UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION
(With Management's Discussion and Analysis)

JUNE 30, 2018 AND 2017

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

CONTENTS

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and analysis provides an overview of the consolidated financial position and activities of the University of Connecticut Health Center Finance Corporation and Subsidiaries (Finance Corporation) as of and for the years ended June 30, 2018, 2017, and 2016. This discussion has been prepared by management and should be read in conjunction with the consolidated financial statements and the notes thereto, which follow this section.

FINANCIAL HIGHLIGHTS

The Finance Corporation's financial position at June 30, 2018, 2017, and 2016, included assets of $221.6 million, $225.3 million and $240.6 million, respectively, and liabilities of $205.4 million, $211.6 million and $229.3 million, respectively. The value of both the assets and liabilities is attributable mainly to the Finance Corporation maintaining the real estate and related financing on the UConn Musculoskeletal Institute formerly known as the Medical Arts and Research Building (MARB), 16 Munson Road (Munson Road), and the Outpatient Pavilion (OP). Changes in net position represent the operating activity of the Finance Corporation, primarily composed of revenues and expenses related to the UConn Musculoskeletal Institute, Munson Road and OP properties and are summarized below for the years ended June 30, 2018, 2017, and 2016:

	2018	2017	2016
	(In thousands)		
Summary of assets and liabilities at June 30:			
Current assets	$ 6,233	$ 6,918	$ 21,557
Net investment in direct financing lease, net of current portion	189,121	191,395	191,287
Capital assets, net	26,216	26,969	27,723
Total assets	$ 221,570	$ 225,282	$ 240,567
Current liabilities	$ 10,234	$ 10,054	$ 15,367
Long-term liabilities	195,156	201,566	213,950
Total liabilities	$ 205,390	$ 211,620	$ 229,317
Net investment in capital assets	$ 19,923	$ 18,560	$ 19,352
Unrestricted deficit	(3,743)	(4,898)	(8,102)
Total net position	16,180	13,662	11,250
Total liabilities and net position	$ 221,570	$ 225,282	$ 240,567

FINANCIAL HIGHLIGHTS (CONTINUED)

	2018	2017	2016
		(In thousands)	
Summary of revenues, expenses, and nonoperating expenses for the year ended June 30:			
Operating revenues	$ 13,248	$ 13,398	$ 14,864
Operating expenses	(10,719)	(10,975)	(11,370)
Nonoperating expenses	(11)	(11)	(11)
Increase in net position	$ 2,518	$ 2,412	$ 3,483

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of management's discussion and analysis and the consolidated financial statements. The basic financial statements (consolidated statements of net position, consolidated statements of revenues, expenses, and changes in net position, and consolidated statements of cash flows) present the financial position of the Finance Corporation at June 30, 2018 and 2017, and the results of its operations and financial activities for the years then ended. These statements report information about the Finance Corporation using accounting methods similar to those used by private-sector companies. The consolidated statements of net position include all of the Finance Corporation's assets and liabilities. The consolidated statements of revenues, expenses, and changes in net position reflect the years' activities on the accrual basis of accounting, i.e., when services are provided or obligations are incurred, not necessarily when cash is received or paid. These consolidated statements report the Finance Corporation's net position and how it has changed. Net position (the difference between assets and liabilities) is one way to measure financial health or position. The consolidated statements of cash flows provide relevant information about each year's cash receipts and cash payments and classify them as to operating, investing, and capital and related financing activities. The consolidated financial statements include notes that explain information in the consolidated financial statements and also provide more detailed data.

CAPITAL AND DEBT RELATED ACTIVITIES

In fiscal year 2018, the Finance Corporation continued the financing of the OP through the mortgage with Teachers Insurance and Annuity Association of America (TIAA) and its facilitator, Wells Fargo. At the end of fiscal year 2018, construction of the main building and garage was substantially complete. The project finished ahead of budget and UCHCFC Circle Road Corporation (Circle Road Corporation) is in the process of closing out the additional funds held in trust to be used for additional site work and minor improvements.

CAPITAL AND DEBT RELATED ACTIVITIES (CONTINUED)

The TIAA mortgage for the OP is supported by a 25 year fixed term lease between University of Connecticut Health Center (UConn Health) and the Finance Corporation. As a result, capital assets associated with the OP have been reclassified and reported as investment in direct financing lease. For additional information on capital assets and the breakout of the OP's underlying assets please see notes 3 and 6.

