

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Independent Auditor's Report and Financial Statements
August 31, 2017 and 2016



City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
August 31, 2017 and 2016

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Independent Auditor's Report

The Honorable Mayor, Board of Trustees,
and Members of the City Council
Community Health Permanent Endowment Fund
City of Lincoln, Nebraska

We have audited the accompanying financial statements of the Community Health Permanent Endowment Fund of the City of Lincoln, Nebraska, as of and for the years ended August 31, 2017 and 2016, and the related notes to financial statements, which collectively comprise the Community Health Permanent Endowment of the City of Lincoln, Nebraska's basic financial statement 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.

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 of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Community Health Permanent Endowment Fund of the City of Lincoln, Nebraska, as of August 31, 2017 and 2016, and the changes in its financial position for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of the Community Health Permanent Endowment Fund are intended to present the financial position and changes in financial position of only that portion of the governmental activities, each major fund and the aggregate remaining fund information of the City of Lincoln, Nebraska, that is attributable to the transactions of the Community Health Permanent Endowment Fund. They do not purport to, and do not, present fairly the financial position of the City of Lincoln, Nebraska as of August 31, 2017 and 2016, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by this missing information.

BKD, LLP

Lincoln, Nebraska
February 15, 2018

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Balance Sheets
August 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Assets		
Cash and cash equivalents	\$ 29,757	\$ 639,237
Equity in pooled cash and investments, including cash and cash equivalents of \$2,172 for 2017 and \$32,555 for 2016	377,890	1,003,629
Investments	65,060,983	61,909,411
Accrued interest receivable	<u>2,803</u>	<u>2,200</u>
Total assets	<u><u>\$ 65,471,433</u></u>	<u><u>\$ 63,554,477</u></u>
Liabilities and Fund Balance		
Liabilities		
Accounts payable	\$ 154,346	\$ 15,590
Accrued liabilities	6,868	10,596
Due to other City funds	<u>158</u>	<u>107</u>
Total liabilities	<u>161,372</u>	<u>26,293</u>
Fund Balance		
Nonspendable	37,000,000	37,000,000
Restricted by constitutional provisions	<u>28,310,061</u>	<u>26,528,184</u>
Total fund balance	<u>65,310,061</u>	<u>63,528,184</u>
Total liabilities and fund balance	<u><u>\$ 65,471,433</u></u>	<u><u>\$ 63,554,477</u></u>

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Statements of Revenues, Expenditures and Changes in Fund Balance
Years Ended August 31, 2017 and 2016

	2017	2016
Revenues		
Investment income	\$ 4,547,388	\$ 4,381,974
Other	170	25,000
Total revenues	4,547,558	4,406,974
Expenditures		
Grants	2,316,158	1,735,825
Salaries and benefits	362,427	357,165
Other services and charges	87,096	71,725
Total expenditures	2,765,681	2,164,715
Increase in Fund Balance	1,781,877	2,242,259
Fund Balance, Beginning of Year	63,528,184	61,285,925
Fund Balance, End of Year	\$ 65,310,061	\$ 63,528,184

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 1: Summary of Significant Accounting Policies

Organization and Nature of Operations

The Community Health Permanent Endowment Fund ("CHE") is a permanent fund of the City of Lincoln, Nebraska (the "City") used for the purpose of funding health and health-related programs or projects which further the health, safety or welfare of the citizens of the City. CHE is operated under the direction of a Board of Trustees appointed by the Mayor. CHE was created from net cash proceeds received from the sale of Lincoln General Hospital on October 31, 1997. Donations, bequests or appropriations are also accepted by CHE.

As stated in the City ordinance, it is the intent of the City that CHE will not spend the original net proceeds from the sale of Lincoln General Hospital. Under the City ordinance, the net cash proceeds received from the sale of Lincoln General Hospital of \$37 million must be maintained by CHE in perpetuity. However, in the event of a community health disaster, the Director of the Lincoln-Lancaster County Health Department may initiate a written request for funds to the CHE Board of Trustees and the City Council to invade the principal, for the purpose of alleviating such disaster. If a majority of trustees of the CHE Board of Trustees has voted to allow the request for funds to alleviate a health disaster, a majority vote of the City Council shall authorize such use of the endowment funds. If a majority of the CHE Board of Trustees has not voted to allow such a request, a two-thirds vote of the City Council shall be required to authorize such requested use of funds. Regardless of the total fund balance at the time of request, such request shall not exceed \$9,250,000.

