

# **Kansas Health Foundation**

Independent Auditor's Report and Consolidated Financial Statements

December 31, 2018 and 2017

**Kansas Health Foundation**  
**December 31, 2018 and 2017**

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## Independent Auditor's Report

Board of Directors  
Kansas Health Foundation  
Wichita, Kansas

We have audited the accompanying consolidated financial statements of Kansas Health Foundation, which comprise the consolidated statements of financial position as of December 31, 2018 and 2017, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

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

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

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

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of KHF Fund, LP, a limited partnership in which Kansas Health Foundation has a controlling financial interest, whose statements reflect total assets constituting 37% and 30% of consolidated total assets as of December 31, 2018 and 2017, respectively, and total revenues, gains and losses of 3% and 15%, respectively, of consolidated total revenues, gains and losses for the years then ended. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for KHF Fund, LP, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Kansas Health Foundation as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of Matter***

As described in *Note 1* to the consolidated financial statements, in 2018, Kansas Health Foundation adopted Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

**BKD, LLP**

Wichita, Kansas  
October 10, 2019

**Kansas Health Foundation**  
**Consolidated Statements of Financial Position**  
**December 31, 2018 and 2017**

	<b>2018</b>	<b>2017</b>
<b>Assets</b>		
<b>Assets</b>		
Cash and cash equivalents	\$ 10,975,435	\$ 15,829,044
Investments	425,797,788	488,218,694
Due from underlying funds	13,844,959	664,015
Property and equipment, net	11,258,573	11,449,955
Construction in progress	1,904,276	-
Other assets	476,600	323,137
Total assets	\$ 464,257,631	\$ 516,484,845
 <b>Liabilities</b>		
<b>Liabilities and Net Assets</b>		
Accounts payable	\$ 173,757	\$ 38,952
Construction costs payable	561,612	-
Grants payable, net	22,852,854	29,964,152
Accrued expenses	210,538	245,829
Total liabilities	23,798,761	30,248,933
Net assets without donor restrictions	440,458,870	486,235,912
Total liabilities and net assets	\$ 464,257,631	\$ 516,484,845

**Kansas Health Foundation**  
**Consolidated Statements of Activities**  
**Years Ended December 31, 2018 and 2017**

	<b>Without Donor Restrictions 2018</b>	<b>Without Donor Restrictions 2017</b>
<b>Revenue, Gains and Losses</b>		
Investment income (loss)	\$ (28,810,316)	\$ 65,611,025
Other income	866,812	742,860
Total revenue, gains and losses	(27,943,504)	66,353,885
<b>Grants and Grant Related Activities, Net</b>	12,428,750	31,805,975
<b>Operating Expenses</b>		
Compensation and benefits	2,784,527	2,596,604
Professional and contractual services	840,157	791,495
Depreciation and amortization	578,123	665,105
Interest expense	-	134,754
Other expenses	1,201,981	1,180,380
Total operating expenses	5,404,788	5,368,338
<b>Increase (Decrease) in Net Assets</b>	(45,777,042)	29,179,572
<b>Net Assets, Beginning of Year</b>	486,235,912	457,056,340
<b>Net Assets, End of Year</b>	\$ 440,458,870	\$ 486,235,912

**Kansas Health Foundation**  
**Consolidated Statements of Functional Expenses**  
**Years Ended December 31, 2018 and 2017**

**Grants and Grant Related Activities - 2018**

	<b>Access to Care</b>	<b>Civic and Community Engagement</b>	<b>Education</b>	<b>Healthy Behaviors</b>	<b>Overall Health</b>	<b>Total Program Services</b>	<b>Total Management and General</b>	<b>Total</b>
Grant and grant related activities	\$ 1,057,284	\$ 4,700,828	\$3,432,867	\$ 1,884,041	\$1,353,730	\$12,428,750	\$ -	\$ 12,428,750
Compensation and benefits	88,318	284,765	197,156	323,186	120,355	1,013,780	1,770,747	2,784,527
Professional and contractual services	13,267	51,665	23,354	40,605	18,909	147,800	692,357	840,157
Depreciation and amortization	3,695	358,548	6,504	11,307	5,266	385,320	192,803	578,123
Other expenses	16,354	229,999	28,789	50,054	23,309	348,505	853,476	1,201,981
	<u>\$ 1,178,918</u>	<u>\$ 5,625,805</u>	<u>\$3,688,670</u>	<u>\$ 2,309,193</u>	<u>\$1,521,569</u>	<u>\$14,324,155</u>	<u>\$ 3,509,383</u>	<u>\$ 17,833,538</u>