The Finance Corporation continues to rent the OP to UConn Health which in turn subleases the space to related parties. Lease payments from UConn Health provide the funding for the Finance Corporation's OP mortgage payments. For the years ended June 30, 2018 and 2017, the Finance Corporation made all regularly scheduled payments on the mortgage thereby reducing the principal amount of secured mortgage on the OP by $4,793,230 and $4,568,617, respectively. For additional information on debt related activities please see note 4.

The Finance Corporation continues to own and rent the UConn Musculoskeletal Institute property to UConn Health. For the years ended June 30, 2018 and 2017, the Finance Corporation made all regularly scheduled payments on the UConn Musculoskeletal Institute's secured mortgage thereby reducing the amount of secured mortgage principal debt on the UConn Musculoskeletal Institute by $1,297,429 and $1,217,928, respectively. There is no outstanding debt on the Munson Road property. The rent charge for the Munson Road property was discontinued in fiscal year 2017.

SUBSIDIARIES

The Finance Corporation is currently the sole member and parent to the Circle Road Corporation. Circle Road Corporation's primary purpose is to serve as the financing vehicle for the OP. Circle Road Corporation is a 501(c) 3 entity.

During fiscal year 2018, the Finance Corporation created a wholly-owned subsidiary corporation, UConn Health Pharmacy Services, Inc. (Pharmacy Services Corporation) which is a Connecticut non-stock corporation that operates within the meaning of Section 115 of the Internal Revenue Code. The Pharmacy Services Corporation provides pharmacy services to the State of Connecticut's Department of Corrections under a renewable, 6 month contract which became effective during fiscal year 2019.

RELATED PARTIES

During fiscal years 2018 and 2017, the Finance Corporation repaid amounts to related entities in the amount of $-0- and $9,995,498, respectively. During fiscal year 2018, the Finance Corporation incurred operating expenses on behalf of Central Administrative Services (CAS) in the amount of $692,406. This amount was offset by operating and investing amounts charged by CAS in the amount of $23,227. In fiscal year 2017, the Finance Corporation received charges for operating and

RELATED PARTIES (CONTINUED)

investing from CAS in the amount of $22,693. These amounts are reflected in operating and financing activities on the consolidated statements of cash flows. For additional information on related parties, see note 5.

FISCAL YEAR 2019 OUTLOOK

The Finance Corporation was created by statute in recognition of UConn Health's need to implement decisions rapidly in order to provide excellent care in a competitive health care environment with a special focus on the need for rapid and expedited processes in the areas of purchasing, leasing, construction, and through joint ventures with other organizations.

The Finance Corporation assists UConn Health by facilitating the acquisition of clinical space. The Finance Corporation has previously served as the vehicle to acquire both the UConn Musculoskeletal Institute and Munson Road properties and is the owner of the OP. The Finance Corporation will continue to serve as owner/leaseholder of these properties in 2019.

The Pharmacy Services Corporation will be providing pharmacy services to the State of Connecticut's Department of Corrections under a renewable, 6 month contract.

The economic position of the Finance Corporation is closely tied to that of UConn Health's clinical entities serviced by the Finance Corporation. Through various rental agreements, UConn Health provides funding which enables the Finance Corporation to make its required debt and principal payments.

The Finance Corporation also provides UConn Health with contracting efficiency and flexibility that is important to meeting the demands of modern healthcare. These services are an integral part of UConn Health operations.

On October 22, 2018, UConn Health published a Solicitation of Interest seeking potential partners for UConn Medical Group and John Dempsey Hospital (the "Clinical Group"). Although not part of the Clinical Group as defined by the Solicitation of Interest, changes to the Clinical Group could impact the operations of the Finance Corporation.

If you have questions about this report or need additional financial information, please contact the Office of the Chief Financial Officer, University of Connecticut Health Center, Farmington, Connecticut 06030-3800.

MARCUM
ACCOUNTANTS ▲ ADVISORS

INDEPENDENT AUDITORS' REPORT

Joint Audit and Compliance Committee
University of Connecticut Health Center

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of the University of Connecticut Health Center Finance Corporation (Finance Corporation or Company), a component unit of the State of Connecticut, as of and for the years ended June 30, 2018 and 2017, and the related notes to the consolidated financial statements, which collectively comprise Finance Corporation's basic consolidated 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 accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the University of Connecticut Health Center Finance Corporation as of June 30, 2018 and 2017, and the consolidated results of their operations and changes in net position, and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the required supplementary information, such as Management's Discussion and Analysis on pages 1 through 4, 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 audits 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 Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the University of Connecticut Health Center Finance Corporation's basic financial statements. The consolidating information in Schedules I and II is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The consolidating information in Schedules I and II is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the 2018 consolidating information in Schedules I and II is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 30, 2018 on our consideration of the Company'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 Company'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 Company's internal control over financial reporting and compliance.