The CHE Board of Trustees has adopted a statement of investment policy. The primary investment objective of CHE is to increase the value of its financial assets by an amount that is greater than the combination of expenditures and the rate of inflation. This objective supports the purpose of CHE by using its resources prudently, while growing and preserving its assets.

The financial statements present only CHE and do not purport to, and do not, present fairly the financial position of the City as of August 31, 2017 and 2016, and the changes in its financial position for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Measurement Focus and Basis of Accounting

The financial statements are prepared using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized as soon as they are both measurable and available, and expenditures are recognized when a liability is incurred and matured (due and payable). Investment income is considered susceptible to accrual. Other revenue is generally recognized when collected in cash.

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 1: 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 contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenditures and other changes in fund balances during the reporting period. Actual results could differ from those estimates.

Fund Balance Classifications

The fund balances for the Community Health Permanent Endowment Fund are displayed in four components, if applicable:

Nonspendable – Nonspendable fund balances are not in a spendable form or are required to be maintained intact.

Restricted – Restricted fund balances may be spent only for the specific purposes stipulated by external resource providers, constitutionally or through enabling legislation. Restrictions may be changed or lifted only with the consent of resource providers.

Committed – Committed fund balances may be used only for the specific purposes determined by resolution of the City Council. Commitments may be changed or lifted only by issuance of a resolution by the City Council.

Assigned – Assigned fund balances are intended to be used by the City for specific purposes as determined by management. In governmental funds other than the general fund, such as the Community Health Permanent Endowment Fund, the assigned fund balance represents the amount that is not restricted or committed. This indicates that resources in other governmental funds are, at a minimum, intended to be used for the purpose of that fund.

Deposits and Investments

The City Treasurer is responsible for the safekeeping of cash and invested funds of CHE. The City is authorized to invest in certificates of deposit, time deposits, and any securities in which the State investment officer is authorized to invest pursuant to the Nebraska Capital Expansion Act and the Nebraska State Funds Investment Act and as provided in the authorized investment guidelines of the Nebraska Investment Council in effect on the date the investment is made. In addition, the Constitution of the State of Nebraska permits public endowments to invest in the manner required of a prudent investor acting with care, skill and diligence under the prevailing circumstance, without restrictions as to the type and limits of investments. Cash balances in excess of current requirements are invested along with cash from other City funds and the interest earned on these investments is allocated monthly to the various funds by the City Treasurer on a pro rata basis using aggregate quarterly balances.

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 1: Summary of Significant Accounting Policies - Continued

Deposits and Investments - Continued

CHE considers cash on hand and in the bank, as well as equity in pooled cash and investments held by the City Treasurer, which are readily convertible to known amounts of cash and have original maturities of three months or less from the date of acquisition, to be cash and cash equivalents.

CHE participates in a cash management pool managed by the City. The pool consists of bank deposits and investments. CHE's interest in this pool is shown as equity in pooled cash and investments in the balance sheets, as applicable. Fair value of the equity in the pool is the same as the value of the pool shares determined using the fair value of the pool's underlying investment portfolio.

Fair value is determined using quoted market prices, if available. Money market mutual funds are valued at amortized cost, which approximates fair value. Institutional funds and limited partnership interests are valued at the net asset value (NAV) of shares held by the fund. The NAV of the fund includes the market value of the securities in the fund, plus any receivables and the market value of the cash collateral fund, if any. The NAV also includes payables and accrued fund expenses. None of CHE's institutional funds or limited partnership interests have any unfunded commitments, and these investments can be redeemed by CHE at any time. Investment income includes interest income and the net change for the year in the fair value of investments.

Grants

Grants are recognized as expenditures and liabilities when all eligibility requirements have been met. The Fund is committed to pay grants totaling approximately \$3,417,000 at August 31, 2017. Such grants are subject to the satisfaction of eligibility requirements before payment and recognition in the financial statements.

