FINANCIAL STATEMENTS

The Nucleus Real Properties, Inc.
An Affiliate of the University of Louisville Foundation, Inc.
Years Ended June 30, 2019 and 2018
With Report of Independent Auditors

Ernst & Young LLP

Building a better
working world

The Nucleus Real Properties, Inc.

Financial Statements

Years Ended June 30, 2019 and 2018

Contents

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Report of Independent Auditors

The Board of Directors
TNRP, Inc.

We have audited the accompanying financial statements of The Nucleus Real Properties, Inc., which comprise the statements of financial position as of June 30, 2019 and 2018, and the related statements of activities and changes in net deficit and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Nucleus Real Properties, Inc. at June 30, 2019 and 2018, and the results of its activities and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

September 26, 2019

The Nucleus Real Properties, Inc.

Statements of Financial Position
(In Thousands)

	June 30 2019	June 30 2018
Assets		
Cash	**$ 930**	$ 612
Restricted cash	**142**	236
Total cash	**1,072**	848
Deferred rent	**3,450**	3,408
Prepaid expenses and other assets	**12**	23
Deferred leasing costs, net	**1,428**	1,582
Tenant improvement allowance, net	**4,717**	5,120
Capital assets, net	**22,465**	23,466
Total assets	**$ 33,144**	$ 34,447
Liabilities and net (deficit) assets		
Liabilities:		
Accounts payable and accrued liabilities	**$ 109**	$ 108
Notes payable	**19,425**	19,393
Note payable to the University of Louisville Foundation, Inc.	**16,160**	16,160
Total liabilities	**35,694**	35,661
Net deficits:		
Without donor restrictions	**439**	275
Distributions to University of Louisville Foundation, Inc., net	**(2,989)**	(1,489)
Total net deficits	**(2,550)**	(1,214)
Total liabilities and net deficits	**$ 33,144**	$ 34,447

See notes to financial statements.

The Nucleus Real Properties, Inc.

Statements of Activities and Changes in Net Assets
(In Thousands)

	Year Ended June 30	
	2019	**2018**
Revenues		
Rental revenue	**$ 3,140**	$ 2,957
Expenses		
Real estate operations	**1,483**	697
Depreciation and amortization	**1,155**	1,199
Total expenses	**2,638**	1,896
	502	1,061
Other expenses		
Interest expense – note payable	**(176)**	(221)
Interest expense – University of Louisville Foundation, Inc.	**(162)**	(162)
Total other expenses	**(338)**	(383)
Increase in net assets without donor restrictions	**164**	678
Net (deficit) assets, beginning of year	**(1,214)**	(699)
Distributions to University of Louisville Foundation, Inc., net	**(1,500)**	(1,193)
Net deficit, end of year	**$ (2,550)**	$ (1,214)

See notes to financial statements.

The Nucleus Real Properties, Inc.

Statements of Cash Flows
(In Thousands)

	Year Ended June 30	
	2019	**2018**
Operating activities		
Increase in net assets without donor restrictions	**$ 164**	$ 678
Adjustments to reconcile increase in net deficits without donor restrictions to net cash provided by operating activities:		
Depreciation and amortization	**1,155**	1,199
Amortization of debt issuance costs	**32**	77
Net changes in assets and liabilities:		
Deferred rent	**(42)**	(96)
Prepaid expenses and other assets	**11**	(9)
Accounts payable and accrued liabilities	**1**	(874)
Tenant improvement allowance, net	**403**	404
Net cash provided by operating activities	**1,724**	1,379
Financing activities		
Distributions to the Foundation	**(1,500)**	1,193
Net cash used in financing activities	**(1,500)**	1,193
Net increase (decrease) in cash	**224**	186
Cash, beginning of year	**848**	662
Cash, end of year	**$ 1,072**	$ 848
Supplemental cash flows information		
Cash paid for interest	**$ 306**	$ 306

See notes to financial statements.

1. Description of Organization and Summary of Significant Accounting Policies

Organization

The Nucleus Real Properties, Inc. (TNRP), a Kentucky not-for-profit corporation, was formed on July 11, 2013, and is a consolidated affiliate of the University of Louisville Foundation, Inc. (the Foundation). TNRP and the Foundation share a common board of directors and certain common management.