Marcum LLP

Hartford, CT
November 30, 2018

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

CONSOLIDATED STATEMENTS OF NET POSITION

JUNE 30, 2018 AND 2017

	2018	2017
Assets		
Current Assets		
Cash	$ 1,447,727	$ 303,607
Malpractice fund	608,177	1,273,817
Construction escrow account	529,145	2,479,424
Due from Central Administrative Services	619,086	--
Net investment in direct financing lease, current portion	3,028,588	2,860,567
Total Current Assets	6,232,723	6,917,415
Noncurrent Assets		
Net investment in direct financing lease, net of current portion	189,121,092	191,395,214
Capital assets, net	26,215,912	26,969,211
Total Noncurrent Assets	215,337,004	218,364,425
Total Assets	$ 221,569,727	$ 225,281,840

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF CONNECTICUT HEALTH CENTER
FINANCE CORPORATION

CONSOLIDATED STATEMENTS OF NET POSITION (CONTINUED)

JUNE 30, 2018 AND 2017

	2018	2017
Liabilities and Net Position		
Current Liabilities		
Accounts payable and accrued expenses	$ 1,199,827	$ 623,606
Due to UConn Health - Malpractice fund	608,177	1,273,817
Due to Central Administrative Services	--	50,091
Due to John Dempsey Hospital, current portion	2,000,000	2,000,000
Advances for construction	6,619	6,619
Security deposits	8,279	8,279
Loans payable, current portion	6,411,004	6,090,659
Total Current Liabilities	10,233,906	10,053,071
Noncurrent Liabilities		
Due to John Dempsey Hospital, net of current portion	2,743,408	2,743,408
Loans payable, net of current portion	192,412,033	198,823,037
Total Noncurrent Liabilities	195,155,441	201,566,445
Total Liabilities	205,389,347	211,619,516
Net Position		
Net investment in capital assets	19,923,363	18,559,952
Unrestricted deficit	(3,742,983)	(4,897,628)
Total Net Position	16,180,380	13,662,324
Total Liabilities and Net Position	$ 221,569,727	$ 225,281,840

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

CONSOLIDATED STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	2018	2017
Operating Revenues		
Rental income	$ 2,132,406	$ 2,123,229
Interest income from direct financing lease	11,115,984	11,274,684
Total Operating Revenues	13,248,390	13,397,913
Operating Expenses		
Professional services	33,475	33,223
Interest expense	9,870,876	10,185,049
Depreciation	753,299	753,300
Other	61,642	3,107
Total Operating Expenses	10,719,292	10,974,679
Operating Income	2,529,098	2,423,234
Nonoperating Expenses		
Loan servicing fees	(11,042)	(11,043)
Total Nonoperating Expenses	(11,042)	(11,043)
Increase in Net Position	2,518,056	2,412,191
Net Position - Beginning	13,662,324	11,250,133
Net Position - End	$ 16,180,380	$ 13,662,324

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF CONNECTICUT HEALTH CENTER
FINANCE CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	2018	2017
Cash Flows from Operating Activities		
Cash paid to suppliers, contractors and others	$ (9,956,179)	$ (10,203,211)
Cash received for rental income	2,132,406	2,123,229
Cash received from related parties	2,350	2,112
Cash paid for administrative expenses	(37,121)	(25,062)
Net Cash Used in Operating Activities	(7,858,544)	(8,102,932)
Cash Flows from Investing Activities		
Payments for purchase of capital assets	(843,344)	(4,749,654)
Net Cash Used in Investing Activities	(843,344)	(4,749,654)
Cash Flows from Capital Financing Activities		
Direct financing lease payments received (including $11,115,984 and $11,274,684 of interest)	13,976,552	13,976,552
Cash returned to John Dempsey Hospital to repay advances in support of Outpatient Pavilion construction	--	(9,995,498)
Cash received from Central Administrative Services in support of Outpatient Pavilion construction	20,878	20,580
Transfers from construction escrow account	1,950,279	7,833,670
Repayments of capital debt	(6,090,659)	(5,786,545)
Loan servicing fees	(11,042)	(11,043)
Net Cash Provided by Capital Financing Activities	9,846,008	6,037,716
Net Increase (Decrease) in Cash	1,144,120	(6,814,870)
Cash - Beginning	303,607	7,118,477
Cash - End	$ 1,447,727	$ 303,607

