on that loan over the 118 months that were remaining on the Wells Fargo loan when the swap was terminated.

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(7) Bonds Payable

Bonds payable consisted of the following at September 30, 2018 (in thousands):

Capital Appreciation Series 1999 Bonds, 4.70% to 5.25%, payable through November 2018	$	7,496
University Facilities Revenue Capital Improvement Bonds, Series 2010, 3.81%, payable through August 2030		20,482
University Facilities Revenue Capital Improvement Bonds, Series 2012-A, 2.92% payable through August 2032		18,842
University Facilities Revenue Capital Improvement Bonds, Series 2013-A, 2.83% payable through August 2033		25,589
University Facilities Revenue Capital Improvement Bonds, Series 2013-B, 2.83% payable through August 2033		6,397
University Facilities Revenue Capital Improvement Bonds, Series 2013-C, 2.78% payable through August 2028		7,112
University Facilities Revenue Refunding Bonds, Series 2014-A, variable rate payable at 68% of LIBOR plus 0.73%, 2.21% at September 30, 2018, payable through March 2024		39,030
University Facilities Revenue Capital Improvement Bonds, Series 2015, 2.47% payable through August 2030		4,500
University Facilities Revenue Refunding Bonds, Series 2016, 3.00% to 5.00% payable through November 2037		85,605
University Facilities Revenue Refunding Bonds, Series 2016-B, variable rate payable at 68% of one-month LIBOR plus 0.72%, 2.20% at September 30, 2018, payable through December 2036, pursuant to the right of the holder to cause all principal to be due after December 1, 2021		20,000
University Facilities Revenue Refunding Bonds, Series 2016-C, variable rate payable at 68% of one-month LIBOR plus 0.77%, 2.25% at September 30, 2018, payable through December 2036, pursuant to the right of the holder to cause all principal to be due after December 1, 2023		35,000
University Facilities Revenue Refunding Bonds, Series 2016-D, variable rate payable at 68% of one-month LIBOR plus 0.83%, 2.31% at September 30, 2018, payable through December 2036, pursuant to the right of the holder to cause all principal to be due after December 1, 2026		45,000
University Facilities Revenue Bonds, Series 2017, 2.00% to 5.00%, payable through October 2037		36,230
		351,283
Plus unamortized premium		20,761
Less unaccreted discount		(3)
Less unamortized debt extinguishment costs		(1,840)
	$	370,201

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Substantially all student tuition and fee and auxiliary revenues secure University bonds. Additionally, security for all bonds includes Children's and Women's Hospital revenues in an amount not exceeding $10,000,000. Capital Appreciation Series 1999 Bonds began maturing in November 2011. Series 1999 Bonds are not redeemable prior to maturity. Series 2008 Bonds were paid in full in August 2018. The Series 2010 Bonds began maturing in August 2011 and are redeemable beginning in February 2020. The Series 2012-A and 2012-B Bonds began maturing in August 2013. The Series 2012-A Bonds are redeemable beginning in August 2021 and the Series 2012-B Bonds were paid in full in February 2018. The Series 2013-A, 2013-B and 2013-C Bonds began maturing in August 2014 and are redeemable beginning in June 2023. The Series 2014-A bonds began maturing in March 2015 and are redeemable by the University at any time. The Series 2015 Bonds began maturing in August 2015 and are redeemable beginning in June 2020. The Series 2016 Bonds will begin maturing in November 2018 and are redeemable beginning in November 2026. The Series 2016-B, C & D Bonds will begin maturing in December 2024 and are redeemable beginning in December 2017. The Series 2017 Bonds began maturing in October 2017 and are redeemable beginning in October 2027.

In September 2016, the University issued its University Facilities Revenue Refunding Bonds, Series 2016, with a face value of $85,605,000. The proceeds from the Series 2016 Bonds were used to partially defease the Series 2008 Bonds. The funds were deposited into escrow trust funds to provide for the subsequent repayment of the Series 2008 Bonds when they are called in December 2018. Neither the asset of the escrow trust account, nor the defeased indebtedness is included in the accompanying statement of net position. The loss on the defeasement of the Series 2008 Bonds of $7,859,000 was recorded as a deferred outflow and is being amortized over the remaining life of the Series 2016 Bonds and the balance of the related deferred outflow totaled $7,051,000 at September 30, 2018. The principal outstanding on all defeased bonds is $93,540,000 at September 30, 2018. The undefeased portion of the Series 2008 bonds was paid in full in August 2018.

In December 2016, the University issued its University Facilities Revenue Refunding Bonds, Series 2016-B, C & D, with a face value totaling $100,000,000. The proceeds refunded the remaining outstanding Series 2006 Bonds. The gain on the refunding of the Series 2006 Bonds of $4,539,000 was recorded as a deferred inflow and is being amortized over the remaining life of the Series 2016-B, C & D Bonds and the balance of the related net deferred inflow at September 30, 2018 totaled $4,122,000.

During the year ended September 30, 2018, the maturity value of the Capital Appreciation Bonds increased $427,000, over the original principal amount of $19,810,000, reflecting accretion of interest.

Approximately $8,189,000 of proceeds from the issuance of the Series 2017 Bonds remained unspent at September 30, 2018 and is included in restricted cash and cash equivalents in the accompanying statement of net position. These funds are restricted for capital purposes as outlined in the bond indenture.

The University is subject to arbitrage restrictions on its bonded indebtedness prescribed by the U.S. Internal Revenue Service. As such, amounts are accrued as needed in the University's basic financial statements for any expected arbitrage liabilities. At September 30, 2018, no amounts were due or recorded in the financial statements.

The University is subject to restrictive covenants related to its bonds payable. At September 30, 2018, management believes the University complied with such financial covenants.