TNRP's purpose is to develop the property and manage improvements located at the corner of Market and Shelby Streets in Louisville, Kentucky, commonly known as The Atria Support Center Building, as revenue-producing assets aimed at furthering the charitable and educational purposes of the Foundation. Additionally, TNRP entered into a New Market Tax Credit (NMTC) agreement to provide financing for the Atria Support Center Building. See Note 3 for additional information.

Prior to July 11, 2013, the Foundation financed the Atria Support Center Building with a construction line of credit. Once construction was substantially complete, the Foundation transferred the assets of the Atria Support Center Building to TNRP. TNRP used a portion of the debt proceeds issued through the NMTC agreement to transfer funds to the Foundation to repay the construction line of credit.

Prior to July 11, 2013, the Foundation entered into a management and leasing agreement with NTS Management Company (NTS) to assist with management, leasing, and operation of the Atria Support Center Building. The Foundation assigned the management and leasing agreement to TNRP.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (U.S. GAAP) 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. Estimates could also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

1. Description of Organization and Summary of Significant Accounting Policies (continued)

Cash

The cash carried on the statements of financial position approximates fair value.

At June 30, 2019 and 2018, TNRP's cash accounts exceeded federally insured limits by approximately $822,000 and $598,000, respectively.

Restricted Cash

In connection with the NMTC financing, TNRP was required to establish a cash reserve account. TNRP established the NNMF Sub-CDE XX, LLC (NNMF) reserve account to provide payment for fees related to asset management, tax and accounting, and annual loan servicing throughout the life of the financing. The reserve account will be reduced pro rata, on a quarterly basis, throughout the term of the agreement as long as asset management fees, due and payable, are current. TNRP classifies this account as restricted cash on the statements of financial position.

Rental Revenue and Deferred Rent

TNRP recognizes revenue over the term of each tenant's lease agreement and structures certain lease agreements to include scheduled and specific rent increases over the lease term. For financial reporting purposes, deferred rent consists of rents receivable from these leases recognized on a straight-line basis over the initial lease term. Accrued income from these leases reflected as deferred rent was approximately $3,450,000 and $3,408,000 as of June 30, 2019 and 2018, respectively.

Capital Assets

TNRP records capital assets at cost and expenses depreciation using the straight-line method based on the estimated useful lives of the assets.

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

Land improvements	10 years
Buildings	40 years
Furniture and fixtures	5 years
Tenant finish	3 to 10 years

1. Description of Organization and Summary of Significant Accounting Policies (continued)

TNRP capitalizes interest costs as a component of construction in progress, based on interest costs specific to the project and net of any interest earned on investments acquired with the borrowed funds. For the years ended June 30, 2019 and 2018, TNRP did not capitalize any interest.

Long-Lived Asset Impairment

TNRP 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 are 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 June 30, 2019 and 2018.

Tenant Improvement Allowance

Tenant improvement allowance represents costs incurred with a tenant buildout that are paid by TNRP. TNRP capitalizes these costs and amortizes such costs using the straight-line method over 8 to 17 years, which represents the terms of the leases.

Deferred Leasing Costs

Deferred leasing costs represent expenses incurred in connection with a management and leasing agreement with NTS. TNRP is required to pay NTS a commercial leasing fee equal to 4% of the future minimum gross rental amounts of any new lease or lease expansion and extension. Fees are 2% of the future minimum gross rental amounts for lease renewals. If NTS works with a cooperating broker in connection with a new lease or lease expansion, the commercial leasing fee is equal to 6% of the future minimum gross rental amounts. If NTS leases space to a tenant that is an affiliate of TNRP or the University of Louisville, the fee is 2% of future minimum gross rental amounts. Leasing fees are due 50% at the time of execution of the lease and 50% upon the lease commencement date.

1. Description of Organization and Summary of Significant Accounting Policies (continued)

TNRP amortizes such costs using the straight-line method over the respective lease terms, ranging from 8 to 17 years.

At June 30, 2019 and 2018, approximately $2,110,000 in leasing commission fees has been paid by TNRP, and approximately $682,000 and $528,000, respectively, have been recorded as accumulated amortization.