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

FOR THE YEARS ENDED JUNE 30, 2018 AND 2017

	2018	2017
Reconciliation of Operating Income to Net Cash Used in Operating Activities		
Operating income	$ 2,529,098	$ 2,423,234
Depreciation	753,299	753,300
Direct financing lease interest payments received	(11,115,984)	(11,274,684)
Changes in operating assets and liabilities:		
Due from Central Administrative Services	2,350	2,112
Accounts payable and accrued expenses, excluding payables for capital assets	(27,307)	(6,894)
Net Cash Used In Operating Activities	$ (7,858,544)	$ (8,102,932)
Schedule of Non-Cash Financing Transactions		
Change in mortgage proceeds held by Trustee in construction escrow account	$ 1,950,279	$ 7,833,670

As of June 30, 2018 and 2017, the Finance Corporation had construction invoices payable of $75,246 and $164,120, respectively, that were included in accounts payable, accrued expenses and due to Central Administrative Services.

As of June 30, 2018 and 2017, the Finance Corporation had invoices payable of $692,406 and zero, respectively, included in accounts payable and accrued expenses related to purchases made on behalf of Central Administrative Services that were included in due from Central Administrative Services.

The accompanying notes are an integral part of these consolidated financial statements.

NOTE 1 – DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

REPORTING ENTITY

Effective July 1, 1987, the University of Connecticut Health Center Finance Corporation (the Finance Corporation or Company) was established pursuant to Public Act No. 87-458. The purpose of the Finance Corporation is to provide greater flexibility for John Dempsey Hospital (21002 Fund) (the Hospital), UConn Medical Group, University Dentists, and Correctional Managed Health Care (CMHC) (collectively the entities) and to promote the more efficient provision of health care services. As such, the Finance Corporation has been empowered to purchase supplies and equipment, acquire facilities, approve write-offs of accounts receivable, in addition to negotiate joint ventures, shared service, and other agreements for all of the entities, as well as process malpractice claims on behalf of University of Connecticut Health Center (UConn Health), the Hospital, UConn Medical Group, and University Dentists.

The Finance Corporation is administered by a board of directors currently consisting of the President of the University of Connecticut, the Secretary of the Office of Policy and Management for the State of Connecticut, a member of the Board of Directors of UConn Health, the Executive Vice President for Health Affairs, and the Chairman of the Board of Trustees for the University of Connecticut who is appointed by the Governor of the State of Connecticut or their designee. The Governor appoints one of these members as Chairman of the Board of the Finance Corporation.

The UCHCFC Circle Road Corporation (Circle Road Corporation), a subsidiary of the Finance Corporation, was formed pursuant to Section 10a-254 of the Connecticut General Statutes by the Finance Corporation (its sole member). This subsidiary corporation is administered by a board of directors elected on an annual basis by the sole member's board of directors or appointed by the Governor of the State of Connecticut, as prescribed in the bylaws of Circle Road Corporation. The number of directors shall be not less than three or more than ten, and 50% shall be members of the board of directors of the sole member or appointed by the Governor. At least one of these directors must be an Independent Director. There are four members of the subsidiary corporation's board of directors and five members of the sole member's board of directors.

NOTE 1 – DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

REPORTING ENTITY (CONTINUED)

During fiscal year 2018, Finance Corporation created a wholly-owned subsidiary corporation, UConn Health Pharmacy Services, Inc. (Pharmacy Services Corporation) pursuant to the authority granted by Section 10a-254 of the Connecticut General Statutes. The subsidiary's main focus is the provision of pharmacy operation services on behalf of UConn Health and its clinical units, including the Hospital and UConn Medical Group. The subsidiary has been empowered to apply for and obtain all licenses, certificates or other credentials as required for pharmacy operations and granted the ability to enter into such contracts that are necessary or desirable for, or incidental to, the conduct of the subsidiary's business and affairs.

The sole member of Pharmacy Services Corporation (the Member) is Finance Corporation. The Member has the power to elect and remove directors to/from the Pharmacy Services Corporation's Board of Directors. The property and affairs of the Pharmacy Services Corporation will be managed by or under the direction of the Pharmacy Service Corporation's Board of Directors.

For 2018, the Pharmacy Services Corporation did not commence operations and activity was minimal, therefore, nominal costs of $1,402 were included with Finance Corporation in the consolidating schedules presented in the supplemental information. Pharmacy Services Corporation had no assets, liabilities or net position as of June 30, 2018 and 2017.

The expenses reported in the consolidated statements of revenues, expenses, and changes in net position do not include undetermined amounts for salaries, services, and expenses provided to and received from UConn Health and other Connecticut State agencies.

The Finance Corporation is a component unit of the State of Connecticut and is therefore generally exempt from federal income taxes under Section 115 of the Internal Revenue Code of 1986.