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Debt Service on Long-Term Obligations

Total debt service (which includes bonds and notes payable) by fiscal year is as follows as of September 30, 2018 (in thousands):

	Debt service on notes and bonds			
	Principal	**Interest**	**Additional maturity**	**Total**
2019	$ 18,182	9,838	(49)	27,971
2020	17,269	9,438	—	26,707
2021	18,032	9,002	—	27,034
2022	18,824	8,549	—	27,373
2023	19,528	8,076	—	27,604
2024–2028	93,045	32,905	—	125,950
2029–2033	94,366	18,498	—	112,864
2034–2038	77,246	4,816	—	82,062
Subtotal	356,492	$ 101,122	(49)	457,565
Plus (less):				
Additional maturity	(49)			
Unamortized bond premium	20,761			
Unaccreted bond discount	(3)			
Unamortized debt extinguishment costs	(1,840)			
Total	$ 375,361			

The principal amount of debt service due on bonds at September 30, 2018, includes $427,000, representing additional maturity value on Capital Appreciation Series 1999 Bonds. These bonds mature through fiscal 2019. Although this additional maturity is presented as principal on the debt service schedule above, it is also recognized as interest expense on an annual basis in the University's basic financial statements as it accretes.

(8) Capital Lease Obligations

The University has entered into various capital leases as a method of financing medical equipment, computer software and hardware, a heat recovery system, and other office equipment.

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Future minimum capital lease payments at September 30, 2018 are as follows (in thousands):

Year ending September 30:		
2019	$	5,495
2020		5,198
2021		5,077
2022		3,505
2023		153
		19,428
Less amounts representing interest		(1,158)
Net minimum lease payments	$	18,270

These amounts are included in long-term debt (and current portion thereof) in the accompanying statement of net position.

(9) Derivative Transactions – Interest Rate Swaps

The University is a party to two derivatives with Wells Fargo Bank, the counterparty. In December 2013, Wells Fargo exercised its option with respect to the synthetic advance refunding of the Series 2004 Bonds to enter into an interest rate swap agreement with the University with an effective date of March 15, 2014. The resulting derivative is a "receive-variable, pay-fixed" interest rate swap. As part of the overall plan of the synthetic refunding of the Series 2004 Bonds, the University redeemed those bonds in April 2014 with proceeds from the Series 2014-A Bonds.

In September 2016, Wells Fargo exercised its option with respect to the synthetic advance refunding of the Series 2006 Bonds to enter into an interest rate swap agreement with the University with an effective date of September 1, 2016. The resulting derivative is a "receive-variable, pay-fixed" interest rate swap. As part of the overall plan of the synthetic refunding of the Series 2006 Bonds, the University redeemed those bonds in December 2016 with proceeds from the Series 2016-B, C & D Bonds.

Objective of the transactions. As noted, both interest rate swaps were the result of the original January 2008 synthetic advance refunding of the Series 2004 and Series 2006 Bonds. The objective of these transactions was to realize debt service savings currently from future debt refunding and create an economic benefit to the University.

The 2014 swap will terminate in March 2024, when the Series 2014-A Bonds mature. The notional amount of the swap will at all times match the outstanding principal amount of the bonds. Under the swap, the University pays the counterparty a fixed semi-annual payment based on an annual rate of 4.9753% and receives on a monthly basis a variable payment of 68% of the one-month LIBOR plus 0.25%. Conversely, the Series 2014-A Bonds bear interest on a monthly basis at 68% of the one-month LIBOR rate plus 0.73%.

The 2016 swap will terminate in December 2036, when the Series 2016-B, C & D Bonds mature. The notional amount of the swap will at all times match the outstanding principal amount of the bonds. Under the swap,

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the University pays the counterparty a fixed semi-annual payment based on an annual rate of 5% and receives on a monthly basis a variable payment of 68% of the one-month LIBOR plus 0.25%. Conversely, the Series 2016-B, C & D Bonds bear a weighted average interest on a monthly basis at 68% of the one-month LIBOR rate plus 0.79%.

Fair value. The 2014 interest rate swap had a negative fair value of approximately $(9,138,000) at its inception. This amount, net of any amortization and adjustments to fair market value, is reported as a borrowing arising from the 2014 interest rate swap as other long-term liabilities in the amount of ($3,597,000) in the statement of net position at September 30, 2018. The change in the fair value of the swap of $2,268,000 during the year ended September 30, 2018, is reported as a deferred inflow and contra liability (other long-term liabilities) in the statement of net position since the interest rate swap is a hedging derivative instrument. Net deferred inflows of resources for the 2014 interest rate swap totaled $1,429,000 at September 30, 2018.

The 2016 interest rate swap had a negative fair value of approximately $(48,530,000) at its inception. This amount, net of any amortization and adjustments to fair market value, is reported as a borrowing arising from the 2016 interest rate swap as other long-term liabilities in the amount of ($30,229,000) in the statement of net position at September 30, 2018. The change in the fair value of the swap of $9,514,000 during the year ended September 30, 2018, is reported as a deferred inflow and contra liability (other long-term liabilities) in the statement of net position since the interest rate swap is a hedging derivative instrument. Net deferred inflows of resources for the 2016 interest rate swap totaled $13,308,000 at September 30, 2018.

The fair values of the interest rate swaps were estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement.

Risks Associated with these Transactions

Interest rate risk. As the LIBOR rate decreases, the net payments on the swaps increase. This, however, is mitigated by the fact that a decline in the LIBOR rate will also result in a decrease of the University's interest payments on the Series 2014-A and Series 2016-B, C & D Bonds. The University's exposure is limited to 0.48% and 0.54% of the notional amounts, the difference in the payment from the counterparty and the interest payment on the Series 2014-A and Series 2016-B, C & D Bonds.

Credit risk. As of September 30, 2018, the University was not exposed to credit risk on the interest rate swaps because they had a negative fair value. However, if interest rates change and the fair value of the derivatives become positive, the University would have a gross exposure to credit risk in the amount of the derivative's fair value. The counterparty was rated Aa2 by Moody's Investor Services and A+ by Standard & Poor's Ratings Services as of September 30, 2018.

Termination risk. The University may be required to terminate the swaps based on certain standard default and termination events, such as failure to make payments, breach of agreements and bankruptcy. As of the current date, no events of termination have occurred.