Tax Status

TNRP is recognized by the Internal Revenue Service as exempt from federal income tax under Section 501(a) of the Internal Revenue Code (the Code) as a charitable organization qualifying under the Code Section 501(c)(3).

TNRP contested its property tax assessment and received a favorable decision from the Louisville Metro Property Valuation Administrator in January 2018, resulting in a refund of taxes during the year ended June 30, 2018. This refund and the change in accrued tax liabilities is reflected in real estate operations on the statements of activities and changes in net deficits for the fiscal year ended June 30, 2018. For the fiscal years ended June 30, 2019 and 2018, TNRP recorded property tax (credits) expenses of approximately $0 and $(654,000), respectively.

Management Fees

TNRP operates under a management agreement with NTS. Under the terms of this agreement, TNRP agrees to pay compensation based on gross revenues, construction supervision costs, and commercial leasing commissions. For the years ended June 30, 2019 and 2018, TNRP recorded management fee expense of approximately $350,000 and $327,000, respectively.

Liquidity

TNRP’s liquid financial assets were approximately $930,000 and $612,000 for the years ended June 30, 2019 and 2018, respectively. These assets consist of cash.

1. Description of Organization and Summary of Significant Accounting Policies (continued)

Recent Accounting Pronouncements

Effective June 30, 2019, TNRP adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities (Topic 958)* (ASU 2016-14). ASU 2016-14 changes certain financial statement requirements for not-for-profit entities in an effort to make the information more meaningful to users and reduce reporting complexity. TNRP adopted ASU 2016-14 in its financial statements, applying it retrospectively to all periods presented. The impact of adoption changes the classification of net deficits on the balance sheets and the statements of changes in net deficits from unrestricted net deficits to net deficits without donor restrictions. TNRP added additional disclosure for the liquidity and availability of financial assets at the balance sheet date to meet cash needs for general expenditures within one year. The adoption of ASU 2016-14 had no impact on the statements of activities and changes in net deficits.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)* (ASU 2016-02). The ASU requires the rights and obligations arising from the lease contracts, including existing and new arrangements, to be recognized as assets and liabilities on the balance sheets. The ASU will require disclosures to help the financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. The ASU is effective for TNRP beginning July 1, 2019, and will be applied using a modified retrospective approach. TNRP is currently in the process of evaluating its lease contracts, as well as certain service contracts that may include embedded leases. Additionally, TNRP is finalizing its analysis of certain key assumptions that will be utilized at the transition date, including the incremental borrowing rate. The primary effect of the new standard will be to record right-of-use assets and obligations for current operating leases, which will have a material impact on the balance sheet and significant incremental disclosures in the financial statement footnotes. The transition adjustment is not expected to have a material impact on the statements of activities and changes in net deficits.

2. Capital Assets

Capital assets as of June 30 are as follows (in thousands):

		2019		2018
Land	**$**	**965**	$	965
Land improvements		**14**		14
Buildings		**22,879**		22,879
Furniture and fixtures		**415**		415
Tenant finish		**3,716**		3,716
Accumulated depreciation and amortization		**(5,524)**		(4,523)
	$	**22,465**	$	23,466

3. Notes Payable

TNRP, a qualified active low-income community business (QALICB), executed a loan agreement on September 12, 2013, that provided borrowings totaling $5,000,000 from PNC CDE 28, LP (PNC) and $14,850,000 from NNMF Sub-CDE XX, LLC (NNMF). These loans financed the construction of the Atria Support Center Building. TNRP secured the loans with a property deed of trust and security agreement filing on the property, along with a guaranty by the Foundation for obligations under the loan agreements. TNRP's loan balance at June 30, 2019 and 2018, is $19,850,000.

Under the terms of the loan agreements, the loans have an interest rate of 0.73%, payable quarterly to PNC and NNMF. The agreement does not permit TNRP to prepay any portion of the loan principal until the seventh anniversary date. Commencing September 2020, TNRP will pay, quarterly in arrears, equal installments of principal and interest in amounts sufficient to fully amortize the principal balances of the loans through the maturity date, December 31, 2043. Total interest expense on the notes for each of the years ended June 30, 2019 and 2018, was approximately $144,000.

