NEW ISSUE – Book-Entry-Only **Ratings: See "RATINGS" herein**

In the opinion of Kutak Rock LLP, Bond Counsel with respect to the Series 2006 A Notes, and in the preliminary opinion of Bond Counsel with respect to the Series 2007 A Notes, under existing laws, regulations, rulings and judicial decisions, interest (including original issue discount treated as interest) on the Series 2006 A Notes is, and on the Series 2007 A Notes would be, excluded from gross income for federal income tax purposes and is not, in the case of the Series 2006 A Notes, and would not be, in the case of the Series 2007 A Notes, an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations, except that such interest must be included in the "adjusted current earnings" of certain corporations for purposes of calculating alternative minimum taxable income. Bond Counsel also is of the opinion with respect to the Series 2006 A Notes and the Series 2006 B Notes, and of the preliminary opinion with respect to the Series 2007 A Notes, that, under existing laws of the Commonwealth of Kentucky, interest on the Series 2006 A Notes and the Series 2006 B Notes is, and on the Series 2007 A Notes would be, excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Series 2006 A Notes and the Series 2006 B Notes are, and the Series 2007 A Notes would be, exempt from ad valorem taxes by the Commonwealth of Kentucky and all political subdivisions thereof. See "TAX MATTERS" herein.

$146,430,000
COMMONWEALTH OF KENTUCKY
KENTUCKY ASSET/LIABILITY COMMISSION
UNIVERSITY OF KENTUCKY GENERAL RECEIPTS PROJECT NOTES

Consisting of

$66,305,000 GENERAL RECEIPTS REFUNDING PROJECT NOTES, 2006 SERIES A	$2,220,000 GENERAL RECEIPTS TAXABLE REFUNDING PROJECT NOTES, 2006 SERIES B	$77,905,000 GENERAL RECEIPTS PROJECT NOTES, 2007 SERIES A

Dated: Date of delivery **Due: As shown on inside front cover**

The Kentucky Asset/Liability Commission (the "Commission") will issue its University of Kentucky General Receipts Project Notes, consisting of $66,305,000 General Receipts Refunding Project Notes, 2006 Series A (the "2006 A Notes"), $2,220,000 General Receipts Taxable Refunding Project Notes, 2006 Series B (the "2006 B Notes") and $77,905,000 General Receipts Project Notes, 2007 Series A (the "2007 A Notes" and collectively, the "Notes"). The Notes will be issued only as fully registered notes, and when issued, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Notes. Purchasers will not receive certificates representing their ownership interest in the Notes purchased. So long as DTC or its nominee is the registered owner of the Notes, payments of the principal of and interest due on the Notes will be made directly to DTC. The Notes will be issued in denominations of $5,000 or any integral multiples thereof. Principal of and interest on the Notes will be paid directly to DTC by U.S. Bank National Association having offices in Atlanta, Georgia, as Trustee and Paying Agent (the "Trustee" and "Paying Agent").

The expected delivery date for the 2007 A Notes is on or about November 1, 2007. The forward delivery date gives rise to certain conditions to the Underwriter's obligation to purchase the 2007 A Notes and to certain risks to investors.

The 2006 A Notes and 2006 B Notes will bear interest payable on each April 1 and October 1, commencing on April 1, 2007. The 2007 A Notes will bear interest payable on each April 1 and October 1, commencing on April 1, 2008. The Notes mature on the dates, in the principal amounts, bear interest at the rates per annum and have the prices or yields shown on the inside front cover.

The Notes are subject to optional redemption prior to maturity, as set forth herein. See "THE NOTES – Optional Redemption" herein.

The Commission is issuing the Notes pursuant to a Resolution of the Commission adopted September 18, 2006, to (i) pay certain expenditures in certain amounts in connection with the construction of the Patient Care Facility Phase II – Hospital for the benefit of the University of Kentucky (the "University"), (ii) pay the interest coming due on the 2007 A Notes through and including October 1, 2009, (iii) refund certain bonds previously issued by the University, (iv) refund certain bonds previously issued by the State Property and Buildings Commission to finance facilities for the University, and (v) pay the costs of issuing the Notes. See "REFUNDING PLAN" and "THE CONSTRUCTION PROJECT" herein. The Notes are being issued pursuant to the Trust Indenture dated as of October 1, 2006 (the "Indenture") between the Commission and the Trustee. See "THE NOTES" herein.

The Notes and any interest due thereon are payable solely and only from a special fund created under the Indenture and defined therein as the Note Payment Fund (the "Note Payment Fund"), into which Financing Payments (as defined herein) received from the University are to be deposited. The Financing Payments arise under a Financing/Lease Agreement, dated as of October 1, 2006 (the "Financing Agreement"), among the Commission, the University and the Commonwealth of Kentucky Finance and Administration Cabinet (the "Cabinet"). The University has authorized and entered into a Trust Agreement dated as of November 1, 2005 (the "Trust Agreement"), under which it has pledged its General Receipts, as defined in the Trust Agreement, as security for the payment of Obligations, as defined in the Trust Agreement, issued thereunder. The Financing Agreement constitutes an Obligation within the meaning of the Trust Agreement. See "SECURITY FOR THE NOTES," "SUMMARY OF THE PRINCIPAL DOCUMENTS" and "APPENDIX B – SUMMARY OF THE TRUST AGREEMENT" herein.

The scheduled payment of principal of and interest on the Series 2006 A Notes and the Series 2006 B Notes, when due, will be guaranteed under a Financial Guaranty Insurance Policy to be issued concurrently with the delivery of the Series 2006 A Notes and the Series 2006 B Notes by Ambac Assurance Corporation (the "Bond Insurer"). The scheduled payment of principal of and interest on the Series 2007 A Notes, when due, will be guaranteed under a Financial Guaranty Insurance Policy to be issued concurrently with the delivery of the Series 2007 A Notes by the Bond Insurer.

Ambac

THE NOTES ARE SPECIAL AND LIMITED OBLIGATIONS OF THE COMMISSION. THE NOTES DO NOT CONSTITUTE A DEBT, LIABILITY OR OBLIGATION OF THE COMMONWEALTH, OR A PLEDGE OF THE FULL FAITH AND CREDIT OR TAXING POWER OF THE COMMONWEALTH, BUT ARE PAYABLE SOLELY FROM AMOUNTS DEPOSITED IN CERTAIN FUNDS AND ACCOUNTS CREATED BY THE RESOLUTION AND FROM RENTAL INCOME DERIVED FROM A FINANCING AGREEMENT WITH THE UNIVERSITY.

The Notes are offered when, as and if issued and accepted by the Underwriters (Morgan Stanley acting as sole underwriter with respect to the 2007 A Notes), subject to the approving legal opinion of Kutak Rock LLP, Bond Counsel. Certain legal matters will be passed on for the Underwriters by their counsel, Thompson Hine LLP, Cincinnati, Ohio. It is expected that delivery of the 2006 A Notes and the 2006 B Notes will be made on or about October 18, 2006 and the 2007 A Notes on or about November 1, 2007, through the facilities of DTC, against payment therefore.

MORGAN STANLEY*

J.J.B. Hilliard, W.L. Lyons, Inc. **Morgan Keegan & Co., Inc.**
NatCity Investments, Inc. **JPMorgan**
Ross, Sinclaire & Associates, LLC **A.G. Edwards**
Edward D. Jones & Co., L.P. **First Kentucky Securities Corp.** **Seasongood & Mayer LLC**

Dated: October 6, 2006

* Morgan Stanley is sole manager on 2007 Series A and lead manager on Series 2006 Series A and B

$66,305,000
UNIVERSITY OF KENTUCKY GENERAL RECEIPTS REFUNDING PROJECT NOTES, 2006 SERIES A
MATURITY SCHEDULE

Maturity	Principal Amount	Interest Rate	Yield	CUSIP*
April 1, 2007	$150,000	4.000%	3.450%	49119GBV0
October 1, 2007	525,000	4.000%	3.450%	49119GBW8
October 1, 2008	2,870,000	4.000%	3.480%	49119GBX6
October 1, 2009	160,000	4.000%	3.520%	49119GBY4
October 1, 2009	2,845,000	5.000%	3.520%	49119GBZ1
October 1, 2010	2,140,000	3.500%	3.550%	49119GCA5
October 1, 2010	1,000,000	5.000%	3.550%	49119GCB3
October 1, 2011	3,780,000	3.500%	3.570%	49119GCC1
October 1, 2012	525,000	4.000%	3.640%	49119GCD9
October 1, 2012	3,415,000	5.000%	3.640%	49119GCE7
October 1, 2013	4,120,000	4.000%	3.680%	49119GCF4
October 1, 2014	2,140,000	4.000%	3.720%	49119GCG2
October 1, 2014	2,155,000	5.000%	3.720%	49119GCH0
October 1, 2015	1,590,000	3.750%	3.770%	49119GCJ6
October 1, 2015	2,905,000	5.000%	3.770%	49119GCK3
October 1, 2016	2,960,000	4.000%	3.820%	49119GCL1
October 1, 2016	1,740,000	5.000%	3.820%	49119GCM9
October 1, 2017	580,000	4.000%	3.940% C	49119GCN7
October 1, 2017	4,335,000	4.625%	3.900% C	49119GCP2
October 1, 2018	2,390,000	4.000%	4.020%	49119GCQ0
October 1, 2018	2,745,000	4.375%	4.010% C	49119GCR8
October 1, 2019	2,060,000	4.000%	4.080%	49119GCS6
October 1, 2019	3,295,000	4.500%	4.070% C	49119GCT4
October 1, 2020	490,000	4.125%	4.200%	49119GCU1
October 1, 2020	5,110,000	4.375%	4.200% C	49119GCV9
October 1, 2021	5,030,000	4.250%	4.280%	49119GCW7
October 1, 2022	5,250,000	4.300%	4.330%	49119GCX5

C – Priced to the October 1, 2016 optional call date at a redemption price of par.