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Derivative payments and hedged debt. As interest rates fluctuate, variable rate debt interest and net derivative payments will fluctuate. Using interest rates as of September 30, 2018 and calculating interest for subsequent years using forward rates of one month LIBOR, debt service requirements for the 2014 interest rate swap payments, by fiscal year, are as follows (in thousands):

	Variable rate loan		Interest rate	
	Principal	Interest	swap, net	Total
2019	$ 665	820	1,291	2,776
2020	6,925	798	1,106	8,829
2021	7,280	640	877	8,797
2022	7,655	463	646	8,764
2023	8,050	284	397	8,731
2024	8,455	96	135	8,686
Total	$ 39,030	3,101	4,452	46,583

Debt service requirements for the 2016 interest rate swap payments, by fiscal year, are as follows (in thousands):

	Variable rate loan		Interest rate	
	Principal	Interest	swap, net	Total
2019	$ —	2,178	3,362	5,540
2020	—	2,358	3,183	5,541
2021	—	2,362	3,177	5,539
2022	—	2,341	3,199	5,540
2023	—	2,338	3,202	5,540
2024–2028	24,180	10,603	14,470	49,253
2029–2033	37,890	6,693	9,220	53,803
2034–2037	37,930	1,621	2,661	42,212
Total	$ 100,000	30,494	42,474	172,968

(10) Patient Service Revenues

USA Health has agreements with governmental and other third-party payers that provide for reimbursement at amounts different from their established rates. Contractual adjustments under third-party reimbursement programs represent the difference between USA Health's billings at established rates for services and amounts reimbursed by third-party payers.

A summary of the basis of reimbursement with major-third party payers follows:

Medicare – Substantially all acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Additionally, USA Health is reimbursed for both direct and indirect

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medical education costs (as defined), principally based on per-resident prospective payment amounts and certain adjustments to prospective rate-per-discharge operating reimbursement payments. USA Health is generally paid for certain retroactively determined items at tentative rates, with final settlement determined after submission of annual cost reports by USA Health and audits by the Medicare fiscal intermediary.

University Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2012.

USA Children's & Women's Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through September 30, 2016.

Revenues from the Medicare program accounted for approximately 18% of USA Health's net patient service revenues for the year ended September 30, 2018.

Blue Cross – Inpatient services rendered to Blue Cross subscribers are paid at a prospectively determined per diem rate. Outpatient services are reimbursed under a cost reimbursement methodology. For outpatient services, USA Health is paid at a tentative rate with final settlement determined after submission of annual cost reports by USA Health and audits thereof by Blue Cross.

University Hospital's and USA Children's & Women's Hospital's Blue Cross cost reports have been audited by Blue Cross through September 30, 2016. The settlement process changed in April 2017 and future settlements will be based on outpatients for the periods prior to April 2017. Blue Cross Cost findings are no longer required and it is not anticipated that settlements will occur for 2018 and future periods.

Revenues from the Blue Cross program accounted for approximately 28% of USA Health's net patient service revenues for the year ended September 30, 2018.

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are reimbursed at all-inclusive prospectively determined per diem rates. Outpatient services are reimbursed based on an established fee schedule.

USA Health qualifies as a Medicaid essential provider and, therefore, also receives supplemental payments based on formulas established by the Alabama Medicaid Agency. There can be no assurance that USA Health will continue to qualify for future participation in this program or that the program will not ultimately be discontinued or materially modified.

Revenues from the Medicaid program accounted for approximately 32% of USA Health's net patient service revenues for the year ended September 30, 2018.

Other – USA Health has entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payments to USA Health under these agreements include discounts from established charges and prospectively determined daily and case rates.

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The composition of net patient service revenues for the year ended September 30, 2018 follows (in thousands):

Gross patient service revenues	$	879,476
Less:		
Provision for contractual and other adjustments		(364,006)
Provision for bad debts		(99,436)
	$	416,034

Changes in estimates related to prior cost reporting periods resulted in an increase of approximately $5,568,000 in patient service revenues for the year ended September 30, 2018.

(11) Defined Benefit Cost Sharing Pension Plan

Employees of the University are covered by a cost sharing multiple-employer defined benefit pension plan administered by the TRS.

(a) Plan Description

The TRS was established in September 1939, under the provisions of Act 419 of the Legislature of 1939 for the purpose of providing retirement allowances and other specified benefits for qualified persons employed by State-supported educational institutions. The responsibility for the general administration and operation of the TRS is vested in its Board of Control. The TRS Board of Control consists of 15 trustees. The Plan is administered by the Retirement Systems of Alabama (RSA). Title 16-Chapter 25 of the code of Alabama grants the authority to establish and amend the benefit terms to the TRS Board of Control. The Plan issues a publicly available financial report that can be obtained at www.rsa-al.gov.

(b) Benefits Provided

State law establishes retirement benefits as well as death and disability benefits and any ad hoc increase in postretirement benefits for the TRS. Benefits for TRS members vest after ten years of creditable service. Tier 1 TRS members who retire after age sixty with ten years or more of creditable service or with twenty-five years of services (regardless of age) are entitled to an annual retirement benefit, payable monthly for life. Service and disability retirement benefits are based on a guaranteed minimum or formula method, with the member receiving payment under the method that yields the higher monthly benefit. Under the formula method, members of the TRS are allowed 2.0125% of their average final compensation (highest three of the last ten years) for each year of service.

Act 377 of the Legislature of 2012 established a new tier of benefits (Tier 2) for members hired on or after January 1, 2013. Tier 2 TRS members are eligible for retirement after age sixty-two with ten years or more of creditable service and are entitled to an annual retirement benefit, payable monthly for life. Service and disability retirement benefits are based on a guaranteed minimum or formula method, with the member receiving payment under the method that yields the highest monthly benefit. Under the formula method, Tier 2 members of the TRS are allowed 1.65% of their average final compensation (highest five of the last ten years) for each year of service. Members are eligible for disability retirement if they have ten years of credible service, are currently in-service, and determined by the RSA Medical

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Board to be permanently incapacitated form further performance of duty. Preretirement death benefits are calculated and paid to the beneficiary based on the member's age, service credit, employment status, and eligibility for retirement.

(c) Contributions

Covered members of the TRS contributed 5% of earnable compensation to the TRS as required by statute until September 30, 2011. From October 1, 2011 to September 30, 2012, covered members of the TRS were required by statute to contribute 7.25% of earnable compensation. Effective October 1, 2012, covered Tier 1 members of the TRS are required by statute to contribute 7.50% of earnable compensation. Certified law enforcement, correctional officers, and firefighters of the TRS contributed 6% of earnable compensation as required by statute until September 30, 2011. From October 1, 2011 to September 30, 2012, certified law enforcement, correctional officers, and firefighters of the TRS were required by statute to contribute 8.25% of earnable compensation. Effective October 1, 2012, certified law enforcement, correctional officers, and firefighters of the TRS are required by statute to contribute 8.50% of earnable compensation.