BASIS OF PRESENTATION

The Finance Corporation's consolidated financial statements are prepared in accordance with all relevant Governmental Accounting Standards Board (GASB) pronouncements.

PROPRIETARY FUND ACCOUNTING

The Finance Corporation utilizes the proprietary fund method of accounting whereby revenues and expenses are recognized on the accrual basis.

NOTE 1 – DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 contingencies 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

Cash includes cash held on behalf of the Finance Corporation by the State of Connecticut.

DESCRIPTION OF LEASING ARRANGEMENTS

The Finance Corporation has leasing arrangements with UConn Health for the UConn Musculoskeletal Institute and the Outpatient Pavilion building and associated equipment. The UConn Musculoskeletal Institute is leased under a year to year operating lease. Effective July 1, 2016, rent was no longer charged for the Munson Road property.

The Outpatient Pavilion lease, effected through the Circle Road Corporation, is a direct financing lease for both the Outpatient Pavilion building and associated equipment. Under this treatment, the underlying capital assets are reported as net investment in direct financing lease. The associated equipment will be depreciated over a maximum 10 year life while the building will be depreciated over 40 years. The term of the lease is 25 years as stipulated in the mortgage agreement with Teachers Insurance and Annuity Association of America (TIAA). At the conclusion of the lease, any residual amounts will revert to capital assets, net. The Finance Corporation will review the estimated residual value of property leased under the direct financing lease on an annual basis. See note 6 for additional information.

NOTE 1 – DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

RENTAL INCOME AND INTEREST INCOME

Rental income on operating leases is recognized on a time basis over the rental period by reference to the lease agreements. Interest income on the direct financing lease is recognized over the term of the lease to produce a constant, periodic rate of return on the net investment of the lease. Unearned income related to the direct financing lease is amortized over the lease term using the interest method.

MALPRACTICE FUND

The malpractice fund includes investments held on behalf of UConn Health and is offset by Due to UConn Health on the consolidated statements of net position. The fund is invested in the State of Connecticut Short-Term Investment Fund (STIF). The STIF is an investment pool of high-quality, short-term money market instruments that is considered a "2a7-like" pool which is excluded from the scope of GASB Statement No. 72, *Fair Value Measurement and Application*. The cost of the STIF approximates fair value. The Finance Corporation is responsible for the timely payment of malpractice fund claims. Therefore, it holds an amount estimated to be the current portion due for the malpractice fund liabilities in its account. The claim liability is reflected on UConn Health's financial statements.

CAPITAL ASSETS

Property and equipment acquisitions are recorded at cost. Betterments and major renewals are capitalized, and maintenance and repairs are expensed as incurred.

Depreciation is provided over the estimated useful life of each class of depreciable assets and is computed using the straight-line method. Buildings have an estimated useful life of 17 to 40 years and equipment has an estimated useful life of 2 to 25 years. Assets acquired under capital leases and leasehold improvements are depreciated no longer than the lease term. Construction in progress is capitalized as costs are incurred during the construction phase and depreciation will begin once the assets are placed in service.

NOTE 1 – DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CONSTRUCTION ESCROW ACCOUNT

The construction escrow account represents amounts advanced from TIAA to Wells Fargo Bank Northwest, N.A. (Trustee) for the financing of the Outpatient Pavilion construction project. Such amounts represent cash held by the Trustee that has not yet been drawn down fully by the Finance Corporation for construction expenses. Refer to note 4 for additional information related to the debt.

ADVANCES FOR CONSTRUCTION

Advances for construction in the amount of $6,619 as of June 30, 2018 and 2017, represent the unused portion of bond proceeds that were received in March 1993 by the Finance Corporation which are to be used for the Farm Hollow Building renovations.

NET POSITION

Net position is classified in two components. Net investment in capital assets consists of capital assets net of accumulated depreciation and reduced by the current net balances of any outstanding borrowings (less amounts held in trust) used to finance the purchase or construction of those assets. All other assets less liabilities are classified as unrestricted.

UPCOMING ACCOUNTING PRONOUNCEMENT

In June 2017, GASB issued Statement No. 87, *Leases*. The objective of this Statement is to improve accounting and financial reporting for leases by governments.

Under this Statement, a lessor should recognize a lease receivable and a deferred inflow of resources at the commencement of the lease term, with certain exceptions for leases of assets held as investments, certain regulated leases, short-term leases, and leases that transfer ownership of the underlying asset. A lessor should not derecognize the asset underlying the lease. The lease receivable should be measured at the present value of lease payments expected to be received during the lease term. The deferred inflow of resources should be measured at the value of the lease receivable plus any payments received at or before the commencement of the lease term that relate to future periods.