$2,220,000
UNIVERSITY OF KENTUCKY GENERAL RECEIPTS TAXABLE REFUNDING PROJECT NOTES, 2006 SERIES B
MATURITY SCHEDULE

Maturity	Principal Amount	Interest Rate	Yield	CUSIP*
October 1, 2007	$2,220,000	5.125%	5.112%	49119GCY3

$77,905,000
UNIVERSITY OF KENTUCKY GENERAL RECEIPTS PROJECT NOTES, 2007 SERIES A
MATURITY SCHEDULE

Maturity	Principal Amount	Interest Rate	Yield	CUSIP*
October 1, 2010	$2,735,000	5.000%	3.700%	49119GBB4
October 1, 2011	2,875,000	5.000%	3.730%	49119GBC2
October 1, 2012	3,025,000	5.000%	3.760%	49119GBD0
October 1, 2013	3,180,000	5.000%	3.810%	49119GBE8
October 1, 2014	3,340,000	5.000%	3.850%	49119GBF5
October 1, 2015	3,515,000	5.000%	3.890%	49119GBG3
October 1, 2016	3,695,000	5.000%	3.950%	49119GBH1
October 1, 2017	3,885,000	5.000%	4.020%	49119GBJ7
October 1, 2018	4,085,000	5.000%	4.070% C	49119GBK4
October 1, 2019	4,290,000	5.000%	4.110% C	49119GBL2
October 1, 2020	4,510,000	5.000%	4.150% C	49119GBM0
October 1, 2021	4,745,000	5.000%	4.180% C	49119GBN8
October 1, 2022	4,985,000	5.000%	4.210% C	49119GBP3
October 1, 2023	5,240,000	5.000%	4.240% C	49119GBQ1
October 1, 2024	5,510,000	5.000%	4.270% C	49119GBR9
October 1, 2025	5,795,000	5.000%	4.290% C	49119GBS7
October 1, 2026	6,090,000	5.000%	4.310% C	49119GBT5
October 1, 2027	6,405,000	5.000%	4.330% C	49119GBU2

C – Priced to the October 1, 2017 optional call date at a redemption price of par.

This Official Statement does not constitute an offer to sell the Notes to any person, or the solicitation of an offer from any person to buy the Notes, in any jurisdiction where such offer or such solicitation of an offer to buy would be unlawful. The information set forth herein is provided by the Commonwealth of Kentucky from sources which are believed to be reliable, but it is not guaranteed as to accuracy or completeness and is not to be construed as a representation of the Underwriter. No dealer, salesman or any other person has been authorized to give any information or to make any representation, other than those contained in this Official Statement, in connection with the offering contained herein, and, if given or made, such information or representation must not be relied upon as having been authorized by the Commonwealth of Kentucky or the Underwriter. The information and expressions of opinion contained herein are subject to change without notice, and neither the delivery of this Official Statement nor the sale of any Notes shall, under any circumstances, create any implication that there has been no change in the matters described herein since the date hereof. The Official Statement is submitted in connection with the issuance of the Notes referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION OR AUTHORITY, NOR HAS SUCH FEDERAL OR ANY STATE COMMISSION OR AUTHORITY PASSED UPON THE ACCURACY OR ADEQUACY OF THIS OFFICIAL STATEMENT. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH TEND TO STABILIZE OR MAINTAIN THE MARKET PRICE FOR THE NOTES ABOVE THE LEVELS WHICH WOULD OTHERWISE PREVAIL. SUCH ACTIVITIES, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

KENTUCKY ASSET/LIABILITY COMMISSION

COMMISSION MEMBERS

John R. Farris, Secretary of the Finance and Administration Cabinet, Chairman

Gregory D. Stumbo, Attorney General

Jonathan Miller, State Treasurer

Bradford L. Cowgill, State Budget Director

Ed C. Ross, State Controller

SECRETARY TO THE COMMISSION

F. Thomas Howard, Executive Director of the Office of Financial Management

UNIVERSITY OF KENTUCKY BOARD OF TRUSTEES

James F. Hardymon, Chair
JoEtta Y. Wickliffe, Vice Chair
Pamela Robinette May, Secretary
Mira S. Ball, Member
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Jonah Brown, Student Member
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Dermontti F. Dawson, Member
Jeffrey B. Dembo, Faculty Member
Ann Brand Haney, Alumni Member
Billy Joe Miles, Member
Sandy Patterson, Alumni Member
Phillip R. Patton, Member
Erwin Roberts, Member
C. Frank Shoop, Member
Myra Leigh Tobin, Alumni Member
Billy B. Wilcoxson, Member
Russ Williams, Staff Member
Ernest J. Yanarella, Faculty Member
Barbara Smith Young, Member

TRUSTEE AND PAYING AGENT

U.S. Bank National Association
Having offices in Atlanta, Georgia

BOND COUNSEL

Kutak Rock LLP
Omaha, Nebraska

UNDERWRITERS' COUNSEL

Thompson Hine LLP
Cincinnati, Ohio

TABLE OF CONTENTS

SUMMARY

The following information is furnished solely to provide limited introductory information regarding the Kentucky Asset/Liability Commission (the "Commission") and the Notes and does not purport to be comprehensive. Such information is qualified in its entirety by reference to the more detailed information and descriptions appearing elsewhere in this Official Statement and should be read together therewith. The terms used in this Summary and not otherwise defined shall have the respective meanings assigned to them elsewhere in this Official Statement. The offering of the Notes is made only by means of the entire Official Statement, including the Appendixes hereto. No person is authorized to make offers to sell, or solicit offers to buy, the Notes unless the entire Official Statement is delivered in connection therewith.

The Commission The Commission is an independent agency of the Commonwealth of Kentucky (the "Commonwealth"). See "THE KENTUCKY ASSET/LIABILITY COMMISSION" herein.

The Offering The Commission is offering its University of Kentucky General Receipts Refunding Project Notes, 2006 Series A in an aggregate principal amount of $66,305,000 (the "2006 A Notes"), University of Kentucky General Receipts Taxable Refunding Project Notes, 2006 Series B in an aggregate principal amount of $2,220,000 (the "2006 B Notes") and University of Kentucky General Receipts Project Notes, 2007 Series A in an aggregate principal amount of $77,905,000 (the "2007 A Notes" and collectively, the "Notes"). See "THE NOTES" herein.

Authority The Notes are being issued pursuant to Section 56.860 *et seq*. of the Kentucky Revised Statutes (the "Act"), a Resolution adopted by the Commission on September 18, 2006 (the "Resolution"), and a Trust Indenture dated as of October 1, 2006 (the "Indenture"), between the Commission and U.S. Bank National Association having offices in Atlanta, Georgia, as trustee and paying agent (the "Trustee" and "Paying Agent"). The State Property and Buildings Commission of the Commonwealth also has approved the issuance of the Notes.

Use of Proceeds The proceeds of the Notes will be used by the Commission to (i) pay certain expenditures in certain amounts in connection with the construction of the Patient Care Facility Phase II - Hospital (the "Construction Project") for the benefit of the University of Kentucky (the "University"), (ii) pay the interest coming due on the 2007 A Notes through and including October 1, 2009, (iii) refund certain bonds previously issued by the University, (iv) refund certain bonds previously issued by the State Property and Buildings Commission to finance facilities for the University, and (v) pay the costs of issuing the Notes. See "REFUNDING PLAN" and "THE CONSTRUCTION PROJECT" herein.

Features The 2006 A Notes and 2006 B Notes will be dated as of their date of delivery, and will bear interest on each April 1 and October 1, commencing April 1, 2007, at the rates set forth on the inside cover page of this Official Statement and will mature on the dates set forth on the inside cover page of this Official Statement.