Tier 2 covered members of the TRS contribute 6% of earnable compensation to the TRS as required by statute. Tier 2 certified law enforcement, correctional officers, and firefighters of the TRS are required by statute to contribute 7% of earnable compensation.

Participating employers' contractually required contribution rates were 12.24% of annual pay for Tier 1 members and 11.01% of annual pay for Tier 2 members. These required contribution rates are a percent of annual payroll, actuarially determined as an amount that, when combined with member contributions, is expected to finance the costs of benefits earned by members during the year, with an additional amount to finance any unfunded accrued liability. Total employer contributions to the pension plan from the University were $22,951,000 for the year ended September 30, 2018.

(d) Pension Liabilities, Pension Expenses, Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At September 30, 2018, the University reported a liability of $296,654,000, for its proportionate share of the collective net pension liability. The collective net pension liability was measured as of September 30, 2017 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of September 30, 2016. The University's proportion of the collective net pension liability is based on the employer's shares of contributions to the pension plan relative to the total employer contributions of all participating TRS employers. At the measurement date of September 30, 2017, the University's proportion of contributions to the pension plan was 3.018313%, which was a decrease of 0.089735% from its proportion measured as of September 30, 2016.

For the year ended September 30, 2018, the University recognized pension expense of approximately $16,792,000, which is included in salaries and benefits on the statement of revenues, expenses, and changes in net position.

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At September 30, 2018, the University reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources (in thousands):

		Deferred outflows of resources	Deferred inflows of resources
Net difference between projected and actual earnings on pension plan investments	$	—	17,737
Changes of assumptions		17,706	—
Differences between expected and actual experience		—	12,718
Changes in proportion and differences between employer contributions and proportionate share of contributions		—	21,769
Employer contributions subsequent to measurement date		22,262	—
	$	39,968	52,224

At September 30, 2018, approximately $22,262,000 reported as deferred outflows of resources related to pensions resulting from University contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability for the year ending September 30, 2019. Other amounts reported as deferred outflows (inflows) of resources related to pensions will be recognized in pension expense as follows (in thousands):

Year ending September 30:		
2019	$	(11,594)
2020		(4,295)
2021		(9,985)
2022		(7,990)
2023		(654)
	$	(34,518)

(e) Actuarial Assumptions

The total pension liability as of September 30, 2018 was determined by an actuarial valuation as of September 30, 2016, using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.75 %
Investment rate of return*	7.75
Projected salary increases	3.25–5.00

* Net of pension plan investment expense

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The actuarial assumptions used in the September 30, 2016 valuation were based on the results of an actuarial experience study for the period October 1, 2010 through September 30, 2015. Mortality rates for TRS were based on the RP-2000 White Collar Mortality Table projected to 2020 using Scale BB and adjusted 115% for all ages for males and 112% for ages 78 and over for females.

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

	Target allocation	Long-term expected rate of return*
Fixed income	17.00 %	4.40 %
U.S. large stocks	32.00	8.00
U.S. mid stocks	9.00	10.00
U.S. small stocks	4.00	11.00
International developed market stocks	12.00	9.50
International emerging market stocks	3.00	11.00
Alternatives	10.00	10.10
Real estate	10.00	7.50
Cash equivalents	3.00	1.50
	100.00 %	

* Includes assumed rate of inflation of 2.50%

(f) Discount Rate

The discount rate used to measure the total pension liability as of September 30, 2018 was 7.75%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that the employer contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rate. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

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

The following table presents the University's proportionate share of the net pension liability calculated using the discount rate of 7.75%, as well as what the University's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.75%) or 1-percentage point higher (8.75%) than the current rate (in thousands):

		1% Decrease (6.75)%	Current rate (7.75)%	1% Increase (8.75)%
University's proportionate share of collective net pension liability	$	409,181	296,654	201,465

(h) Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in the separately issued RSA Comprehensive Annual Report for the fiscal year ended September 30, 2017 as well as prior year reports. The supporting actuarial information is included in the GASB Statement No. 67 Report for the TRS prepared as of September 30, 2017. The auditors' report dated April 4, 2018 on the total pension liability, total deferred outflows of resources, total deferred inflows of resources, and total pension expense for the sum of all participating entities as of September 30, 2017 along with supporting schedules is also available. The additional financial and actuarial information is available at www.rsa-al.gov.

(12) Other Employee Benefits

(a) Other Pension Plans

Certain employees of the University also participate in a defined contribution pension plan. The defined contribution pension plan covers certain academic and administrative employees, and participation by eligible employees is optional. The plan is administered by the University and the plan assets are held in annuity contracts and custodial accounts. The annuity contracts are with, and the custodial account assets are invested through investment options offered by, Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF) and Variable Annuity Life Insurance Company (VALIC). Under this plan, contributions by eligible employees are matched equally by the University up to a maximum of 3% of current annual pay. The University contributed $551,000 in 2018, representing 241 employees participating in this Plan.

All employees of HCM working at least half time are eligible to participate in a defined contribution pension plan. The plan is administered by HCM and the plan assets are held in annuity contracts and custodial accounts. The annuity contracts are with, and the custodial account assets are invested through investment options offered by, TIAA-CREF and VALIC. Under this plan, contributions by eligible employees are matched equally by HCM up to a maximum of 5% of current annual pay. HCM contributed $4,703,000 in 2018, representing 1,369 employees, participating in this plan. University employees as of September 30, 2010, who later transfer to HCM, are immediately vested in the plan. All other employees

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do not vest until they have held employment with HCM for thirty-six months; at which time they become 100% vested in the plan.

(b) Compensated Absences

Regular University employees accumulate vacation and sick leave and hospital and clinical employees accumulate paid time off. These are subject to maximum limitations, at varying rates depending upon their employee classification and length of service. Upon separation of employment, employees who were hired before January 1, 2012 are paid all unused accrued vacation at their regular rate of pay up to a maximum of two times their annual accumulation rate. Employees hired after January 1, 2012 are not eligible for payment of unused accrued vacation or PTO hours upon separation of employment. The accompanying statement of net position include accruals for vacation pay and paid time off of approximately $13,793,000 at September 30, 2018. The accrual is included in other long-term liabilities (and current portion thereof) in the accompanying basic financial statements. No accrual is recognized for sick leave benefits since no terminal cash benefit is available to employees for accumulated sick leave.