NOTE 1 – DESCRIPTION OF REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

UPCOMING ACCOUNTING PRONOUNCEMENT (CONTINUED)

A lessor should recognize interest revenue on the lease receivable and an inflow of resources (for example, revenue) from the deferred inflows of resources in a systematic and rational manner over the term of the lease. The notes to financial statements should include a description of leasing arrangements and the total amount of inflows of resources recognized from leases.

The provisions of this Statement are effective for reporting periods beginning after December 15, 2019. The Finance Corporation is currently evaluating the impact this standard will have on its consolidated financial statements.

NOTE 2 – DUE TO RELATED PARTIES

As of June 30, 2018 and 2017, the Finance Corporation had the following amounts due to related parties:

	2018	2017
Due to John Dempsey Hospital	$ (4,743,408)	$ (4,743,408)
Due to UConn Health - Malpractice fund	(608,177)	(1,273,817)
Due from (to) Central Administrative Services	619,086	(50,091)

NOTE 3 – CAPITAL ASSETS

Capital assets as of June 30, 2018 and 2017, consisted of the following:

	2018	2017
Building	$ 29,730,870	$ 29,730,870
Land	6,593,084	6,593,084
Equipment	20,998	20,998
	36,344,952	36,344,952
Less accumulated depreciation	10,129,040	9,375,741
Capital assets, net	$ 26,215,912	$ 26,969,211

As of June 30, 2018, the main building and garage of the Outpatient Pavilion were substantially complete. The remaining balance in the custodial construction escrow account was $529,145 as of June 30, 2018 and will be utilized for additional site work and minor repairs.

As described in note 1, the Outpatient Pavilion is leased to UConn Health under the terms of a direct financing lease. During the year ended June 30, 2018, additional costs were added to the direct financing lease to bring the total costs to $200,879,648. The cumulative costs incurred as of June 30, 2017 were $200,125,181.

Capital assets and depreciation activity for the years ended June 30, 2018 and 2017 was as follows:

	2017	Additions	Deductions	2018
Building	$ 29,730,870	$ --	$ --	$ 29,730,870
Land	6,593,084	--	--	6,593,084
Equipment	20,998	--	--	20,998
Less depreciation - Buildings	(9,354,743)	(753,299)	--	(10,108,042)
Less depreciation - Office equipment	(20,998)	--	--	(20,998)
	$ 26,969,211	$ (753,299)	$ --	$ 26,215,912

NOTE 3 – CAPITAL ASSETS (CONTINUED)

	2016	Additions	Deductions	2017
Building	$ 29,730,870	$ --	$ --	$ 29,730,870
Land	6,593,084	--	--	6,593,084
Equipment	20,998	--	--	20,998
Less depreciation - Buildings	(8,601,443)	(753,300)	--	(9,354,743)
Less depreciation - Office equipment	(20,998)	--	--	(20,998)
	$ 27,722,511	$ (753,300)	$ --	$ 26,969,211

NOTE 4 – NONCURRENT LIABILITIES

The Finance Corporation has a loan agreement with Capital Lease Funding which financed the construction of the UConn Musculoskeletal Institute. The Finance Corporation through its subsidiary, the Circle Road Corporation, has a mortgage with TIAA which financed the construction of the Outpatient Pavilion. Activity related to these loans was as follows:

	June 30, 2017 Balance	Repayments	June 30, 2018 Balance	Amounts due within 1 year
Secured mortgages -				
Capital Lease Funding	$ 11,893,211	$ (1,297,429)	$ 10,595,782	$ 1,382,118
TIAA	193,020,485	(4,793,230)	188,227,255	5,028,886
	$ 204,913,696	$ (6,090,659)	$ 198,823,037	$ 6,411,004

NOTE 4 – NONCURRENT LIABILITIES (CONTINUED)

	June 30, 2016 Balance	Repayments	June 30, 2017 Balance	Amounts due within 1 year
Secured mortgages -				
Capital Lease Funding	$ 13,111,139	$ (1,217,928)	$ 11,893,211	$ 1,297,429
TIAA	197,589,102	(4,568,617)	193,020,485	4,793,230
	$ 210,700,241	$ (5,786,545)	$ 204,913,696	$ 6,090,659

Long-term debt obligations as of June 30 consisted of the following:

	2018	2017
Secured mortgage - Capital Lease Funding, principal and interest payments began January 2004 and continue until November 2024, with interest at 6.34%	$ 10,595,782	$ 11,893,211
Secured mortgage - TIAA, 25 year, 4.809% coupon. Principal and interest payments began on April 15, 2015 and will continue until March 15, 2040.	188,227,255	193,020,485
	$ 198,823,037	$ 204,913,696

Aggregate maturities of long-term debt are as follows:

Year ending June 30,	
2019	$ 6,411,004
2020	6,748,463
2021	7,103,967
2022	7,478,497
2023	7,873,091
Thereafter	163,208,015
	$ 198,823,037

The Finance Corporation made interest payments of $9,894,381 and $10,185,049, respectively, during 2018 and 2017.