The 2007 A Notes will be dated as of their date of delivery, and will bear interest on each April 1 and October 1, commencing April 1, 2008, at the rates set forth on the inside cover page of this Official Statement and will mature on the dates set forth on the inside cover page of this Official Statement.

The Notes are subject to optional redemption prior to their respective maturities as described herein.

The Notes are issuable only as fully registered Notes, without coupons. The Notes are being offered in the authorized denominations of $5,000 or any integral multiples thereof, at the rates shown on the inside cover page hereof. The Notes, when issued, will be registered in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), which will act as securities depository for the Notes. Purchasers will not receive certificates representing their ownership interest in the Notes purchased. So long as DTC or its nominee is the registered owner of the Notes, payments of the principal of and interest due on the Notes will be made directly to DTC.

Principal of and interest on the Notes will be paid directly to DTC by the Trustee.

It is expected that delivery of the 2006 A Notes and 2006 B Notes will be made on or about October 18, 2006.

It is expected that delivery of the 2007 A Notes will be made on or about November 1, 2007. See "CERTAIN FORWARD DELIVERY CONSIDERATIONS" herein.

Security

The Notes and the interest thereon are payable solely from payments of the Financing Payments (as defined herein) to be made by the University, as lessee of the Project (consisting of the Construction Project and the refunding of the Refunded Bonds), to the Commission, as lessor of the Project, under the Financing/Lease Agreement dated as of October 1, 2006 (the "Financing Agreement") among the Commission, the Commonwealth of Kentucky Finance and Administration Cabinet (the "Cabinet") and the University, and from the other sources described herein. The Commission has pledged to the payments of its obligations with respect to the Notes, the Financing Payments to be received from the University under the Financing Agreement. In addition, if the University fails to make timely payments under the Financing Agreement, the Secretary of the Cabinet is obligated, pursuant to KRS 164A.608, to apply to such payments, any funds that have been appropriated to the University that have not been disbursed.

See "SECURITY FOR THE NOTES" and "SUMMARY OF THE PRINCIPAL DOCUMENTS" herein.

The University has authorized and entered into a Trust Agreement dated as of November 1, 2005 (the "Trust Agreement"), under which it has pledged its General Receipts, as defined in the Trust Agreement, as security for the payment of Obligations, as defined in the Trust Agreement, issued thereunder. The Financing Agreement constitutes an Obligation within the meaning of the Trust Agreement. The University's obligations under the Financing Agreement are, therefore, secured by a pledge of the University's General Receipts. See "SECURITY FOR THE NOTES" and "APPENDIX B – SUMMARY OF THE TRUST AGREEMENT" herein.

THE NOTES ARE SPECIAL AND LIMITED OBLIGATIONS OF THE COMMISSION. THE NOTES DO NOT CONSTITUTE A DEBT, LIABILITY OR OBLIGATION OF THE COMMONWEALTH, OR A PLEDGE OF THE FULL FAITH AND CREDIT OR TAXING POWER OF THE COMMONWEALTH, BUT ARE PAYABLE SOLELY FROM AMOUNTS DEPOSITED IN CERTAIN FUNDS AND ACCOUNTS CREATED BY THE RESOLUTION AND FROM RENTAL INCOME DERIVED FROM A FINANCING AGREEMENT WITH THE UNIVERSITY.

Bond Insurance Policy

The scheduled payment of principal of and interest on the Series 2006 A Notes and the Series 2006 B Notes, when due, will be guaranteed under a Financial Guaranty Insurance Policy (the "2006 Bond Insurance Policy") to be issued concurrently with the delivery of the Series 2006 A Notes and the Series 2006 B Notes by Ambac Assurance Corporation (the "Bond Insurer"). The scheduled payment of principal of and interest on the Series 2007 A Notes, when due, will be guaranteed under a Financial Guaranty Insurance Policy (the "2007 Bond Insurance Policy" and, together with the 2006 Bond Insurance Policy, the "Bond Insurance Policies") to be issued concurrently with the delivery of the Series 2007 A Notes by the Bond Insurer.

Tax Status

In the opinion of Bond Counsel for the Notes, based upon an analysis of existing laws, regulations, rulings and court decisions, interest on the 2006 A Notes is, and interest on the 2007 A Notes would be, excludable from gross income for Federal income tax purposes. Bond Counsel for the Notes is also of the opinion that interest is not, in the case of the 2006 A Notes, and would not be, in the case of the 2007 A Notes, a specific item of tax preference under Section 57 of the Internal Revenue Code of 1986 (the "Code") for purposes of the Federal individual or corporate alternative minimum taxes. Interest on the 2006 B Notes is includable in gross income for Federal income tax purposes. Furthermore, Bond Counsel for the Notes is of the opinion that interest on the Notes is exempt from income taxation by the Commonwealth and the Notes are exempt from ad valorem taxation by the Commonwealth and any of its political subdivisions. See "TAX MATTERS" herein, and "APPENDIX F."

Continuing Disclosure	Rule 15c2-12 under the Securities and Exchange Act of 1934, as amended, generally prohibits an underwriter from purchasing or selling municipal securities in an initial offering unless it has determined that the issuer of such securities has committed to provide annually, certain information, including audited financial information and notice of various events, if material, to enable the purchaser to comply with the provisions of Rule 15c2-12.
General	The Official Statement speaks only as of its date, and the information contained herein is subject to change. All summaries of documents and agreements in the Official Statement are qualified in their entirety by reference to such documents and agreements, copies of which are available from the Office of Financial Management.
Information	Information regarding the Notes is available by contacting the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601 (502) 564-2924; or Office of the Treasurer, University of Kentucky, 301 Peterson Office Building, Lexington, Kentucky 40506 (859) 257-4758; or, during the initial offering period, the Underwriter, Morgan Stanley & Co. Incorporated, 2000 Westchester Avenue, Purchase, New York 10577 (914) 225-0203.

OFFICIAL STATEMENT

$146,430,000
COMMONWEALTH OF KENTUCKY
KENTUCKY ASSET/LIABILITY COMMISSION
UNIVERSITY OF KENTUCKY GENERAL RECEIPTS PROJECT NOTES

Consisting of

$66,305,000 GENERAL RECEIPTS REFUNDING PROJECT NOTES, 2006 SERIES A	$2,220,000 GENERAL RECEIPTS TAXABLE REFUNDING PROJECT NOTES, 2006 SERIES B	$77,905,000 GENERAL RECEIPTS PROJECT NOTES, 2007 SERIES A

INTRODUCTION

This Official Statement (the "Official Statement"), which includes the cover page, is being distributed by the Kentucky Asset/Liability Commission (the "Commission"), an independent agency of the Commonwealth of Kentucky (the "Commonwealth"), to furnish pertinent information to the purchasers of $146,430,000 aggregate principal amount of its University of Kentucky General Receipts Project Notes, consisting of $66,305,000 General Receipts Refunding Project Notes, 2006 Series A (the "2006 A Notes"), $2,220,000 University of Kentucky General Receipts Taxable Refunding Project Notes, 2006 Series B (the "2006 B Notes" and, together with the 2006 A Notes, the "2006 Notes") and $77,905,000 General Receipts Project Notes, 2007 Series A Notes (the "2007 A Notes" and collectively, the "Notes"). The Notes are being issued pursuant to Section 56.860 *et seq.* of the Kentucky Revised Statutes (the "Act"), a Resolution adopted by the Commission on September 18, 2006 (the "Resolution"), and a Trust Indenture dated as of October 1, 2006 (the "Indenture"), between the Commission and U.S. Bank National Association having offices in Atlanta, Georgia, as trustee and paying agent (the "Trustee" and "Paying Agent").

The proceeds of the Notes will be used to (i) provide financing for the Project (as defined and described herein), (ii) pay the interest coming due on the 2007 A Notes through and including October 1, 2009, (iii) refund certain bonds previously issued by the University, (iv) refund certain bonds previously issued by the State Property and Buildings Commission to finance facilities for the University, and (v) pay the costs of issuing the Notes. See "REFUNDING PLAN" and "THE CONSTRUCTION PROJECT" herein.

The Notes and the interest thereon are payable solely from payments of the Financing Payments (as defined herein) to be made by the University of Kentucky (the "University") to the Commission under the Financing/Lease Agreement dated as of October 1, 2006 (the "Financing Agreement") among the Commission, the Commonwealth of Kentucky Finance and Administration Cabinet (the "Cabinet") and the University. The Notes are also secured by certain other funds and accounts pledged therefor and described herein. In addition, if the University fails to make timely payments under the Financing Agreement, the Secretary of the Cabinet is obligated, pursuant to KRS 164A.608, to apply to such payments, any funds that have been appropriated to the University that have not been disbursed. See "SECURITY FOR THE NOTES" herein.