(13) Other Post-Employment Benefit Plans

Retirees of the University are covered by the Public Education Employees Health Insurance Plan (PEEHIP), which is a cost sharing multiple-employer defined benefit OPEB plan administered by the TRS.

(a) Plan Description

The Alabama Retiree Health Care Funding Act of 2007 authorized and directed the Public Education Employees Health Insurance Board (Board) to create an irrevocable trust to fund postemployment healthcare benefits to retirees participating in PEEHIP. Active and retiree health insurance benefits are paid through the PEEHIP. The PEEHIP was established in 1983 pursuant to the provisions of the Code of Alabama 1975, Title 16, Chapter 25A to provide a uniform plan of health insurance for active and retired employees of state and local educational institutions and to fund benefits related to the plan. The responsibility for the general administration and operation of the PEEHIP is vested in its Board, which consists of 15 trustees. Title 16-Chapter 25 of the code of Alabama grants the authority to establish and amend the benefit terms to the PEEHIP Board. Effective for the year ended September 30, 2018, GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions,* requires the reporting of the net OPEB liability and the OPEB expense in the financial statements as well as enhanced financial statement note disclosures.

(b) Benefits Provided

PEEHIP offers a basic hospital medical plan to active members and non-Medicare eligible retirees or active employees and non-Medicare eligible retirees who do not have Medicare eligible dependents can enroll in a health maintenance organization (HMO). In addition to or in lieu of the basic hospital medical plan or HMO, the PEEHIP offers four optional plans: Hospital Indemnity, Cancer, Dental, and Vision. Also, PEEHIP members (only active and non-Medicare eligible) may elect the Supplemental Plan as their hospital medical coverage instead of the PEEHIP Hospital Medical Plan. This Supplemental Plan provides secondary benefits to the member's primary plan provided by another employer.

Effective January 1, 2017, Medicare eligible members and Medicare eligible dependents who are covered on a retiree contract were enrolled in the United Healthcare Group Medicare Advantage plan for

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PEEHIP retirees. The Medicare Advantage Prescription Drug (MAPD) plan is fully insured by United Healthcare and members are able to have all of their Medicare Part A, Part B, and Part D in one convenient plan.

(c) Contributions

For employees who retired after December 31, 2011, the employer contribution to the health insurance premium set forth by the Board for each retiree class is reduced by 4% for each year of service less than 25 and increased by 2% for each year over 25, subject to adjustment by the Board for changes in Medicare premium costs required to be paid by a retiree. For employees who retired after December 31, 2011, who are not covered by Medicare, regardless of years of service, the employer contribution to the health insurance premium set forth by the Board for each retiree class is reduced by a percentage equal to 1% multiplied by the difference between the Medicare entitlement age and the age of the employee at the time of retirement as determined by the Board. This reduction in the employer contribution ceases upon notification to the Board of the attainment of Medicare coverage.

Total employer contributions to the OPEB plan from the University were $7,728,000 for the year ended September 30, 2018.

(d) OPEB Liabilities, OPEB Expenses, Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

At September 30, 2018, the University reported a liability of $256,178,000, for its proportionate share of the net OPEB liability. The net OPEB liability was measured as of September 30, 2017 and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of September 30, 2016. The University's proportion of the net OPEB liability was based on a projection of the University's long-term share of contributions to the OPEB plan relative to the projected contributions of all participating employers, actuarially determined. At the measurement date of September 30, 2017, the University's proportion of contributions to the OPEB plan was 3.449076%, which was an increase of 0.485263% from its proportion measured as of September 30, 2016.

For the year ended September 30, 2018, the University recognized OPEB expense of approximately $21,731,000, which is included in salaries and benefits on the statement of revenues, expenses, and changes in net position.

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At September 30, 2018, the University reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources (in thousands):

		Deferred outflows of resources	Deferred inflows of resources
Net difference between projected and actual earnings on OPEB plan investments	$	—	1,364
Changes of assumptions		—	26,599
Changes in proportion and differences between employer contributions and proportionate share of contributions		32,722	—
Employer contributions subsequent to the measurement date		7,728	—
	$	40,450	27,963

At September 30, 2018, approximately $7,728,000 reported as deferred outflows of resources related to OPEB resulting from University contributions subsequent to the measurement date will be recognized as a reduction of the net OPEB liability in the year ended September 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows (in thousands):

Year ending September 30:		
2019	$	830
2020		830
2021		830
2022		830
2023		1,171
Thereafter		268
	$	4,759

(CONTINUED)

(e) Actuarial Assumptions

The total OPEB liability as of September 30, 2018 was determined by an actuarial valuation performed as of September 30, 2016 using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.75%
Projected salary increases*	3.25%–5.00%
Long-term investment rate of return**	7.25%
Municipal bond index rate at the measurement date	3.57%
Municipal bond index rate at the prior measurement date	2.93%
Projected year for fiduciary net position to be depleted	2042
Single equivalent interest rate at the measurement date	4.63%
Single equivalent interest rate at the prior measurement date	4.01%
Healthcare cost trend rate	
Pre-medicare eligible	7.75%
Medicare eligible	5.00%
Ultimate trend rate	
Pre-medicare eligible	5.00%
Medicare eligible	5.00%
Year of ultimate trend rate	2022

* Includes 3.00% wage inflation

** Compounded annually, net of investment expense, and includes inflation

Rates of mortality for the period after service retirement are according to the RP-2000 White Collar Mortality Table projected to 2020 using scale BB and adjusted 115% for all ages for males and 112% for ages 78 and over for females. The rates of disabled mortality were based on the RP-2000 Disabled Mortality Table projected to 2020 using scale BB and adjusted 105% for males and 120% for females.

The decremental assumptions used in the valuation were selected based on the actuarial experience study prepared as of September 30, 2015, submitted to and adopted by the TRS on September 13, 2016. The remaining actuarial assumptions (e.g. initial per capita costs, health care cost trends, rate of plan participation, rates of plan election, etc.) used in the September 30, 2016 valuation were based on a review of recent plan experience done concurrently with the September 30, 2016 valuation.