Note 2: Deposits, Investments and Investment Return

Deposits

Custodial credit risk is the risk that in the event of a bank failure, a government's deposits may not be returned to it. The Fund has been allocated a portion of the City's pooled cash and investments. The City's deposit policy for custodial credit risk requires compliance with the provisions of state law.

State Statutes 15-846 and 15-847 R.R.S., 1943 require banks either to provide a bond, provide a Federal Home Loan Bank letter of credit, or to pledge government securities (types of which are specifically identified in the Statutes) to the City Treasurer in the amount of the City's deposits. The Statutes allow pledged securities to be reduced by the amount of the deposit insured by the Federal Deposit Insurance Corporation (FDIC).

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 2: Deposits, Investments and Investment Return - Continued

Deposits - Continued

The City's cash deposits, including certificates of deposit, are insured up to \$250,000 by the FDIC. Any cash deposits or certificates of deposit in excess of the \$250,000 FDIC limits are covered by collateral held in a Federal Reserve pledge account or by an agent for the City, or a letter of credit issued by the Federal Reserve Bank, and thus no custodial credit risk exists. No legal opinion has been obtained regarding the enforceability of any of the collateral arrangements.

Investments

As a public endowment fund, under State law, CHE is permitted to invest in the manner required of a prudent investor acting with care, skill and diligence under the prevailing circumstance, without restrictions as to the type and limits of investments. CHE has engaged one of the world's largest institutional investment firms to advise on portfolio management. That investment firm and affiliates are also the sponsor and investment manager for all of the institutional funds listed below.

At August 31, 2017 and 2016, CHE had the following investments and maturities:

	Carrying Value	Maturities in Years			
		Less Than 1	1-5	6-10	More Than 10
August 31, 2017					
Money market mutual funds	\$ 17,856	\$ 17,856	\$ -	\$ -	\$ -
Institutional funds					
Fixed income	11,416,091	-	10,742,694	23,249	650,148
Intermediate term credit	3,241,099	-	3,241,099	-	-
Large cap equity	4,519,561	4,519,561	-	-	-
International equity	15,774,951	15,774,951	-	-	-
High-yield bonds	6,440,478	-	-	6,440,478	-
Emerging markets equity	3,925,256	3,925,256	-	-	-
Mid cap equity	3,189,559	3,189,559	-	-	-
U.S. Treasuries	6,500,011	-	6,500,011	-	-
Small cap equity	3,218,636	3,218,636	-	-	-
Commodities	3,261,553	3,261,553	-	-	-
Real estate	3,208,682	3,208,682	-	-	-
Limited partnership	365,106	365,106	-	-	-
	<u>\$ 65,078,839</u>	<u>\$ 37,481,160</u>	<u>\$ 20,483,804</u>	<u>\$ 6,463,727</u>	<u>\$ 650,148</u>

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 2: Deposits, Investments and Investment Return - Continued

Investments - Continued

	Carrying Value	Maturities in Years			
		Less Than 1	1-5	6-10	More Than 10
August 31, 2016					
Money market mutual funds	\$ 628,439	\$ 628,439	\$ -	\$ -	\$ -
Institutional funds					
Fixed income	14,411,386	-	13,630,712	151,673	629,001
Intermediate term credit	5,126,826	-	5,126,826	-	-
Large cap equity	3,062,221	3,062,221	-	-	-
International equity	9,912,274	9,912,274	-	-	-
High-yield bonds	7,511,787	-	3,764,613	3,747,174	-
Emerging markets equity	2,500,263	2,500,263	-	-	-
Mid cap equity	3,105,027	3,105,027	-	-	-
U.S. Treasuries	4,971,149	-	4,971,149	-	-
Small cap equity	3,092,878	3,092,878	-	-	-
Commodities	1,983,866	1,983,866	-	-	-
Real estate	5,795,363	5,795,363	-	-	-
Limited partnership	436,371	-	436,371	-	-
	<u>\$ 62,537,850</u>	<u>\$ 30,080,331</u>	<u>\$ 27,929,671</u>	<u>\$ 3,898,847</u>	<u>\$ 629,001</u>

Interest Rate Risk - As a means of limiting its exposure to fair value losses arising from rising interest rates, CHE's investment policy requires the average duration of the fixed income portfolio to be no more than 120% of the appropriate fixed income benchmark.