The University has authorized and entered into a Trust Agreement dated as of November 1, 2005 (the "Trust Agreement"), under which it has pledged its General Receipts, as defined in the Trust Agreement, as security for the payment of Obligations, as defined in the Trust Agreement, issued thereunder. The Financing Agreement constitutes an Obligation within the meaning of the Trust Agreement. The University's obligations under the Financing Agreement are, therefore, secured by a pledge of the University's General Receipts. See "SECURITY FOR THE NOTES" and "APPENDIX B – SUMMARY OF THE TRUST AGREEMENT" herein.

The scheduled payment of the principal of and interest on the Series 2006 A Notes and the Series 2006 B Notes, when due, will be guaranteed under a Financial Guaranty Insurance Policy (the "2006 Bond Insurance Policy") to be issued concurrently with the delivery of the Series 2006 A Notes and the Series 2006 B Notes by Ambac Assurance Corporation (the "Bond Insurer"). The scheduled payment of the principal of and interest on the Series 2007 A Notes, when due, will be guaranteed under a Financial Guaranty Insurance Policy (the "2007 Bond Insurance Policy" and, together with the 2006 Bond Insurance Policy, the "Bond Insurance Policies") to be issued concurrently with the delivery of the Series 2007 A Notes by the Bond Insurer.

The summaries and references to the Act, the Trust Agreement, the Indenture, the Financing Agreement described herein, and the Notes included in this Official Statement do not purport to be comprehensive or definitive, and such summaries and references are qualified in their entirety by reference to each such document, copies of which are available for inspection at the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601 (502) 564-2924; or Office of the Treasurer, University of Kentucky, 301 Peterson Office Building, Lexington, Kentucky 40506 (859) 257-4758; or, during the initial offering period, the Underwriter, Morgan Stanley & Co. Incorporated, 2000 Westchester Avenue, Purchase, New York 10577 (914) 225-0203, the underwriter of the Notes (the "Underwriter").

Capitalized terms used in this Official Statement and not otherwise defined will have the meanings given them under the caption "SUMMARY OF THE PRINCIPAL DOCUMENTS - Definitions" herein and in "APPENDIX B."

THE NOTES

General

The Notes are issuable only as fully registered Notes. The 2006 A Notes and 2006 B Notes will be issuable in the denominations of $5,000 or any integral multiples thereof, will be dated as of their date of delivery, will bear interest payable on each April 1 and October 1, commencing April 1, 2007, at the rates set forth on the inside cover page of this Official Statement and will mature on the dates set forth on the inside cover page of this Official Statement. The 2007 A Notes will be issuable in the denominations of $5,000 or any integral multiples thereof, will be dated as of their date of delivery, will bear interest payable on each April 1 and October 1, commencing April 1, 2008, at the rates set forth on the inside cover page of this Official Statement and will mature on the dates set forth on the inside cover page of this Official Statement. Principal of and interest on the Notes are payable in lawful money of the United States to the registered owner of the Notes, Cede & Co., as nominee of The Depository Trust Company ("DTC") in New York, New York, pursuant to the global book-entry system operated by DTC. See "APPENDIX E – Book-Entry-Only System."

Optional Redemption

The 2006 Notes maturing on or before October 1, 2016 are not subject to optional redemption prior to maturity. The 2006 Notes maturing after October 1, 2016 are subject to redemption at the option of the Commission on or after October 1, 2016, in whole or in part at any time, at a redemption price equal to 100% of the principal amount of the 2006 Notes to be redeemed, plus accrued interest to the date fixed for redemption. The 2007 A Notes maturing on or before October 1, 2017 are not subject to optional redemption prior to maturity. The 2007 A Notes maturing after October 1, 2017 are subject to redemption at the option of the Commission on or after October 1, 2017, in whole or in part at any time, at a redemption price equal to 100% of the principal amount of the 2007 A Notes to be redeemed, plus accrued interest to the date fixed for redemption.

Book-Entry-Only System

The Notes initially will be issued solely in book-entry form to be held in the book-entry-only system maintained by DTC. So long as such book-entry system is used, only DTC will receive or have the right to receive physical delivery of the Notes and, except as otherwise provided herein with respect to tenders by Beneficial Owners of Beneficial Ownership Interests, each as hereinafter defined, Beneficial Owners will not be or be considered to be, and will not have any rights as, owners or holders of the Notes under the Indenture. For additional information about DTC and the book-entry-only system see "APPENDIX E – Book-Entry-Only System."

Authorization

The University, at a meeting held on September 12, 2006, adopted resolutions, which, among other things, authorized the Financing Agreement.

The Commission, at a meeting held on September 18, 2006, adopted the Resolution, which, among other things (i) authorized the Indenture, (ii) authorized and approved the issuance of the Notes, subject to approval by a representative of the Office of Financial Management ("OFM") acting as authorized officer of the Commission (the "Authorized Officer"), (iii) authorized the Financing Agreement and (iv) directed the preparation and distribution of this Official Statement.

The State Property and Buildings Commission of the Commonwealth also has approved the issuance of the Notes.

SECURITY FOR THE NOTES

General

The Notes and the interest thereon are payable solely from payments of the Financing Payments to be made by the University, as lessee of the Project, to the Commission, as lessor of the Project, under the Financing Agreement and from other sources described under this heading.

The University, as lessee, has entered into the Financing Agreement with the Commission and the Cabinet in order to provide the Commission, as lessor, with amounts to pay the principal of and interest on the Notes as they become due. The Commission has pledged to the payments of its obligations with respect to the Notes, the Financing Payments to be received from the University under the Financing Agreement. The University has pledged its General Receipts as security for its payment obligations under the Financing Agreement.

Budgetary Process in the Commonwealth

The General Assembly is required by the Kentucky Constitution to adopt measures providing for the Commonwealth's revenues and appropriations for each fiscal year. The Governor is required by law to submit a biennial State Budget (the "State Budget") to the General Assembly during the legislative session held in each even numbered year. State Budgets have generally been adopted by the General Assembly during those legislative sessions, which end in mid-April, to be effective upon the Governor's signature for appropriations commencing for a two-year period beginning the following July 1.

Although the University is required to submit its budgets to the General Assembly for approval as a part of the State Budget, the pledge of General Receipts by the University described herein is not subject to appropriation. However, the funds of the University that are subject to intercept (see “SECURITY FOR THE NOTES - **State Intercept**”) are funds that are appropriated to the University.

Pledge of General Receipts

In the Financing Agreement, which is an "Obligation" under the Trust Agreement, the University has pledged its General Receipts as security for its payment obligations thereunder.

"General Receipts" means, as reported in the Financial Statements of the University (having the designations, to the extent not otherwise defined in the Trust Agreement, set forth in the Financial Statements or such successor designations that may hereafter be used in Financial Statements):

(a) certain operating and non-operating revenues of the University, being (i) Student Registration Fees, (ii) nongovernmental grants and contracts, (iii) recoveries of facilities and administrative costs, (iv) sales and services, (v) Hospital Revenues, (vi) Housing and Dining Revenues, (vii) auxiliary enterprises – other auxiliaries, (viii) other operating revenues, (ix) state appropriations (for general operations), (x) gifts and grants, (xi) investment income, (xii) other nonoperating revenues and (xiii) other;

(b) but excluding (i) any receipts described in clause (a) which are contracts, grants, gifts, donations or pledges and receipts therefrom which, under restrictions imposed in such contracts, grants, gifts, donations or pledges, or, which as a condition of the receipt thereof or of amounts payable thereunder are not available for payment of Debt Service Charges, (ii) federal grants and contracts, (iii) state and local grants and contracts, (iv) federal appropriations, (v) county appropriations, (vi) professional clinical service fees, (vii) auxiliary enterprises – athletics; (viii) capital appropriations, (ix) capital grants and gifts, and (x) additions to permanent endowments, including research challenge trust funds;

provided, however, that General Receipts may

(c) include any other receipts that may be designated as General Receipts from time to time by a resolution of the board of the University delivered to the Trustee; and

(d) exclude any receipts not heretofore pledged, which may be designated from time to time by a resolution of the board of the University delivered to the Trustee;

(e) exclude any receipts heretofore pledged, which may be designated from time to time by a resolution of the board of the University delivered to the Trustee and each Rating Service then rating any Obligations, but only if each such Rating Service confirms in writing to the University that the exclusion of any such receipt would not cause a reduction or withdrawal of the then current rating on any Outstanding Obligations.