**Grants and Grant Related Activities - 2017**

	<b>Access to Care</b>	<b>Civic and Community Engagement</b>	<b>Education</b>	<b>Healthy Behaviors</b>	<b>Overall Health</b>	<b>Total Program Services</b>	<b>Total Management and General</b>	<b>Total</b>
Grant and grant related activities	\$ 1,634,625	\$ 21,829,130	\$ -	\$ 6,055,436	\$2,286,784	\$31,805,975	\$ -	\$ 31,805,975
Compensation and benefits	199,217	498,615	81,467	365,666	4,064	1,149,029	1,447,575	2,596,604
Professional and contractual services	12,543	46,032	22,080	38,389	17,877	136,921	654,574	791,495
Depreciation and amortization	3,804	439,002	6,697	11,644	5,422	466,569	198,536	665,105
Interest expense	-	134,754	-	-	-	134,754	-	134,754
Other expenses	16,146	220,790	28,422	49,416	23,012	337,786	842,594	1,180,380
	<u>\$ 1,866,335</u>	<u>\$ 23,168,323</u>	<u>\$ 138,666</u>	<u>\$ 6,520,551</u>	<u>\$2,337,159</u>	<u>\$34,031,034</u>	<u>\$ 3,143,279</u>	<u>\$ 37,174,313</u>

**Kansas Health Foundation**  
**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2018 and 2017**

	<b>2018</b>	<b>2017</b>
<b>Operating Activities</b>		
Increase (Decrease) in net assets	\$ (45,777,042)	\$ 29,179,572
Items not requiring (providing) cash		
Depreciation and amortization	578,123	665,105
Net realized and unrealized losses (gains) on investments	29,230,416	(64,681,197)
Changes in		
Other assets	(153,463)	929
Accounts payable	134,805	(259,807)
Grants payable	(7,111,298)	12,256,696
Accrued expenses	16,848	(11,344)
Net cash used in operating activities	(23,081,611)	(22,850,046)
<b>Investing Activities</b>		
Additions to property and equipment	(1,729,405)	(164,990)
Proceeds from sale of investments	87,266,642	60,738,275
Purchase of investments	(67,309,235)	(46,890,025)
Net cash provided by investing activities	18,228,002	13,683,260
<b>Financing Activities</b>		
Repayment of bonds payable	-	(6,051,002)
Net cash used in financing activities	-	(6,051,002)
<b>Decrease in Cash and Cash Equivalents</b>	(4,853,609)	(15,217,788)
<b>Cash and Cash Equivalents, Beginning of Year</b>	15,829,044	31,046,832
<b>Cash and Cash Equivalents, End of Year</b>	\$ 10,975,435	\$ 15,829,044
<b>Supplemental Cash Flows Information</b>		
Construction costs payable included in property and equipment	\$ 561,612	\$ -



**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2018 and 2017**

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

***Nature of Operations***

The mission of the Kansas Health Foundation is to improve the health of all Kansans. To accomplish its mission, the Kansas Health Foundation focuses the majority of its grant making and direct charitable activities in the following areas: promoting the healthy behaviors of Kansans; strengthening the public health system; growing community philanthropy; providing health data and information to policymakers; and building civic leadership.

The Foundation was previously classified as a private foundation. On November 23, 2014, the IRS approved the Foundation's request to be classified as a public charity, effective January 1, 2015, for an advance ruling period which ends December 31, 2019. Management believes that the Foundation's normal activities over the 60-month period will allow the IRS to issue a permanent "public charity" ruling in 2020.