Under the terms of the loan agreement, TNRP has certain compliance requirements, including compliance reporting and maintaining its status as a QALICB as defined by the Code.

3. Notes Payable (continued)

Notes payable consist of the following at June 30 (in thousands):

	Description	Fiscal Year of Maturity	2019	2018
PNC CDE Note "A"	Fixed rate of 0.73%, with quarterly interest-only payments of $6 through December 2020, then quarterly principal and interest payments of $42 through maturity	2044	**$ 3,518**	$ 3,518
PNC CDE Note "B"	Fixed rate of 0.73%, with quarterly interest-only payments of $3 through December 2020, then quarterly principal and interest payments of $18 through maturity	2044	**1,482**	1,482
NNMF Note "A"	Fixed rate of 0.73%, with quarterly interest-only payments of $20 through December 2020, then quarterly principal and interest payments of $129 through maturity	2044	**10,886**	10,886
NNMF Note "B"	Fixed rate of 0.73%, with quarterly interest-only payments of $7 through December 2020, then quarterly principal and interest payments of $45 through maturity	2044	**3,964**	3,964
Notes payable			**19,850**	19,850
Less debt issuance costs			**(425)**	(457)
Total notes payable			**$ 19,425**	$ 19,393

TNRP signed a $16,160,194 promissory note, issued September 2013, with the Foundation, maturing in December 2043. The loan has an interest rate of 1%, payable quarterly through September 2020. Beginning in December 2020, TNRP shall make principal and interest payments of $196,847 to amortize the outstanding balance over the remaining period. For each of the years ended June 30, 2019 and 2018, TNRP incurred approximately $162,000 of interest expense to the Foundation related to this note. This note payable to the Foundation is subordinate to the four NMTC notes payable.

3. Notes Payable (continued)

At June 30, 2019, principal payments on the above obligations due in the next five years and thereafter are as follows (in thousands):

	Notes Payable	Note Payable to the University of Louisville Foundation, Inc.
2020	$ –	$ –
2021	742	470
2022	794	633
2023	800	639
2024	805	645
Thereafter	16,709	13,773
	$ 19,850	$ 16,160

4. Related-Party Transactions

During the years ended June 30, 2019 and 2018, TNRP distributed cash to the Foundation approximating $1,500,000 and $1,193,000, respectively, which is included in distributions to the University of Louisville Foundation, Inc. within the statements of activities and changes in net deficits. The distributions represent net available cash flows from TNRP and are transferred to the Foundation monthly.

Rental revenues with related parties included in rental revenue within the statements of activities and changes in net deficits for the years ended June 30, 2019 and 2018, include the following (in thousands):

	2019	2018
University of Louisville Institute for Optimal Aging	**$ 130**	$ 130
University of Louisville Executive Vice President for Research and Innovation	**574**	574
University of Louisville Physicians, Inc.	**1,084**	1,060
Advanced Cancer Therapeutics, LLC	**33**	44
	$ 1,821	$ 1,808

5. Leasing Activities

TNRP leases space to tenants under noncancelable operating leases. As of June 30, 2019 and 2018, TNRP had leases with five tenants. These leases expire in 4 to 12 years, through 2031. These leases generally require TNRP to pay all executory costs (property taxes, maintenance, and insurance).

Future leasing rent payments due to TNRP during the next five years ending June 30 and thereafter are as follows (in thousands):

	Leasing Payments Due
For the year ending June 30:	
2020	$ 3,449
2021	3,505
2022	3,562
2023	3,620
2024	3,348
Thereafter	14,781
Total	$ 32,265

6. Major Tenants

As of June 30, 2019 and 2018, TNRP has leased approximately 95% of leasable space to three tenants.

7. Unleased Space

As of June 30, 2019, approximately 2% of leasable space is vacant.

8. Subsequent Events

TNRP has evaluated and disclosed subsequent events through September 26, 2019, which is the date the financial statements were made publicly available. No recognized or nonrecognized subsequent events were identified for recognition or disclosure in the financial statements.

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