The University has outstanding, certain Consolidated Educational Buildings Revenue Bonds (the "Building Bonds") and certain Housing and Dining System Revenue Bonds (the "Housing Bonds"), to which General Receipts described in (a)(i) and (a)(vi) above are respectively pledged on a priority basis to the pledge of those General Receipts under the Trust Agreement. The University has covenanted not to issue any additional Building Bonds. The prior pledge of those General Receipts securing Building Bonds will terminate when there are no Building Bonds outstanding. See "APPENDIX A" for information regarding outstanding Building Bonds. The prior pledge of certain General Receipts securing Housing Bonds will terminate when there are no outstanding Housing Bonds that were outstanding as of the date of the Trust Agreement, which will be the case upon the issuance of the Notes and the defeasance of the Refunded Housing and Dining Bonds. There are currently no other Obligations outstanding under the Trust Agreement other than the University's $7,160,000 General Receipts Bonds, 2005 Series A, the University's obligations related to the Commission's $107,540,000 University of Kentucky General Receipts Project Notes, 2005 Series A and the University's $24,325,000 General Receipts Bonds (Student Health Facility Project), 2006 Series A.

State Intercept

If the University fails to make timely payments under the Financing Agreement, the Secretary of the Cabinet is obligated, pursuant to KRS 164A.608, to apply to such payments, any funds that have been appropriated to the University that have not yet been disbursed. Payments under the Financing Agreement are required to be deposited with the Trustee at least ten days prior to the corresponding due date for a payment of any debt service on the Notes. If the amount required to pay debt service is not on deposit by that date, the Trustee is obligated under the Indenture to immediately notify the Secretary of the Cabinet of the default in payment. Under KRS 164A.608, the Secretary of the Cabinet is required, within five days of the default, to remit the amount required to pay debt service to the Trustee from undisbursed funds which have been appropriated to the University.

Additional Obligations

The University has reserved the right to issue additional Obligations secured by a pledge of General Receipts. See "APPENDIX B". Those Obligations may be in the form of financing agreements related to the future issuance of notes by the Commission for the University.

Bond Insurance

The scheduled payment of the principal of and interest on the Series 2006 Notes, when due, will be guaranteed under the 2006 Bond Insurance Policy to be issued concurrently with the delivery of the Series 2006 Notes by the Bond Insurer. The scheduled payment of the principal of and interest on the Series 2007 A Notes, when due, will be guaranteed under the 2007 Bond Insurance Policy to be issued concurrently with the delivery of the Series 2007 A Notes by the Bond Insurer. See “BOND INSURANCE” and “APPENDIX G.”

BOND INSURANCE

The Bond Insurer has supplied the following information for inclusion in this Official Statement. No representation is made by the Commission, the University or the underwriters as to the accuracy or completeness of this information. Reference is made to “APPENDIX G” for a specimen of the Bond Insurance Policies.

Payment Pursuant to Financial Guaranty Insurance Policy

The Bond Insurer has made a commitment to issue a financial guaranty insurance policy (the “2006 Bond Insurance Policy”) relating to the Series 2006 A Notes and the Series 2006 B Notes effective as of the date of issuance of the Series 2006 A Notes and the Series 2006 B Notes. The Bond Insurer also has made a commitment to issue a financial guaranty insurance policy (the “2007 Bond Insurance Policy”) relating to the Series 2007 A Notes to be delivered and effective as of the date of issuance of the Series 2007 A Notes. The 2006 Bond Insurance Policy and the 2007 Bond Insurance Policy are separate obligations of the Bond Insurer insuring payments on the 2006 Notes and the 2007 A Notes, respectively. Under the terms of the Bond Insurance Policies, the Bond Insurer will pay to The Bank of New York, in New York, New York or any successor thereto (the “Insurance Trustee”) that portion of the principal of and interest on the Notes which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Commission. The Bond Insurer will make such payments to the Insurance Trustee on the later of the date on which such principal and interest becomes Due for Payment or within one business day following the date on which the Bond Insurer shall have received notice of Nonpayment from the Trustee. The insurance will extend for the term of the Notes and, once issued, cannot be canceled by the Bond Insurer.

The Bond Insurance Policies will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Notes become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Notes, the Bond Insurer will remain obligated to pay principal of and interest on outstanding

Notes on the originally scheduled interest and principal payment dates including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Notes, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration, except to the extent that the Bond Insurer elects, in its sole discretion, to pay all or a portion of the accelerated principal and interest accrued thereon to the date of acceleration (to the extent unpaid by the Commission). Upon payment of all such accelerated principal and interest accrued to the acceleration date, the Bond Insurer's obligations under the Bond Insurance Policies shall be fully discharged.

In the event the Trustee has notice that any payment of principal of or interest on a Note which has become Due for Payment and which is made to a Holder by or on behalf of the Commission has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from the Bond Insurer to the extent of such recovery if sufficient funds are not otherwise available.

The Bond Insurance Policies do **not** insure any risk other than Nonpayment, as defined in the Policies. Specifically, the Bond Insurance Policies do **not** cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity.
2. payment of any redemption, prepayment or acceleration premium.
3. nonpayment of principal or interest caused by the insolvency or negligence of any Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Bond Insurance Policies, payment of principal requires surrender of Notes to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Notes to be registered in the name of the Bond Insurer to the extent of the payment under the Bond Insurance Policies. Payment of interest pursuant to the Bond Insurance Policies requires proof of Holder entitlement to interest payments and an appropriate assignment of the Holder’s right to payment to the Bond Insurer.

Upon payment of the insurance benefits, the Bond Insurer will become the owner of the Note, appurtenant coupon, if any, or right to payment of principal or interest on such Note and will be fully subrogated to the surrendering Holder’s rights to payment.

Ambac Assurance Corporation

The Bond Insurer is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin and licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately $9,599,000,000 (unaudited) and statutory capital of approximately $6,000,000,000 (unaudited) as of June 30, 2006. Statutory capital consists of the Bond Insurer’s policyholders’ surplus and statutory contingency reserve. Standard & Poor’s Credit Markets Services, a Division of The McGraw-Hill Companies, Moody’s Investors Service and Fitch Ratings have each assigned a triple-A financial strength rating to the Bond Insurer.

The Bond Insurer has obtained a ruling from the Internal Revenue Service to the effect that the insuring of a note by the Bond Insurer will not affect the treatment for federal income tax purposes of interest on such note and that insurance proceeds representing maturing interest paid by the Bond Insurer under policy provisions substantially identical to those contained in its financial guaranty insurance policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Commission on the Notes.

The Bond Insurer makes no representation regarding the Notes or the advisability of investing in the Notes and makes no representation regarding, nor has it participated in the preparation of, the Official Statement other than the information supplied by the Bond Insurer and presented under the heading "BOND INSURANCE."

Available Information

The parent company of the Bond Insurer, Ambac Financial Group, Inc. (the "Ambac Financial"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be read and copied at the SEC's public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The SEC maintains an internet site at http://www.sec.gov that contains reports, proxy and information statements and other information regarding companies that file electronically with the SEC, including Ambac Financial. These reports, proxy statements and other information can also be read at the offices of the New York Stock Exchange, Inc. (the "NYSE"), 20 Broad Street, New York, New York 10005.

Copies of the Bond Insurer's financial statements prepared in accordance with statutory accounting standards are available from the Bond Insurer. The address of the Bond Insurer's administrative offices and its telephone number are One State Street Plaza, 19th Floor, New York, New York 10004 and (212) 668-0340.

Incorporation of Certain Documents by Reference

The following documents filed by Ambac Financial with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

1. Ambac Financial's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and filed on March 13, 2006;
2. Ambac Financial's Current Report on Form 8-K dated and filed on April 26, 2006;
3. Ambac Financial's Quarterly Report on Form 10-Q for the fiscal quarterly period ended March 31, 2006 and filed on May 10, 2006;
4. Ambac Financial's Current Report on Form 8-K dated July 25, 2006 and filed on July 26, 2006;
5. Ambac Financial's Current Report on Form 8-K dated and filed on July 26, 2006; and
6. Ambac Financial's Quarterly Report on Form 10-Q for the fiscal quarterly period ended June 30, 2006 and filed on August 9, 2006.

All documents subsequently filed by Ambac Financial pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in **"Available Information".**

REFUNDING PLAN

The 2006 A Notes are being issued to refund the Refunded Series K Housing and Dining Bonds, Refunded Series N Housing and Dining Bonds, Refunded Series P Housing and Dining Bonds, Refunded Series Q Housing and Dining Bonds, Refunded Series R Housing and Dining Bonds, Refunded Series S Housing and Dining Bonds and the Refunded SPBC Bonds and to pay costs of issuance of the Notes. The Refunded Series K Housing and Dining Bonds, Refunded Series N Housing and Dining Bonds, Refunded Series P Housing and Dining Bonds, Refunded Series Q Housing and Dining Bonds, Refunded Series R Housing and Dining Bonds and Refunded Series S Housing and Dining Bonds were issued to finance or refinance the cost of renovating and completing buildings for housing purposes at the

University. The Refunded SPBC Bonds were issued to finance a building located in Paducah, Kentucky and the remaining portion of a building located in Lexington, Kentucky. Proceeds of the 2006 A Notes will be deposited in the Escrow Fund to provide for the refunding and redemption of each series of the Refunded Bonds to be refunded by the 2006 A Notes. Separate escrow accounts will be established for (i) the Refunded SPBC Bonds and (ii) for the other Refunded Bonds to be refunded by the 2006 A Notes.