KHF Fund, LP, a limited partnership, was formed on November 4, 2015, and commenced operations on January 1, 2016. The Kansas Health Foundation has a 99.9993% limited partnership interest in KHF Fund. Cambridge Associates Resources, LLC serves as general partner with a .0007% interest and Cambridge Associates, LLC serves as the investment manager of KHF Fund. The KHF Fund serves as an investment vehicle for the Kansas Health Foundation with investment decisions made in accordance with investment guidelines and approval required by the Kansas Health Foundation.

***Principles of Consolidation***

The consolidated financial statements include the accounts of the Kansas Health Foundation and the KHF Fund (collectively referred to as the "Foundation"). The KHF Fund is consolidated as the Kansas Health Foundation has a controlling financial interest in the KHF Fund. All inter-organizational transactions have been eliminated in consolidation.

***Basis of Accounting***

The accompanying consolidated financial statements are prepared on the accrual basis of accounting. Revenue is recognized when earned and expenses are recognized upon receipt of goods or services.

**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2018 and 2017**

***Use of Estimates***

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

***Cash Equivalents***

Cash equivalents include short-term investments with original maturities of three months or less. Cash equivalents of \$9.6 million and \$13.8 million, as of December 31, 2018 and 2017, respectively, are invested in an institutional U.S. government securities money market fund.

At December 31, 2018, the Foundation's cash accounts exceeded federally insured limits by approximately \$1,073,000.

***Investments and Net Investment Return***

The Foundation measures securities, other than investments that qualify for the equity method of accounting, at fair value. Investments in commingled funds, trusts, and limited partnerships are recorded at net asset value (NAV), as a practical expedient, to determine fair value of the investments.

Investment return includes dividend, interest and other investment income; realized and unrealized gains and losses on investments carried at fair value; and realized gains and losses on other investments, less external and direct internal investment expenses.

***Property and Equipment***

Property and equipment acquisitions are stated at cost, less accumulated depreciation. Depreciation is charged to expense on the straight-line basis over the estimated useful life of each asset.

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

Building and improvements	3-40 years
Equipment, furniture and fixtures	3-10 years

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**Notes to Consolidated Financial Statements**  
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***Long-lived Asset Impairment***

The Foundation evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

No asset impairment was recognized during the years ended December 31, 2018 and 2017.

***Income Taxes***

The Foundation is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and a similar provision of state law. It is classified as a public charity described in Code section 509(a)(3) under a determination letter received from the Internal Revenue Service (IRS) dated November 23, 2014. However, the Foundation is subject to federal income tax on any unrelated business taxable income. The Foundation files tax returns in the U.S. federal jurisdiction.

As of December 31, 2018 and 2017, the Foundation had a federal cumulative net operating loss carry-forward of approximately \$1,393,706 and \$1,473,793, respectively, which was available to offset future taxable income.

No provision for federal income taxes is recorded in the accompanying consolidated financial statements. In accordance with U.S. generally accepted accounting principles, the Foundation recognizes the income tax benefits, if any, of uncertain tax positions only when the position is “more likely than not” to be sustained assuming examination by federal taxing authorities. Management has analyzed the Foundation’s tax positions taken on federal income tax returns subject to possible examination by federal taxing authorities (years ended December 31, 2015 through 2018) and concluded the Foundation did not require a provision for any uncertain tax positions as of December 31, 2018 and 2017.

***Grants and Grant Related Activities***

Grants and grant related activities are recorded in the accompanying consolidated financial statements when the Foundation has an obligation to transfer assets to a grantee, normally when a grant contract is executed. Grants are recorded based on the present value of estimated future cash flows, discounted at an average annual market rate of interest in the year of approval.

**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
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***Functional Allocation of Expenses***

The costs of supporting the various programs and other activities have been summarized on a functional basis in the statements of activities. The statements of functional expenses present the natural classification detail of expenses by function. Grants and grant related activities, net are allocated solely to program services. Operating expenses, other than compensation and benefits, are allocated to the program services, management and general categories benefited based on square footage. Compensation and benefits are allocated based on estimates of time and effort. There were no fund raising costs during the years ended December 31, 2018 and 2017.