Credit Risk - Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. It is CHE's policy to limit its investments in fixed income securities to issues with at least BBB-/Baa3 ratings (S&P/Moody's). Short-term fixed income issues should have a minimum A-2/P-2 rating. None of CHE's investments were rated at August 31, 2017 and 2016.

Custodial Credit Risk - For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, CHE will not be able to recover the value of its investment securities that are in the possession of an outside party. All investments are held in CHE's name.

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 2: Deposits, Investments and Investment Return - Continued

Investments - Continued

Concentration of Credit Risk - Concentration of credit risk is the risk associated with the amount of investments CHE has with any one issuer that exceeds 5% or more of its total investments. CHE limits the percentage that may be invested in any one sector, company and issuer. CHE's portfolio shall not own more than 5% of the outstanding securities of any single issuer. Exceptions are allowed where a fund's benchmark includes securities greater than 3%, in which case the investment manager may have no more than the securities index weight plus 2%. The entire portfolio shall have no more than 5% of its assets invested in the securities of any one issuer, with the exception of U.S. Treasury and U.S. agencies obligations.

Foreign Currency Risk - This risk relates to adverse affects on the fair value of an investment from changes in exchange rates. CHE had no investments denominated in foreign currency at August 31, 2017 and 2016.

Summary of Carrying Values

The carrying values of deposits and investments are included in the balance sheets as follows:

	2017	2016
Carrying value		
Deposits	\$ 11,901	\$ 10,798
Investments	65,078,839	62,537,850
Equity in pooled cash and investments	377,890	1,003,629
	\$ 65,468,630	\$ 63,552,277
Included in the following balance sheet captions		
Cash and cash equivalents	\$ 29,757	\$ 639,237
Equity in pooled cash and investments	377,890	1,003,629
Investments	65,060,983	61,909,411
	\$ 65,468,630	\$ 63,552,277

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 3: Active Living Center

In fiscal year 2012, construction was completed on the Active Living Center, a mixed-use building located in the City's newly constructed Antelope Valley Redevelopment Area. CHE's portion of the Active Living Center is being used for its office and meeting space. CHE owns, manages, and operates its portion of the building and, consistent therewith, the internal records of the City identify CHE as the owner. However, as CHE is a permanent endowment governmental fund of the City of Lincoln, capital assets are not shown as assets in the financial statements, but were presented as expenditures in the period when the related costs were incurred. Total capital expenditures incurred by CHE, in prior years, for its portion of the building totaled approximately \$725,000.

Note 4: Risk Management

CHE participates in the City's self-insurance program, administered by the City's Risk Management Division. The City is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees and the public; or acts of God. The City has a self-insured retention for workers' compensation exposures up to \$800,000 per individual; building and contents exposures up to \$75,000 per occurrence; general liability exposures up to \$250,000 per occurrence and employee long-term disability.

Workers' compensation and general liability are covered by excess insurance which provides statutory limits above the City's retention. The Nebraska Political Tort Claims Act limits the City's liability for tort claims to \$1 million per individual and \$5 million per occurrence. Settled claims have not exceeded coverage in any of the past three fiscal years.

Premium amounts are paid to the Insurance Revolving Fund, including an estimate of the liability for claims incurred, but not yet reported as of August 31, 2017 and 2016.

Note 5: Retirement Plan

CHE offers employees a deferred compensation plan created in accordance with provisions in IRS Section 457. The deferred compensation plan allows employees to defer a portion of current salary to future years, but the deferred balance is not available to employees until termination, retirement, death, or unforeseeable emergency. All amounts of compensation deferred under the plan, including income attributed to such amounts, are placed in a trust which is not the property of CHE. Therefore, assets and liabilities related to the deferred compensation plan are not included in the basic financial statements.

City of Lincoln, Nebraska
Community Health Permanent Endowment Fund
Notes to Financial Statements
August 31, 2017 and 2016

Note 6: Disclosures About Fair Value of Assets and Liabilities

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. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- 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 are significant to the fair value of the assets or liabilities

CHE's investments in money market mutual funds are carried at cost, and thus are not included within the fair value hierarchy. CHE's investments in institutional funds and limited partnership interests are carried at net asset value, and thus are not included within the fair value hierarchy.