The 2006 B Notes are being issued to refund the Refunded Series M and O Housing and Dining Bonds, and Refunded Series P and Q Housing and Dining Bonds and to pay costs of issuance of the Notes. The Refunded Series M and O Housing and Dining Bonds and the Refunded Series P and Q Housing and Dining Bonds were issued to finance or refinance the cost of renovating and completing buildings for housing purposes at the University. Proceeds of the 2006 B Notes will be deposited in the Escrow Fund to provide for the refunding and redemption of each series of the Refunded Bonds. A separate escrow account will be established for the Refunded Bonds to be refunded by the 2006 B Notes.

THE CONSTRUCTION PROJECT

The 2007 A Notes are being issued to pay a portion of the costs of the Construction Project and costs of issuance of the Notes, and pay interest on the 2007 A Notes to and including October 1, 2009.

The Construction Project entails an expansion of and limited renovation to the existing University Hospital, situated adjacent to the existing Hospital Critical Care Center and the Gill Heart Institute, and the addition of a parking structure and overhead concourse (bridge) connector to the new addition.

In general the Construction Project is to contain the following:

1. Hospital Expansion of approximately 1,000,000 gross square feet of building space, with 490,000 square feet to be occupied space of various hospital program elements. An additional 532,000 square feet will be shelled for future program interior fit-up. Program elements include: a new acute care Nursing Unit (152 private patient room beds configured as a 24 bed ICU and four 32-bed med/surg nursing units); admitting and related support space, linking the new and existing Hospital buildings; 2-MRI Imaging units in one suite; new Emergency Services department with new CT Scan and two R/F X-Ray suites; shell space for new Diagnostic and Treatment Department; new lobby and entrance with related amenities; new Food Services department; new surgery area containing 8 operating room suites; new same day surgery intake and stage two recovery areas; new Central Sterile Supply department; and a new helipad on the roof to access the new Emergency Services Department.

2. Parking Structure containing space for approximately 1,600 cars. (The Parking Structure is expected to be completed in 2007.)

3. Bridge concourse over South Limestone Street connecting the new parking structure and new hospital expansion. The estimated size is 20 feet in width and 250 feet in length. The juncture of the concourse to the garage will utilize any available space at street level and the concourse level for retail spaces, designed as shell only for future tenant fit-out.

4. Infrastructure expansion to the University's heating and cooling piping loops to include one (1-100,000 BTU/HR) new boiler and four new 2,500 ton chillers.

5. Renovation of existing Critical Care Center and Gill Heart Institute buildings, to interface with the new hospital expansion for operational efficiencies. Renovation is limited to construction required to make new building connections.

6. New entrance drive to support new Hospital Public and Visitor entrance and site improvements for Emergency Services entrance.

The Regular Sessions of the 2005 and 2006 Kentucky General Assemblies authorized $100 million and $150 million, respectively, of bonds for the Construction Project, as well as $100 million and $25 million of University funds.

ESTIMATED SOURCES AND USES OF FUNDS

The estimated sources and uses of funds are to be applied as follows:

Sources	2006 A Notes	2006 B Notes	2007 A Notes	Total
Par Amount of Notes	$66,305,000.00	$2,220,000.00	$77,905,000.00	$146,430,000.00
Net Premium	1,700,930.80	199.80	4,890,544.80	6,591,675.40
Other Funds Provided by the University	5,794,463.85	7,645,556.33	0.00	13,440,020.18
Total Sources	$73,800,394.65	$9,865,756.13	$82,795,544.80	$166,461,695.58
Uses				
Deposit to Project Fund	$0.00	$0.00	$75,000,000.00	$75,000,000.00
Deposit to Note Payment Fund (capitalized interest)	0.00	0.00	7,113,232.65	7,113,232.65
Deposit to Escrow Fund	73,250,801.07	9,856,478.48	0.00	83,107,279.55
Costs of Issuance [1]	549,593.58	9,277.65	682,312.15	1,241,183.38
Total Uses	$73,800,394.65	$9,865,756.13	$82,795,544.80	$166,461,695.58

[1] Includes underwriters' discount, bond insurance premium, legal fees, rating agency fees, printing, and other costs of issuance

THE UNIVERSITY

The University is a comprehensive, land-grant institution located in Lexington (Fayette County), Kentucky. Founded in 1865 under the provisions of the Morrill Land-Grant Act, the University began as part of Kentucky University. In 1878, the Agricultural and Mechanical College was separated from Kentucky University and reestablished on land given by Lexington and Fayette County. To provide a separate campus for the new institution, Lexington donated its 50-acre fairground and park and, along with Fayette County, contributed construction of the buildings. Thirty years later the name was changed to State University, Lexington, Kentucky, and in 1916 it became the University of Kentucky.

The University is organized into sixteen colleges and graduate schools plus extension programs, and is located in Lexington, Kentucky. From an enrollment of 273 students in 1876, the University has grown to over 27,000 students and more than 11,000 faculty and staff. The campus today has more than 100 major buildings including not only modern teaching and research facilities, but also renovated history-laden structures dating back to the 1800's. The University has produced two Nobel Laureates and seven governors of the Commonwealth including the first female governor. Scientific advances in medicine, energy, equine and other fields of research have caused the University to be ranked among the top 100 research universities in the nation, the only university in Kentucky to be so recognized.

Additional information regarding the University is set forth in "APPENDIX A."

THE KENTUCKY ASSET/LIABILITY COMMISSION

General Information

The Act created the Kentucky Asset/Liability Commission, which is composed of five members, each serving in an ex officio capacity. Under the Act, the members are as follows: the Secretary of the Finance and Administration Cabinet, who acts as Chairman; the Attorney General; the State Treasurer; the State Budget Director; and the State Controller. The State Controller was added to the Commission by Executive Order 2006-679 dated June 19, 2006 and effective June 16, 2006.

The current members of the Commission are as follows:

John R. Farris	Secretary of the Finance and Administration Cabinet, Chairman
Gregory D. Stumbo	Attorney General
Jonathan Miller	State Treasurer
Bradford L. Cowgill	State Budget Director
Ed C. Ross	State Controller

The Secretary to the Commission is the Executive Director of OFM.

The Commission was created by the General Assembly to develop policies and strategies to minimize the impact of fluctuating interest rates on the Commonwealth's interest-sensitive assets and interest-sensitive liabilities. The Commission is authorized to issue tax and revenue anticipation notes, project notes and funding notes. Tax and revenue anticipation notes are to be used for the purpose of providing monies to discharge expenditure demands in anticipation of revenues and taxes to be collected during the fiscal year. Project notes are to be used for authorized projects upon request of the Finance and Administration Cabinet, to be repaid through financing agreements or alternative agreements. Funding notes are to be used for the purpose of funding judgments against the Commonwealth or any state agency. OFM, which is in the Finance and Administration Cabinet, serves as staff to the Commission.

Financings of the Commission

Information regarding outstanding notes of the Commission is included in "APPENDIX D" under the heading "Financings of the Commission."

THE FINANCE AND ADMINISTRATION CABINET

The Cabinet, created and governed by the provisions of KRS 12.020 and KRS 42.011, is a statutory administrative organization of the Commonwealth headed by the Secretary of the Cabinet, who is appointed by the Governor. The Secretary of the Cabinet is the chief financial officer of the Commonwealth.

Senate Bill 49 of the 2005 General Assembly reorganized the Finance and Administration Cabinet to assume the responsibilities of the former Revenue Cabinet and the Governor's Office of Technology. In addition to the newly assumed responsibilities, Cabinet functions include, (1) coordination and supervision of the fiscal affairs and fiscal procedures of the Commonwealth; (2) accounting, fiscal reporting and auditing of Commonwealth accounts; (3) purchasing, storekeeping and control of property and stores; (4) the construction, maintenance and operation of public buildings, except those provided for the exclusive use of certain agencies; (5) providing administrative services of a financial nature to other agencies of state government; (6) the investment and management of all Commonwealth funds other than pension funds; and (7) oversight of the issuance and management of all debt incurred in the name of the Commonwealth or any agency thereof.

Under the Act, the Cabinet is required to be a party to the Financing Agreement.

THE COMMONWEALTH

The Commonwealth of Kentucky, nicknamed the Bluegrass State, was the first state west of the Alleghenies to be settled by pioneers. Kentucky is bounded by the Ohio River to the north and the Mississippi River to the west, and is bordered by the States of Illinois, Indiana, Ohio, West Virginia, Tennessee, Missouri and the Commonwealth of Virginia.