***Change in Accounting Principle***

On January 1, 2018, the Foundation adopted the Financial Accounting Standards Board Accounting Standards Update 2016-14, *Not-For-Profit Entities (Topic 958): Presentation of Financial Statements of Not-For-Profit Entities*. A summary of the changes is as follows:

***Statement of Activities***

- Investment income (loss) is shown net of external and direct internal investment expenses. Disclosure of the expenses netted against investment income is no longer required.
- Direct internal investment expenses, including compensation for employees, related to the development and execution of investment strategy are included in investment income (loss).

***Statement of Functional Expenses***

- Expenses are reported by both nature and function in one location.

***Notes to the Financial Statements***

- Enhanced quantitative and qualitative disclosures provide additional information useful in assessing liquidity and cash flows available to meet operating expenses for one-year from the date of the Consolidated Statement of Financial Position.
- Amounts and purposes of Governing Board designations and appropriations as of the end of the year are disclosed.

This change had no impact on previously reported total change in net assets.

**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2018 and 2017**

**Note 2: Investments**

***Objective***

The Foundation's long-term financial objectives are to preserve and enhance the inflation adjusted value of its assets in perpetuity and provide a relatively stable stream of earnings consistent with spending needs. These financial objectives are intended to balance the needs of current and future generations of the Foundation's beneficiaries. The Foundation's primary long-term absolute investment objective is to earn an average annual inflation adjusted total return of at least 5%, net of all investment management fees, operating expenses and taxes over long-term periods.

***Composition of Investments***

Investments presented in the accompanying consolidated financial statements are comprised of the following:

	<u>2018</u>	<u>2017</u>
U.S. equities and commingled funds	\$ 60,095,546	\$ 84,576,350
International equities and commingled funds	102,323,330	146,910,870
Marketable alternative equities	133,865,180	127,562,520
Real estate investment trust	6,141,800	7,434,863
Non-marketable investments:		
Real estate and natural resources funds	34,459,773	38,824,553
Private equity funds	15,289,946	14,012,807
Venture capital funds	31,329,398	27,978,798
Fixed income commingled funds	<u>42,292,815</u>	<u>40,917,933</u>
	<u>\$ 425,797,788</u>	<u>\$ 488,218,694</u>

***Fair Value Measurements***

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

**Level 1** Quoted prices in active markets for identical assets or liabilities

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**Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

**Level 3** Unobservable inputs supported by little or no market activity and that are significant to the fair value of the assets or liabilities

***Recurring Measurements***

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying statements of financial position measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2018 and 2017:

	<b>2018</b>			<b>Total</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
U.S. equities	\$ 26,077,060	\$ -	\$ -	\$ 26,077,060
Marketable alternative equities	12,341,233	-	4,742,988	17,084,221
Non-marketable investments:				
Real estate and natural resource funds	-	-	8,839,631	8,839,631
Fixed income commingled funds	12,721,484	-	-	12,721,484
Total investments in the fair value hierarchy	<u>\$ 51,139,777</u>	<u>\$ -</u>	<u>\$ 13,582,619</u>	64,722,396
Investments measured at net asset value (A)				<u>361,075,392</u>
Total investments at fair value				<u>\$425,797,788</u>
	<b>2017</b>			<b>Total</b>
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
U.S. equities	\$ 39,995,522	\$ -	\$ -	\$ 39,995,522
Marketable alternative equities	11,157,923	-	-	11,157,923
Non-marketable investments:				
Real estate and natural resource funds	-	-	8,891,621	8,891,621
Fixed income commingled funds	14,300,530	-	-	14,300,530
Total investments in the fair value hierarchy	<u>\$ 65,453,975</u>	<u>\$ -</u>	<u>\$ 8,891,621</u>	74,345,596
Investments measured at net asset value (A)				<u>413,873,098</u>
Total investments at fair value				<u>\$488,218,694</u>

**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
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- (A) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts included above are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the Consolidated Statements of Financial Position.