NOTE 5 – RELATED PARTY TRANSACTIONS

The Finance Corporation enters into transactions for the benefit of UConn Health entities. In 2006, the Finance Corporation entered into transactions resulting in the acquisition of the UConn Musculoskeletal Institute and Munson Road properties. The Finance Corporation leases these buildings to entities from UConn Health under operating agreements that renew annually. As disclosed in note 1, for the years ended June 30, 2018 and 2017, rent was not charged to UConn Health related to its occupancy of the Munson Road property.

The Circle Road Corporation has a 25 year direct financing lease with UConn Health, designed to facilitate the monthly debt service payments on its mortgage with TIAA. Beginning in April 2015, the Circle Road Corporation began charging rent to UConn Health's clinical enterprises, including the Hospital and UConn Medical Group. The amounts allocated to each of UConn Heath's internal business units is determined based on the square footage.

Payments to be received under these agreements over the next five years and thereafter are estimated to be as follows:

Year ending June 30,	Outpatient Pavilion (a)	UConn Musculoskeletal Institute
2019	$ 13,976,552	$ 2,020,230
2020	13,976,552	2,020,230
2021	13,976,552	2,020,230
2022	13,976,552	2,020,230
2023	13,976,552	2,020,230
Thereafter	234,107,245	2,861,993
	$ 303,990,005	$ 12,963,143

(a) Outpatient Pavilion amounts are due under a non-cancellable direct financing lease with UConn Health. Additional details can be found in note 6.

During the years ended June 30, 2018 and 2017, the Finance Corporation repaid advances previously received from the Hospital to facilitate the Outpatient Pavilion construction and operating transactions made on its behalf by the Finance Corporation in the amounts of zero and $9,995,498, respectively. Advances are non-interest bearing.

NOTE 5 – RELATED PARTY TRANSACTIONS (CONTINUED)

During fiscal year 2018, the Finance Corporation incurred operating expenses on behalf of Central Administrative Services (CAS) in the amount of $692,406. This amount was offset by operating and investing amounts charged by CAS in the amount of $23,227. In fiscal year 2017, the Finance Corporation received charges for operating and investing from CAS in the amount of $22,693.

NOTE 6 – INVESTMENT IN DIRECT FINANCING LEASE

The Outpatient Pavilion lease, created through the Circle Road Corporation, is a non-cancellable 25 year lease supporting the repayment of the TIAA mortgage. As such, this lease is classified as a direct financing lease. Under this treatment, the underlying capital assets are not recorded separately on the consolidated statements of net position, but the Finance Corporation records its net investment in direct financing lease. The components of the net investment in direct financing lease are shown below as of June 30, 2018 and 2017.

	2018	2017
Net minimum lease payments receivable	$ 303,990,005	$ 317,966,557
Estimated residual value of leased property (unguaranteed)	65,861,269	65,861,269
Less unearned income	(177,701,594)	(189,572,045)
Net investment in direct financing lease	$ 192,149,680	$ 194,255,781

The following schedule provides an analysis of the Circle Road Corporation's cost of the property held for lease under the direct financing lease as of June 30, 2018 and 2017.

	2018	2017
Building	$ 182,419,251	$ 181,668,261
Equipment	18,356,046	18,352,569
Art	104,351	104,351
	$ 200,879,648	$ 200,125,181

The associated equipment has a maximum useful life of 10 years while the building has a useful life of 40 years. The term of the lease is 25 years as stipulated in the mortgage agreement with TIAA. At the conclusion of the lease, any residual amounts will revert to capital assets, net.

NOTE 7 – SUBSEQUENT EVENTS

The Finance Corporation has evaluated subsequent events through November 30, 2018, which represents the date the financial statements were available to be issued. The following matters were noted:

Effective August 15, 2018, Key Bank assumed the mortgage on the UConn Musculoskeletal Institute. There are no changes to the terms of the mortgage payable disclosed in note 4.

In August 2018, CAS advanced $4.0 million to Pharmacy Services Corporation to facilitate the initial purchases of pharmaceuticals for the State of Connecticut Department of Corrections' contract that began in fiscal year 2019.