The long-term expected rate of return on the OPEB plan investments is determined based on the allocation of assets by asset class and by the mean and variance of real returns.

(CONTINUED)

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

	Target allocation	Long-term expected real rate of return*
Fixed income	30.00 %	4.40 %
U.S. large stocks	38.00	8.00
U.S. mid stocks	8.00	10.00
U.S. small stocks	4.00	11.00
International developed market stocks	15.00	9.50
Cash	5.00	1.50
	100.00 %	

* Geometric mean, includes 2.5% inflation

(f) *Discount Rate*

The discount rate used to measure the total OPEB liability at September 30, 2017 was 4.63%. The projection of cash flows used to determine the discount rate assumed that plan contributions will be made at the current contribution rates. Each year, the State specifies the monthly employer rate that participating employers must contribute for each active employee. Approximately 27.08% of the employer contributions were used to assist in funding retiree benefit payments in 2016 and it is assumed that amount will increase by 3.00% per year. The discount rate determination will use a municipal bond rate to the extent the trust is projected to run out of money before all benefits are paid. The rate used for this purpose is the monthly average of the Bond Buyers General Obligation 20-year Municipal Bond Index Rate. Therefore, the projected future benefit payments for all current plan members were projected through 2115. The long-term rate of return is used until the assets are expected to be depleted in 2042, after which the municipal bond rate is used.

(g) *Sensitivity of the University's Proportionate Share of the Net OPEB Liability to Changes in the Health Care Cost Trend Rates and Discount Rates*

The following table presents the University's proportionate share of the net OPEB liability calculated using the health care cost trend rate of 7.75%, as well as what the net OPEB liability would be if calculated using 1-percentage point lower (6.75%) or 1-percentage point higher (8.75%) than the current rate (in thousands):

		1% Decrease (6.75)%	Current rate (7.75)%	1% Increase (8.75)%
University's proportionate share of collective net OPEB liability	$	206,833	256,178	319,846

(CONTINUED)

The following table presents the University's proportionate share of the net OPEB liability calculated using the discount rate of 4.63%, as well as what the net OPEB liability would be if calculated using 1-percentage point lower (3.63%) or 1-percentage point higher (5.63%) than the current rate (in thousands):

		1% Decrease (3.63)%	Current rate (4.63)%	1% Increase (5.63)%
University's proportionate share of collective net OPEB liability	$	309,666	256,178	213,541

(h) OPEB Plan Fiduciary Net Position

Detailed information about the OPEB plan's fiduciary net position is available in the Alabama Retired Education Employees' Health Care Trust's financial statements for the fiscal year ended September 30, 2017. The supporting actuarial information is included in the GASB Statement No. 74 Report for PEEHIP prepared as of September 30, 2017. Additional financial and actuarial information is available at www.rsa-al.gov.

(14) Risk Management

The University, HCM, SAMSF and HCA participate in the PLTF and the University, HCM, SAMSF, the Corporation and HCA participate in the GLTF. An independent trustee administers both funds. These trust funds are revocable and use contributions by the University and HCA, together with earnings thereon, to pay liabilities arising from the performance of its employees, trustees and other individuals acting on behalf of the University. Any risk related to the payment of claims is the responsibility of the PLTF and GLTF. If the trust funds are ever terminated, appropriate provision for payment of related claims will be made and any remaining balance may be distributed to the participating entities in proportion to contributions made.

As discussed in note 1, the PLTF and GLTF are blended component units of the University, and as such are included in the basic financial statements of the University for the year ended September 30, 2018. Claims and expenses are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Those losses include an estimate of claims that have been incurred but not reported and the future costs of handling claims. These liabilities are generally based on actuarial valuations and are reported at their present value.

The University, HCM and HCA each participate in a separate self-insured health plan, administered by unaffiliated entities. Administrative fees paid by the University for such services were approximately $2,276,000 in 2018. Contributions by the University and its employees, together with earnings thereon, are used to pay liabilities arising from healthcare claims. It is the opinion of University administration that plan assets are sufficient to meet future plan obligations.

(CONTINUED)

The changes in the total self-insurance liabilities for the year ended September 30, 2018 for the PLTF, GLTF and health plan are summarized as follows (in thousands):

Balance, beginning of year	$	39,115
Liabilities incurred and other additions		69,543
Claims, administrative fees paid and other reductions		(68,253)
Balance, end of year	$	40,405

These amounts are included in other long-term liabilities (and current portion thereof) in the accompanying statement of net position.

(15) Other Related Parties and Related-Party Transactions

SAMSF is a not-for-profit corporation that exists for the purpose of promoting education and research at the University. At September 30, 2018, SAMSF had total assets of $12,704,000, net assets of $10,828,000, and total revenues of $1,735,000. SAMSF reimburses the University for certain administrative expenses and other related support services. Total amounts received for such expenses were approximately $759,000 in 2018, and are reflected as private grants and contracts in the accompanying statement of revenues, expenses, and changes in net position.

(16) Commitments and Contingencies

(a) Grants and Contracts

At September 30, 2018, the University had been awarded approximately $18,442,000 in grants and contracts for which resources had not been received and for which reimbursable expenditures had not been made for the purposes specified. These awards, which represent commitments of sponsors to provide funds for research or training projects, have not been reflected in the accompanying basic financial statements, as the eligibility requirements of the awards have not been met. Advances are included in unrecognized revenues, and include amounts received from grant and contract sponsors which have not been expended under the terms of the agreements and, therefore, have not yet been included in revenues in the accompanying basic financial statements. Federal awards are subject to audit by federal agencies. The University's management believes any potential adjustment from such audits will not be material.

(b) Letter of Credit

In connection with USA Health's participation in the State of Alabama Medicaid Program, the University has established a $55,382 irrevocable standby letter of credit with Wells Fargo. The Alabama Medicaid Agency is the beneficiary of this letter of credit. No funds were advanced under this letter during the year ended September 30, 2018.

(c) Federal Program Review

In November 2014, the University was the subject of a program review conducted by the U. S. Department of Education. The program review assessed the University's administration of Title IV, Higher Education Act programs for the 2013-2014 fiscal year and the first two months of the 2015 fiscal year.