Following is a description of the valuation methodologies and inputs used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying Consolidated Statements of Financial Position, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2018. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

***Investments***

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

**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
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**Alternative Investments**

Investments in certain entities measured at fair value using the net asset value per share as a practical expedient, Level 2 and 3 consist of the following (all \$ amounts in millions):

	December 31, 2018					
	Fair Value	Unfunded Commit- ments	Expected Liquidation Term	Redemption Terms	Redemption Restrictions	Redemption Restrictions
U.S. equity commingled funds (a)	<u>\$ 34.0</u>	N/A	N/A	daily to quarterly 1-60 days notice	N/A	N/A
International equity commingled funds (a)	<u>\$ 102.3</u>	N/A	N/A	daily to 36 mos 1-90 days notice	1 fund has exit frequency greater than 12 mos	1 fund has gate restrictions of 50% (f)
Marketable alternative equities (b)	<u>\$ 121.6</u>	<u>\$ 12.5</u>	<1-14 years	daily to 36 mos 1-93 days notice	1 fund has exit frequency greater than 12 mos; 13 funds not redeemable until underlying funds are liquidated; 1 fund has a 24 month lockup that expires January 31, 2020	Investor level quarterly gate restrictions of 12.5% to 25%; fund level gate restrictions of 10% to 20% (f)
Real estate investment trusts (c)	<u>\$ 6.1</u>	N/A	N/A	monthly, 16 days notice	N/A	N/A
Non-marketable investments (d)						
Real estate/natural resources funds	\$ 34.5	\$ 10.9	1-12 years	N/A*	N/A*	N/A*
Private equity funds	15.3	9.4	1-15 years	N/A*	N/A*	N/A*
Venture capital funds	31.3	6.0	1-15 years	N/A*	N/A*	N/A*
Total non-marketable investments	<u>\$ 81.1</u>	<u>\$ 26.3</u>				
Fixed income commingled fund (e)	<u>\$ 29.6</u>	N/A	N/A	daily, 15 days notice	N/A	N/A



**Kansas Health Foundation**  
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	December 31, 2017					
	Fair Value	Unfunded Commit- ments	Expected Liquidation Term	Redemption Terms	Redemption Restrictions	Redemption Restrictions
U.S. equity commingled funds (a)	<u>\$ 44.6</u>	N/A	N/A	daily to quarterly 15-60 days notice	N/A	1 fund has 20% fund level gate restriction (f)
International equity commingled funds (a)	<u>\$ 146.9</u>	N/A	N/A	daily to 36 mos 1-90 days notice	1 fund has exit frequency greater than 12 mos	fund level gate restrictions of 25-50% (f)
Marketable alternative equities (b)	<u>\$ 116.4</u>	<u>\$ 9.6</u>	<1-10 years	daily to 36 mos 1-90 days notice	1 fund has exit frequency greater than 12 mos; 11 funds not redeemable until underlying funds are liquidated; 1 fund has a 12 month lockup that expired August 1, 2018	Investor level quarterly gate restrictions of 12.5% to 25%; fund level gate restrictions of 10% to 20% (f)
Real estate investment trusts (c)	<u>\$ 7.4</u>	N/A	N/A	monthly, 16 days notice	N/A	N/A
Non-marketable investments (d)						
Real estate/natural resources funds	\$ 38.8	\$ 13.4	1-13 years	N/A*	N/A*	N/A*
Private equity funds	14.0	11.8	1-10 years	N/A*	N/A*	N/A*
Venture capital funds	28.0	5.2	1-11 years	N/A*	N/A*	N/A*
Total non-marketable investments	<u>\$ 80.8</u>	<u>\$ 30.4</u>				
Fixed income commingled fund (e)	<u>\$ 26.6</u>	N/A	N/A	daily, 15 days notice	N/A	N/A

\* These investments are in private funds which may not be redeemed.