The Commonwealth's economy in many ways resembles a scaled-down version of the U.S. economy in its diversity. The Kentucky economy, once dominated by coal, horses, bourbon and tobacco has become a diversified modern economy including manufacturing of industrial machinery, automobiles and automobile parts and consumer appliances. In addition, Kentucky's nonmanufacturing industries have grown considerably in recent years, with strong gains in air transportation, health and business services, and retail trade. The Commonwealth's parks, horse breeding and racing industry, symbolized by the Kentucky Derby, play an important role in expanding the tourism industry in the Commonwealth.

Additional information regarding the Commonwealth is set forth in "APPENDIX D."

SUMMARY OF THE PRINCIPAL DOCUMENTS

Summarized below are certain provisions of the Indenture and the Financing Agreement. This summary does not purport to be complete, and is qualified by reference to the Indenture and the Financing Agreement. UNDER THE FINANCING AGREEMENT, THE UNIVERSITY HAS PLEDGED ITS GENERAL RECEIPTS. A SUMMARY OF THE PROVISIONS OF THE TRUST AGREEMENT UNDER WHICH THE FINANCING AGREEMENT WAS ISSUED IS INCLUDED IN APPENDIX B.

Definitions

Set forth below are the definitions of some of the terms used in this Official Statement, the Indenture and the Financing Agreement. Reference is made to the Indenture and the Financing Agreement for a complete recital of the terms defined therein.

"Act" means Section 56.860 et seq. of the Kentucky Revised Statutes, as amended.

"Additional Notes" means notes issued under the provisions of Section 2.06(a) of the Indenture.

"Additional Payments" means the Additional Payments payable under the Financing Agreement.

"Authorized Denominations" means $5,000 and integral multiples thereof.

"Authorized Officer" means, as to the Cabinet or the Commission, the Executive Director of the Office of Financial Management and any other officer, member or employee of the Office of Financial Management authorized by a certificate of the Executive Officer to perform the act or sign the document in question, and if there is no such authorization, means the Executive Officer and as to the University, its Treasurer and any other officer, member or employee of the University authorized by a certificate of the Chairman or Secretary of the Board of Trustees of the University to perform the act or sign the document in question.

"Budget Act" means House Bill 380 as enacted and vetoed in part of the General Assembly of the Commonwealth of Kentucky, 2006 Regular Session.

"Business Day" means any day other than (i) a day on which the Trustee or the Paying Agent is required, or is authorized or not prohibited, by law (including executive orders) to close and is closed and (ii) a day on which the New York Stock Exchange is closed.

"Cabinet" means the Finance and Administration Cabinet of the Commonwealth.

"Commission" means the Kentucky Asset/Liability Commission.

"Construction Project" means the Patient Care Facility Phase II – Hospital, authorized for the University by the Budget Act and described in the Financing Agreement.

"Cost of Issuance Fund" means the Fund so designated which is established and created by Sections 5.03 and 5.04 of the Indenture.

"Costs of Issuance" means only the costs of issuing Notes as designated by the Commission; including, but not being limited to, the fees and charges of the financial advisors or Underwriter, bond counsel, Trustee, Trustee's counsel, rating agencies, note and official statement printers and such other fees and expenses normally attendant to an issue of the Notes.

"Counsel" or "Counsel's Opinion" means an opinion signed by such attorney or firm of attorneys of recognized national standing in the field of law relating to municipal bonds and municipal finance as may be selected by the Commission.

"Debt Servicing Date" means any Interest Payment Date, as defined herein.

"Debt Servicing Obligation" means the aggregate amounts required to be paid in respect of the Notes on any Debt Servicing Date, including (i) the scheduled maturity of principal of any Notes maturing on such Debt Servicing Date and the principal amount of Notes, if any, called for redemption on such Debt Servicing Date, and the premium, if any, with respect to such Notes, (ii) the interest required or estimated (by the Commission) to be paid on the Notes, and (iii) the reasonable and agreed fees of the Trustee, the Paying Agent and the Registrar, but only to the extent not otherwise paid directly by the University. The University shall be entitled to a credit against the Debt Servicing Obligation otherwise required to be paid on any Debt Servicing Date to the extent there are funds in the Interest Account of the Note Payment Fund prior to the payment of the Debt Servicing Obligation hereunder which, under the terms of the Indenture and applicable law, can be used to meet the Debt Servicing Obligation. It is understood that, pursuant to the Indenture, all income derived from investment of the Project Fund may, at the discretion of the University, be transferred to the Note Payment Fund and, if so transferred, shall be a credit against Financing Payments due and payable by the University. Amounts transferred from the Cost of Issuance Fund, established by the Indenture, to the Note Payment Fund, shall be a further credit against Financing Payments due and payable by the University.

"Eligible Investments" means any investment authorized by Section 42.500 of the Kentucky Revised Statutes, as the same may be amended from time to time.

"Escrow Agreement" means the Escrow Agreement dated as of October 1, 2006 between the commission and U.S. Bank National Association, as escrow trustee.

"Escrow Fund" means the Escrow Fund established under the Escrow Agreement.

"Executive Officer" means the Chairman of the Commission.

"Fiduciary" or "Fiduciaries" means the Trustee, any Paying Agent or Agents, or any combination of them, as may be appropriate.

"Financing Agreement" means the Financing/Lease Agreement, dated as of October 1, 2006 among the Commission, the Cabinet and the University by which the Project is leased to the University, and any amendments or supplements thereto.

"Financing Payments" means Financing Payments payable under the Financing Agreement.

"Fitch" means Fitch Ratings.

"Funds and Accounts" means the Cost of Issuance Fund, Note Payment Fund, Project Fund and Rebate Fund and the accounts within such funds established by the Trust Indenture.

"Holder" or "Owner" or any similar term (when used with reference to Notes) means the person in whose name a Note is registered.

"Indenture" or "Trust Indenture" means the Indenture, dated as of October 1, 2006, and entered into between the Commission and the Trustee, as amended or supplemented from time to time.

"Interest Accounts" means the accounts by that name in the Note Payment Fund established under the Indenture.

"Interest Payment Date" means each April 1 and October 1, commencing April 1, 2007 with respect to the 2006 A Notes and 2006 B Notes and commencing April 1, 2008 with respect to the 2007 A Notes.

"Memorandum of Instructions" means a Memorandum of Instructions Regarding Rebate which may be delivered to the Commission and the Trustee at the time of the issuance and delivery of the Notes, as the same may be amended or supplemented in accordance with its terms.

"Moody's" means Moody's Investors Service, Inc.

"Note Payment Fund" means the Fund so designated which is established and created by Sections 5.03 and 5.05 of the Indenture.

"Notes" means the 2006 A Notes, the 2006 B Notes and the 2007 A Notes, collectively.

"Outstanding" when used with reference to Notes, means, as of any date, all Notes theretofore or then being authenticated and delivered under the Indenture except:

(a) Notes cancelled upon surrender, exchange or transfer or cancelled because of payment or redemption at or prior to such date;

(b) Notes for the payment, redemption or purchase for cancellation of which sufficient moneys have been deposited and credited for the purpose on or prior to that date in the Note Payment Fund (whether upon or prior to the maturity or Redemption Date of those Notes); provided that if any of those Notes are to be redeemed prior to their maturity, notice of that redemption shall have been given or arrangements satisfactory to the Trustee shall have been made for giving notice of that redemption, or waiver by the affected Noteholders of that notice satisfactory in form to the Trustee shall have been filed with the Trustee, and provided further that if any of those Notes are to be purchased for cancellation a firm offer for sale stating the price shall have been received and accepted;

(c) Notes which are deemed to have been paid pursuant to the provisions of Article IX of the Indenture or any Notes which are deemed to have been paid pursuant to the provisions of the Indenture; and

(d) Notes in lieu of which others have been authenticated under Sections 3.07, 3.08 and 3.11 of the Indenture.

"Paying Agent" means initially, the Trustee, and any bank or trust company so designated, and its successor or successors hereafter appointed, as paying agent for the Notes in the manner provided in the Indenture.

"Pledged Receipts" include:

(i) all of the Financing Payments and Additional Payments, as defined in the Financing Agreement, to be paid by the University to the Commission pursuant to the Financing Agreement; and

(ii) all interest earned and gains realized on Eligible Investments (a) except for earnings and gains on any investments in the Rebate Fund and (b) unless this Trust Indenture specifically requires such interest earned or gains realized to remain in a particular Fund or Account and does not therefore constitute a Pledged Receipt.

"Principal Accounts" means the accounts by that name in the Note Payment Fund established under Section 5.05 of the Indenture.

"Project" means the Construction Project and the refunding of the Refunded Bonds.