(CONTINUED)

On October 10, 2017, the University received the final program review determination letter. Management appealed the factual and legal contentions in, and the calculation of the monetary liabilities and interest asserted in and associated with two findings. Management believes there will be no liability to the University beyond the amount currently accrued in the basic financial statements. The other findings were resolved to the US Department of Education's satisfaction.

(d) Litigation

Various claims have been filed against the University alleging discriminatory employment practices and other matters. University administration and legal counsel are of the opinion the resolution of these matters will not have a material effect on the financial position or the statement of revenues, expenses, and changes in net position of the University.

(e) Rent Supplement Agreements

The University has entered into two irrevocable rent supplement agreements with the Corporation and a financial institution. The agreements require that, in the event the Corporation fails to maintain a debt service coverage ratio of one to one with respect to all of its outstanding indebtedness, the University will pay to the Corporation any and all rent amounts necessary to cause the Corporation's net operating income to be equal to the Corporation's annual debt service obligations (see note 6). As of September 30, 2018, no amounts were payable pursuant to these agreements.

(f) USA Research and Technology Corporation Leases

The Corporation leases space in Building I to three tenants under operating leases. One lease has a 5-year initial term expiring in October 2018 with two 5-year renewal options. The second lease has a 67-month initial term expiring in December 2018 with no renewal options. The third lease has a 90-month initial term with two 5-year renewal options.

Space in Buildings II and III is leased under operating leases to the University and various other tenants. The leases have remaining terms varying from month-to-month to four years.

The Corporation leases from the University the third floor of a campus building. Located on that floor is the Coastal Innovation Hub (the Hub), a technology incubator, which currently houses six tenants with month-to-month leases.

Under leases for Buildings I, II, and III, the Corporation must pay all operating expenses of the buildings, including utilities, janitorial, maintenance and insurance. Tenants will reimburse the Corporation for such expenses only as the total expenses for a year increase over the total expenses for the base year of the lease (the Corporation's fiscal year beginning after the date the lease is signed). Under Hub leases, the Corporation must pay all operating expenses of the space, without reimbursement from tenants.

Space under lease to the University was 51,168 square feet at September 30, 2018.

The Corporation owns a building located on the premises of the USA University Hospital, which is leased to a single tenant. The Corporation paid for construction of the building shell and land improvements while the tenant paid for the cost of finishing the building's interior. The lease has a 10-year initial term expiring in March 2020 with three 5-year renewal options. Under the lease, the tenant must also pay for

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utilities, taxes, insurance, and interior repairs and maintenance. The Corporation is responsible for repairs and maintenance to the exterior and HVAC system.

The Corporation, as lessor, had three ground leases in place at September 30, 2018. One lease is for a 40-year initial term expiring in October 2046 with 20-year, and 15-year renewal options. The second lease is for a 30-year initial term expiring in October 2036 with four 5-year renewal options. The third lease has a 38.5-year initial term expiring in September 2046 with 20-year and 15-year renewal options.

Minimum future rentals by fiscal year are as follows (in thousands):

2019	$	2,029
2020		1,459
2021		1,224
2022		1,131
2023		613
2024–2047		6,458
Total	$	12,914

(17) Functional Expense Information

Operating expenses by functional classification for the year ended September 30, 2018 are listed below (in thousands). In preparing the basic financial statements, all significant transactions and balances among blended component units have been eliminated.

Instruction	$	113,094
Research		25,578
Public service		7,871
Academic support		25,443
Student services		34,701
Institutional support		41,877
Operation and maintenance of plant		33,573
Scholarships		14,991
USA Health		450,748
Auxiliary enterprises		22,895
Depreciation and amortization		48,611
	$	819,382

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(18) Blended Component Units

As more fully described in note 1, HCM, PLTF and GLTF are reported as blended component units. Required combining financial information of the aggregate blended component units as of and for the year ended September 30, 2018 is presented below (in thousands):

Current assets	$	18,243
Noncurrent assets		60,482
Total assets		78,725
Current liabilities		40,616
Noncurrent liabilities		36,414
Total liabilities		77,030
Net position	$	1,695
Operating revenues	$	186,467
Operating expenses		(190,872)
Operating loss		(4,405)
Nonoperating revenues		4,482
Change in net position	$	77

(19) Recently Issued Accounting Pronouncements

In March 2016, the GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements* and Statement No. 82, *Pension Issues*. Both statements are effective for the University of South Alabama for the current reporting period. Statement No. 81 changes the reporting requirements for gifts given to the University in which the University is a beneficiary of a split-interest agreement. Statement No. 82 was issued to address certain matters that have been raised from Statements No. 67, 68 and 73 and clarifies the presentation of payroll-related measures in the required supplementary information, the selection of assumptions and treatment of deviations from the guidance, and the classification of payments made by employers to satisfy employee contribution requirements. In November 2016, the GASB issued Statement No. 83, *Certain Asset Retirement Obligations*. This statement will be effective for the University beginning with the fiscal year ending September 30, 2019. Statement 83 establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for ARO's.

(CONTINUED)

The GASB issued Statement No. 84, *Fiduciary Activities*, in January 2017. This statement will be effective for the University beginning with the fiscal year ending September 30, 2020. Statement 84 addresses the criteria for identifying fiduciary activities of all state and local governments. In March 2017, the GASB issued Statement No. 85, *Omnibus 2017*, which was effective for the University in the current reporting period. The objective is to ensure consistency in the application of accounting and financial reporting requirements related to various topics, including blending component units, goodwill, fair value measurement and application, and postemployment benefits. The GASB issued Statement No. 86, *Certain Debt Extinguishment Issues,* in May 2017. This statement was effective for the University in the current reporting period. Statement 86 addresses financial reporting for in-substance defeasance of debt and prepaid insurance on debt that is extinguished. In June 2017, the GASB issued Statement No. 87, *Leases,* which will be effective for the University beginning with the fiscal year ending September 30, 2021. This statement establishes a single model for lease accounting whereby certain leases that were previously classified as operating leases will now be reported on the statement of net position. Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements,* was issued in March 2018 to enhance note disclosure for debt agreements. This statement is effective for the University beginning with the fiscal year September 30, 2019. In June 2018, the GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period,* which will be effective beginning with fiscal year September 30, 2021. This statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. GASB Statement No. 90, *Majority Equity Interests,* was issued in August 2018. Effective for the University beginning with the fiscal year ending September 30, 2020, this statement specifies that a majority equity interest in a legally separate organization should be reported as an investment using the equity method, with certain exceptions, if a government holding of the equity interest meets the definition of an investment.