**Kansas Health Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2018 and 2017**

- (a) U.S. and international equities and commingled funds include an S&P 500 ex-tobacco index fund, an actively managed U.S. equity long/short fund, an actively managed domestic equity fund, a mutual fund, domestic publicly traded securities, and ten actively managed global/international equity funds. The underlying assets of all these funds are marketable equity securities. The fair value of these commingled investments is estimated using the NAV of the Foundation's ownership interest in each fund.
- (b) Marketable alternative equities include diversifier and long/short hedge funds, opportunistic global long-only funds, and energy and commodities funds. Diversifier hedge funds include macro, event arbitrage and distressed securities strategies that seek to diversify risk and reduce portfolio volatility. Managers of these funds have significant discretion to allocate resources among several strategies including event arbitrage, convertible bond arbitrage, special situations and distressed securities. Managers may have the flexibility to use limited leverage and to implement strategies on a U.S. or global basis. Long/short hedge fund managers have the flexibility to trade securities both long and short, to use limited leverage and to invest in either U.S. or global markets.

The Foundation uses a "fund of funds" approach to investing in hedge funds. The fair value of investments in both diversifier and long/short hedge funds have been estimated based on the NAV of the underlying hedge funds as reported to the "fund of funds" administrator.

Two alternative funds invest in global long-only equities, using highly concentrated and unconstrained investment strategies. The underlying assets of these funds are marketable equity securities. The fair value of these commingled investments is estimated using the NAV of the Foundation's ownership interest in each fund.

Energy and commodities funds include a commingled energy fund and a commingled commodities fund. The underlying assets of the energy fund are marketable securities. The commodities funds invest in energy, precious metals and consumer staples futures contracts. The fair value of these commingled investments is estimated using the NAV of the Foundation's ownership interest in each fund.

- (c) The global real estate investment trust (REIT) is an actively managed commingled fund which invests in publicly traded REIT securities. The fair value of the fund is estimated using the NAV of the Foundation's ownership interest in the trust.
- (d) Non-marketable investments include real estate/natural resources funds, private equity funds, and venture capital funds. Real estate/natural resources funds include investments in global private real estate and natural resources funds. Real estate investments include U.S. and global commercial and residential investments in land and rental property. Global natural resources investments include timber, farmland and energy investments such as oil and natural gas exploration and production, and mineral and wind royalty interests. Private equity funds include investments in funds of funds, which invest in limited partnerships, which in turn invest in U.S. and global privately held companies in such industries as consumer goods, electronics, communications, health care and medical devices. Venture capital funds include investments in funds of funds, which invest in limited partnerships, which in turn invest in primarily U.S. based new companies, often focusing on technological innovation.

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The fair value of non-marketable investments is estimated using the NAV of the Foundation's ownership interest in the fund of funds capital. These investments can never be redeemed. Instead, distributions are received from liquidation of the underlying assets of the fund of funds. The Foundation may sell its interests in non-marketable fund of funds in a secondary market, but as of December 31, 2018, it had no plans to sell any non-marketable investments before they were liquidated. Since December 31, 2018, the Foundation has not funded any new capital calls on non-marketable investments.

- (e) The commingled, fixed income fund invests in index funds, which in turn invest in U.S. Treasury and agency intermediate maturity bonds. The fair value is estimated using the NAV of the Foundation's ownership interest in the fund.
- (f) Liquidity of certain investments vary based on various factors and may include "gates," "holdbacks" and "side pockets" imposed by the manager of the funds, as well as redemption fees which may also apply. These investments may provide the manager with the ability to suspend or postpone redemption (a "gate") or "holdback" from the payment of redemption proceeds a portion of the redemption (*e.g.* 10%) until the annual audited financial statements are distributed. A side pocket is a type of account utilized by hedge fund managers to differentiate illiquid, hard to value assets from liquid assets.

***Level 3 Valuation Process and Activity***

Fair value determinations for Level 3 measurements of securities are the responsibility of Foundation management. Management contracts with a pricing specialist to generate fair value estimates on a monthly or quarterly basis. Management challenges the reasonableness of the assumptions used and reviews the methodology to ensure the estimated fair value complies with accounting standards generally accepted in the United States.

Purchases for Level 3 investments approximated \$5.0 million and \$0 for the years ended December 31, 2018 and 2017, respectively. There were no sales, transfers in or transfers out of Level 3 investments.