On October 22, 2018, UConn Health published a Solicitation of Interest seeking potential partners for UConn Medical Group and the Hospital (the "Clinical Group"). The Solicitation of Interest represents UConn Health's effort, as mandated by the General Assembly, to seek partners who can help strengthen UConn Health's clinical offerings while adding overall financial stability to the whole of UConn Health. Responses are expected back by December 3, 2018. Although not part of the Clinical Group as defined by the Solicitation of Interest, changes to the Clinical Group could impact the future operations of the Finance Corporation.

No other subsequent events requiring recognition or disclosure in the financial statements were identified.

MARCUM
ACCOUNTANTS ▲ ADVISORS

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Joint Audit and Compliance Committee
University of Connecticut Health Center

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the University of Connecticut Health Center Finance Corporation (the Company), which comprise the consolidated statement of net position as of June 30, 2018, and the related consolidated statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 30, 2018.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of This Report

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

Marcum LLP

Hartford, CT
November 30, 2018

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

SCHEDULE I – CONSOLIDATING STATEMENT OF NET POSITION

JUNE 30, 2018

	University of Connecticut Health Center Finance Corporation	UCHCFC Circle Road Corp.	Total
Assets			
Current Assets			
Cash	$ 1,290,448	$ 157,279	$ 1,447,727
Malpractice fund	608,177	--	608,177
Construction escrow account	--	529,145	529,145
Due from (to) Central Administrative Services	692,178	(73,092)	619,086
Net investment in direct financing lease, current portion	--	3,028,588	3,028,588
Total Current Assets	2,590,803	3,641,920	6,232,723
Noncurrent Assets			
Net investment in direct financing lease, net of current portion	--	189,121,092	189,121,092
Capital assets, net	26,215,912	--	26,215,912
Total Noncurrent Assets	26,215,912	189,121,092	215,337,004
Total Assets	$ 28,806,715	$ 192,763,012	$ 221,569,727

See independent auditors' report.

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

SCHEDULE I – CONSOLIDATING STATEMENT OF NET POSITION (CONTINUED)

JUNE 30, 2018

	University of Connecticut Health Center Finance Corporation	UCHCFC Circle Road Corporation	Total
Liabilities and Net Position			
Current Liabilities			
Accounts payable and accrued expenses	$ 747,421	$ 452,406	$ 1,199,827
Due to UConn Health – Malpractice fund	608,177	--	608,177
Due to John Dempsey Hospital, current portion	2,000,000	--	2,000,000
Advances for construction	6,619	--	6,619
Security deposits	--	8,279	8,279
Loans payable, current portion	1,382,118	5,028,886	6,411,004
Total Current Liabilities	4,744,335	5,489,571	10,233,906
Noncurrent Liabilities			
Due to John Dempsey Hospital, net of current portion	2,743,408	--	2,743,408
Loans payable, net of current portion	9,213,664	183,198,369	192,412,033
Total Noncurrent Liabilities	11,957,072	183,198,369	195,155,441
Total Liabilities	16,701,407	188,687,940	205,389,347
Net Position			
Net investment in capital assets	15,620,130	4,303,233	19,923,363
Unrestricted deficit	(3,514,822)	(228,161)	(3,742,983)
Total Net Position	12,105,308	4,075,072	16,180,380
Total Liabilities and Net Position	$ 28,806,715	$ 192,763,012	$ 221,569,727

See independent auditors' report.

UNIVERSITY OF CONNECTICUT HEALTH CENTER FINANCE CORPORATION

SCHEDULE II – CONSOLIDATING STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

FOR THE YEAR ENDED JUNE 30, 2018

	University of Connecticut Health Center Finance Corporation	UCHCFC Circle Road Corporation	Total
Operating Revenues			
Rental income	$ 2,020,230	$ 112,176	$ 2,132,406
Interest income from direct financing lease	--	11,115,984	11,115,984
Total Operating Revenues	2,020,230	11,228,160	13,248,390
Operating Expenses			
Professional services	31,900	1,575	33,475
Interest expense	702,859	9,168,017	9,870,876
Depreciation	753,299	--	753,299
Other	3,142	58,500	61,642
Total Operating Expenses	1,491,200	9,228,092	10,719,292
Operating Income	529,030	2,000,068	2,529,098
Nonoperating Expenses			
Loan servicing fee	(6,042)	(5,000)	(11,042)
Total Nonoperating Expenses	(6,042)	(5,000)	(11,042)
Increase in Net Position	522,988	1,995,068	2,518,056
Net Position - Beginning	11,582,320	2,080,004	13,662,324
Net Position - End	$ 12,105,308	$ 4,075,072	$ 16,180,380

See independent auditors' report.