The effect of the implementation of GASB Statement Nos. 83, 84, 87, 88, 89 and 90 on the University has not yet been determined.

Statement No. 82 defines covered payroll, which is be presented in schedules of required supplementary information.

Statement Nos. 81, 85 and 86 did not have an impact on the University's financial statements.

UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Required Supplementary Information

Schedule of the University's Proportionate Share of the Net Pension Liability (Unaudited)

Teachers' Retirement Plan of Alabama

September 30, 2018

(In thousands)

		2018	2017	2016	2015
University's proportion of the net pension liability		3.018313 %	3.108048 %	3.185471 %	3.322348 %
University's proportionate share of the net pension liability	$	296,654	336,477	329,294	297,734
University's covered-employee payroll		191,520	200,464	198,378	201,858
University's proportionate share of the net pension liability as a percentage of its covered-employee payroll		154.89 %	167.85 %	165.99 %	147.50 %
Plan fiduciary net position as a percentage of the total pension liability		71.50 %	67.93 %	67.51 %	71.01 %

Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying independent auditors' report.

UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Required Supplementary Information

Schedule of the University's Pension Contributions (Unaudited)

Teachers' Retirement Plan of Alabama

September 30, 2018

(In thousands)

		2018	2017	2016	2015
Contractually required contribution	$	22,951	23,664	23,405	23,524
Contributions in relation to the contractually required contribution		22,951	23,664	23,405	23,524
Contribution deficiency (excess)	$	—	—	—	—
University's covered-employee payroll	$	191,520	200,464	198,378	201,858
Contributions as a percentage of covered-employee payroll		11.98 %	11.80 %	11.80 %	11.65 %

Schedule is intended to show information for 10 years.
Additional years will be displayed as they become available.

See accompanying independent auditors' report.

UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Required Supplementary Information

Schedule of the University's Proportionate Share of the Net OPEB Liability (Unaudited)

Alabama Retired Education Employees' Health Care Trust

September 30, 2018

(In thousands)

		2018	2017
University's proportion of the net OPEB liability		3.449076 %	2.963813 %
University's proportionate share of the net OPEB liability	$	256,178	238,060
University's covered-employee payroll		191,520	200,464
University's proportionate share of the net OPEB liability as a percentage of its covered-employee payroll		133.76 %	118.75 %
Plan fiduciary net position as a percentage of the total OPEB liability		15.37 %	13.38 %

Schedule is intended to show information for 10 years. Additional years will be displayed as they become available.

See accompanying independent auditors' report.

UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)

Required Supplementary Information

Schedule of the University's OPEB Contributions (Unaudited)

Alabama Retired Education Employees' Health Care Trust

September 30, 2018

(in thousands)

		2018	2017
Contractually required contribution	$	7,728	8,373
Contributions in relation to the contractually required contribution		7,728	8,373
Contribution deficiency (excess)	$	—	—
University's covered-employee payroll	$	191,520	200,464
Contributions as a percentage of covered-employee payroll		4.04 %	4.18 %

Schedule is intended to show information for 10 years.
Additional years will be displayed as they become available.

See accompanying independent auditors' report.

(1) Summary of Cost Sharing Pension Plan Provisions and Assumptions

Employees of the University of South Alabama are covered by a cost sharing multiple-employer defined benefit pension plan administered by the Teachers Retirement System (TRS) of the State of Alabama.

(a) Actuarial Assumptions

The total pension liability as of September 30, 2018 was determined by an actuarial valuation as of September 30, 2016, using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.75 %
Investment rate of return*	7.75
Projected salary increases	3.25–5.00

* Net of pension plan investment expense

The actuarial assumptions used in the September 30, 2016 valuation were based on the results of an actuarial experience study for the period October 1, 2010 through September 30, 2015. Mortality rates for TRS were based on the RP-2000 White Collar Mortality Table projected to 2020 using Scale BB and adjusted 115% for all ages for males and 112% for ages 78 and over for females.

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

(b) Discount Rate

The discount rate used to measure the total pension liability as of September 30, 2018 was 7.75%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that the employer contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rate. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

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UNIVERSITY OF SOUTH ALABAMA
(A Component Unit of the State of Alabama)
Notes to Required Supplementary Schedules (Unaudited)
September 30, 2018

(2) Summary of OPEB Plan Provisions and Assumptions

Retirees of the University of South Alabama are covered by the Public Education Employees Health Insurance Plan (PEEHIP), which is a cost sharing multiple-employer defined benefit OPEB plan administered by the Teachers Retirement System (TRS) of the State of Alabama.

(a) Changes in Actuarial Assumptions

In 2016, rates of withdrawal, retirement, disability, mortality, spouse coverage, and tobacco usage were adjusted to more closely reflect actual experience. In 2016, economic assumptions and the assumed rates of salary increase were adjusted to more closely reflect actual and anticipated experience. In 2016 and later, the expectation of retired life mortality was changed to the RP-2000 White Collar Mortality Table projected to 2020 using scale BB and adjusted 115% for all ages for males and 112% for ages 78 and over for females.

(b) Recent Plan Changes

Effective January 1, 2017, Medicare eligible medical and prescription drug benefits are provided through the Medicare Advantage Prescription Drug plan.

The Health Plan was changed in 2017 to reflect the ACA maximum annual out-of-pocket amounts.

(c) Method and Assumptions Used in Calculations of Actuarially Determined Contributions

The actuarially determined contribution rates in the schedule of employer contributions are calculated as of September 30, 2014, three years prior to the end of the fiscal year in which contributions are reported. The following actuarial methods and assumptions were used to determine the most recent contribution rate reported in that schedule:

Actuarial cost method	Projected unit credit
Amortization method	Level percent of pay
Remaining amortization period	27 year, closed
Asset valuation method	Market value of assets
Inflation	3.00%
Health care cost trend rate:	
Pre-medicare eligible	7.50%
Medicare eligible	5.75%
Ultimate trend rate:	
Pre-medicare eligible	5.00%
Medicare eligible	5.00%
Year of ultimate trend rate	2019 for Pre-medicare eligible 2017 for Medicare eligible
Investment rate of return	5.00%, including inflation


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