***Unobservable (Level 3) Inputs***

The fair value of the Foundation's investment in two limited partnerships which invest in natural gas and oil royalty and mineral interests and one limited liability company is calculated using the income approach and estimating the present value of future net cash flows and resulting distributions. Significant accounting estimates in determining fair value include the calculation of cost depletion which require assumptions and estimates with respect to future production.

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**Note 3: Due from Underlying Funds**

Due from underlying funds includes receivables from sales pending settlement. Purchases and sales of investments are accounted for on a trade date basis. Due from underlying funds equals \$13,844,959 and \$664,015 at December 31, 2018 and 2017, respectively.

**Note 4: Property and Equipment**

Property and equipment at December 31, 2018 and 2017, consists of:

	<u>2018</u>	<u>2017</u>
Land	\$ 953,428	\$ 953,428
Building and improvements	13,431,121	13,384,709
Equipment, furniture and fixtures	<u>3,109,509</u>	<u>3,067,846</u>
	17,494,058	17,405,983
Less accumulated depreciation	<u>(6,235,485)</u>	<u>(5,956,028)</u>
Property and equipment, net	<u><u>\$ 11,258,573</u></u>	<u><u>\$ 11,449,955</u></u>

**Note 5: Grants Payable and Grants and Grant Related Activities**

Grants and grant related activities are recorded on a discounted present value basis. At December 31, 2018 and 2017, the grant contracts and discount were as follows:

	<u>2018</u>	<u>2017</u>
Grant contracts	\$ 23,756,014	\$ 31,554,890
Discount to present value	<u>(903,160)</u>	<u>(1,590,738)</u>
Grants payable	<u><u>\$ 22,852,854</u></u>	<u><u>\$ 29,964,152</u></u>

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In addition to grants payable recorded in the consolidated financial statements, the Foundation’s Board of Directors has authorized future funding for grants in certain program areas. These authorized grants are not recorded as grants payable and grants and grant related activities in the consolidated financial statements, since grant contracts have not been executed. Management’s best estimate of when the total of grant contracts and authorized grants as of December 31, 2018, will be paid is as follows:

	<b>Grant Contracts</b>	<b>Authorized Grants</b>
2019	\$ 12,154,166	\$ 3,909,070
2020	7,035,430	3,314,229
2021	2,014,925	2,865,398
2022	147,187	159,656
2023 and future years	134,264	3,524,223
	21,485,972	\$ 13,772,576
Amortization of Kansas Leadership Center’s leased building	2,270,042	
Grants payable	\$ 23,756,014	

During 2018 and 2017, the Foundation paid \$2,700,000 and \$2,639,853, respectively, for core operations of the Kansas Health Institute (KHI), a non-profit, tax-exempt corporation located in Topeka, Kansas. KHI was created by the Foundation in 1994 as a health policy and research institute for Kansas.

During 2018 and 2017, the Foundation paid \$3,000,000 and \$700,474, respectively, for operations of a separate non-profit, tax-exempt corporation, the Kansas Leadership Center (KLC). Included in December 31, 2018, grant contracts is \$6 million to be paid from 2019 – 2020 (\$3 million per year) for core operations of KLC. KLC was created by the Foundation in 2006. KLC’s mission is to strengthen and expand civic leadership across Kansas.

Approximately 24,000 square feet of an addition to the Foundation’s office building have been leased to KLC at a below market rate. The original lease commenced on August 1, 2013, and was renewed on August 1, 2017. Based on an independent appraisal of the leased premises, the Foundation recorded a grant liability and expense in 2017 of \$3,167,500 representing the fair value lease rate per square foot over a five-year lease term. The grant liability is being amortized monthly on the straight-line basis over the lease term. The grant liability was reduced by \$633,500 and \$626,792 in 2018 and 2017, respectively, and the same amount was recognized as “other income” in the Consolidated Statement of Activities. In future years, the grant liability will be reduced annually by \$633,500, and the same amount will be recognized as “other income” in the Consolidated Statement of Activities. The remaining grant liability balance is \$2,270,042 at December 31, 2018.

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Grants and grant related activities in the accompanying Consolidated Statements of Activities are reported net of grant contracts written off.

The authorized grants are designated by the board for the following program areas:

	<u>2018</u>	<u>2017</u>
Access to care	\$ 73,087	\$ 73,087
Civic and community engagement	12,084,588	9,322,496
Healthy behaviors	1,491,020	2,069,645
Overall health	<u>123,881</u>	<u>736,983</u>
	<u>\$ 13,772,576</u>	<u>\$ 12,202,211</u>

**Note 6: Information Regarding Liquidity and Availability**

The Foundation strives to maintain liquid financial assets sufficient to cover six months of general expenditures. Financial assets in excess of daily cash requirements are invested in short-term investments, bonds, equities, and alternative investments.

The following table reflects the Foundation's financial assets as of December 31, 2018 and 2017, reduced by amounts that are not available to meet general expenditures within one year of the statement of financial position date because of contractual restrictions or internal board designations. Amounts not available include certain alternative investments with redemption limitations as more fully described in *Note 2*, contracted grants, and board-designated initiatives not considered in the annual operating budget. In the event the need arises to use the board-designated funds for liquidity purposes, the reserves could be drawn upon through board resolution. There were no net assets with donor restrictions at December 31, 2018 and 2017.

	<u>2018</u>	<u>2017</u>
Cash and cash equivalents	\$ 10,975,435	\$ 15,829,044
Investments	425,797,788	488,218,694
Due from underlying funds	<u>13,844,959</u>	<u>664,015</u>
	450,618,182	504,711,753
Investments with liquidity horizons greater than one year	(132,588,539)	(137,205,760)
Board designated funding for certain program areas	<u>(3,909,070)</u>	<u>(882,384)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 314,120,573</u>	<u>\$ 366,623,609</u>

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**Note 7: Bonds Payable and Building Addition**

On October 5, 2012, the City of Wichita (City) agreed to issue up to \$7 million in tax exempt revenue bonds to assist the Foundation in financing approximately 80% of the construction costs of a 36,000 square foot addition to its office completed in 2013. The addition served as the new state-wide headquarters for KLC and as a conference center for the Foundation. During construction, the bonds were issued as needed and purchased in a private placement. The City held title to the addition as collateral for the bonds and leased the addition to the Foundation. The bonds were originally scheduled to mature and the lease expire on July 1, 2033. The bonds bore interest payable at an annual rate of 2.73%. Principal and interest payments began on August 1, 2013, and made in equal monthly installments of \$37,833 through August 31, 2017.

On September 30, 2017, management decided to exercise an option to purchase the addition by providing funds to the bond trustee to retire the bonds. Management retired bond debt of \$5,844,868 on September 30, 2017, and wrote-off the remaining unamortized bond issuance costs of \$76,322 which are included in “depreciation and amortization” in the 2017 Consolidated Statement of Activities.

**Note 8: Land Lease**

The Foundation, as lessor, has leased certain land (cost of \$366,155) under a long-term operating lease which expires in 2081. Future rentals to be received under the lease are as follows:

2019	\$ 107,140
2020	107,140
2021	107,140
2022	107,140
2023	107,140
2024 - 2081	<u>6,205,848</u>
	<u>\$ 6,741,548</u>

**Note 9: Employees’ Retirement Plans**

The Foundation provides retirement benefits to its employees through two defined contribution pension plans. All employees are eligible to participate in the plans immediately on employment. The Foundation contributed \$267,935 and \$269,904 to the plans in 2018 and 2017, respectively. The Foundation’s policy is to fund pension costs as accrued and no prior service costs exist under the plans. Employees may contribute additional amounts to the plans. Employer and employee contributions are fully vested.

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**Note 10: Significant Estimates and Concentrations**

***Investments***

The Foundation invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the accompanying Consolidated Statements of Financial Position.

**Note 11: Subsequent Events**

Subsequent events have been evaluated through October 10, 2019, which is the date the financial statements were available to be issued.