"Project Fund" means the Project Fund created by Sections 5.03 and 5.06 of the Indenture.

"Rating Service" means Moody's, if Moody's is then rating the Notes, S&P, if S&P is then rating the Notes, and Fitch, if Fitch is then rating the Notes, and their respective successors and assigns.

"Rebate Fund" means a fund by that name established pursuant to Sections 5.03 and 5.07 of the Indenture.

"Record Date" means the first day of the month next preceding the applicable Interest Payment Date.

"Redemption Date" means the date established for the redemption of Notes as described under the heading "THE NOTES – Optional Redemption."

"Refunded Bonds" means the Refunded Housing and Dining Bonds and the Refunded SPBC Bonds.

"Refunded Housing and Dining Bonds" means the Refunded Series K Housing and Dining Bonds, Refunded Series N Housing and Dining Bonds, Refunded Series P Housing and Dining Bonds, Refunded Series Q Housing and Dining Bonds, Refunded Series R Housing and Dining Bonds, Refunded Series S Housing and Dining Bonds, Refunded Series M and O Housing and Dining Bonds, Refunded Series P and Q Housing and Dining Bonds and Refunded SPBC Bonds.

"Refunded Series K Housing and Dining Bonds" means University of Kentucky Housing and Dining System Revenue Bonds, Series K dated December 1, 1978.

"Refunded Series N Housing and Dining Bonds" means University of Kentucky Housing and Dining System Refunding Revenue Bonds, Series N dated February 1, 1994.

"Refunded Series P Housing and Dining Bonds" means University of Kentucky Housing and Dining System Revenue Bonds, Series P dated April 1, 1996.

"Refunded Series Q Housing and Dining Bonds" means University of Kentucky Housing and Dining System Revenue Bonds, Series Q dated May 1, 1997.

"Refunded Series R Housing and Dining Bonds" means University of Kentucky Housing and Dining System Revenue Bonds, Series R dated December 1, 2000.

"Refunded Series S Housing and Dining Bonds" means University of Kentucky Housing and Dining System Revenue Bonds, Series S dated August 1, 2003.

"Refunded Series M and O Housing and Dining Bonds" means University of Kentucky Housing and Dining System Refunding Revenue Bonds, Series M and O (Second Series) dated October 1, 2003.

"Refunded Series P and Q Housing and Dining Bonds" means University of Kentucky Housing and Dining System Refunding Revenue Bonds, Series P and Q (Second Series) dated January 11, 2005.

"Refunded SPBC Bonds" means State Property and Buildings Commission Agency Fund Revenue Bonds, Project No. 70 dated March 15, 2001.

"Refunding Notes" means notes issued under the provisions of Section 2.06(b) of the Indenture, the proceeds of which are used solely and only to refund a portion of the Notes then Outstanding under the Indenture and to pay the costs of issuing such Refunding Notes.

"Registrar" means the registrar maintaining the registration books for any Notes.

"Resolution" means the resolution of the Commission adopted September 18, 2006 authorizing the issuance of the Notes and the execution and delivery of the Indenture.

"S&P" means Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc.

"State" means the Commonwealth of Kentucky.

"Supplemental Trust Indenture" means any trust indenture supplemental to or amendatory of the Indenture adopted by the Commission in accordance with the Indenture.

"Treasurer" means the Treasurer of the State.

"Trust Estate" means the trust estate created by the Indenture and by the pledges specifically set forth in Section 5.02 of the Indenture.

"Trustee" means the Trustee appointed pursuant to Section 9.01 of the Indenture, and its successor or successors, and any other corporation which may at any time be substituted in its place pursuant to the Indenture.

“2006 Notes” means the 2006 A Notes and the 2006 B Notes.

"2006 A Notes" means the Commission's University of Kentucky General Receipts Refunding Project Notes, 2006 Series A, issued from time to time under the provisions of the Indenture.

"2006 B Notes" means the Commission's University of Kentucky General Receipts Taxable Refunding Project Notes, 2006 Series B, issued from time to time under the provisions of the Indenture.

"2007 A Notes" means the Commission's University of Kentucky General Receipts Project Notes, 2007 Series A, issued from time to time under the provisions of the Indenture.

"University" means the University of Kentucky.

The Indenture

Delivery of the Notes. The Indenture authorizes the issuance of the Notes in the aggregate amount set forth on the cover page hereto. All Notes issued under the Indenture will rank on a parity and equality with one another and are entitled to the benefit of the continuing pledge and lien created by the Indenture to secure the full and final payment of the principal of and interest on the Notes. (Section 2.04)

Additional Notes; Refunding Notes. The Indenture provides that if the proceeds of the Notes, together with one or more series of Additional Notes authorized by the Budget Act plus other available funds, are not sufficient to complete the Construction Project, the Commission, pursuant to the Indenture, is required to authorize, issue, sell and deliver a sufficient amount, but only a sufficient amount, of Additional Notes which will be fully on a parity with and have the same security as the Notes, in order to complete the Construction Project for its intended uses and purposes. In addition, the Commission reserves the right and covenants that, to the extent the Executive Branch Budget of the State subsequently authorizes the University to incur additional debt for the purpose of completing additional construction projects, then the Commission may authorize, issue, sell and deliver a sufficient amount, but only a sufficient amount, of Additional Notes which may be on a parity as to security with the Notes in order to complete the construction projects to the extent approved by Executive Branch Budget. Additional Notes may also be issued pursuant to the Indenture, if at any time insurance proceeds are insufficient to make repairs or replace portions of the Construction Project which have been damaged, but only a sufficient amount, of Additional Notes in order to make such necessary repairs and replacements, subject to any limitations on the issuance of such notes as may then exist under the Kentucky Revised Statutes.

No Additional Notes on a parity as to security with the Notes for such specific purposes provided for in the Indenture, may be issued unless at such time the Commission is and has been in continuous compliance with all of the provisions with reference to the payment of the principal and interest with respect to the Notes and is and has been in continuous compliance with the Indenture. If any Additional Notes for such purposes are issued on a basis of parity as to security with the Notes, the Financing Agreement shall be amended to provide for payments sufficient to pay the principal and interest with respect to all Notes Outstanding under the Indenture and all Additional Notes.

No other Additional Notes may be issued at any time secured by the Pledged Receipts except and unless such pledge is made subject and subordinate to the priority of the pledges made in the Indenture to secure the Notes.

The Commission reserves the right to issue Refunding Notes which may be on a parity as to security with the Notes in order to refund any Notes then Outstanding under the Indenture.

No Refunding Notes on a parity as to security with the Notes may be issued unless at such time the Commission is and has been in continuous compliance with all of the provisions with reference to the payment of the principal and interest with respect to the Notes and is and has been in continuous compliance with all of the covenants under the Indenture. (Section 2.06)

The Pledge Effected By The Indenture. Pursuant to the Act and the Indenture, there is pledged for the payment of the principal of and interest on the Notes, payable in accordance with their terms and the provisions of the Indenture, subject only to the provisions of the Indenture permitting the application thereof for or to the purposes and on the terms and conditions set forth in the Indenture, (i) the proceeds of sale of the Notes, (ii) Eligible Investments acquired from Note proceeds or by application of moneys in Funds and Accounts (subject to the limitations of (iv) below), (iii) the Pledged Receipts, and (iv) all

Funds and Accounts created and established pursuant to the Indenture other than the Rebate Fund, including moneys and securities therein. (Section 5.02)

Establishment of Funds. The Indenture establishes (i) the Cost of Issuance Fund; (ii) the Note Payment Fund; (iii) the Project Fund; (iv) the Rebate Fund and (v) such other Funds and Accounts which may be created from time to time in order to accomplish the purposes of the Act and the Indenture and which are not inconsistent with the requirements of the Indenture. Each of the above Funds, in addition to other Accounts from time to time established, are required to be held and maintained by the Trustee pursuant to the provisions of the Indenture, except for the Project Fund, which is required to be held by the Treasurer. (Section 5.03)

Cost of Issuance Fund. The Indenture establishes and creates a separate Cost of Issuance Fund with a separate account established within the Cost of Issuance Fund for each series of Notes. There will be deposited in the Cost of Issuance Fund, the amount required by the Indenture. The Trustee is required from time to time pay out, or permit the withdrawal of, moneys from the Cost of Issuance Fund, free and clear of any lien or pledge or assignment in trust created by the Indenture, for the purpose of paying, any Costs of Issuance, upon receipt by the Trustee of a written requisition of the Commission signed by an Authorized Officer of the Commission stating with respect to each payment to be made, the Costs of Issuance to be so paid.

If any moneys remain in the Cost of Issuance Fund on the date which is five months from the date of issuance of the Notes, the Trustee is required to transfer such amounts to the Note Payment Fund. (Section 5.04)

Note Payment Fund. The Indenture establishes and creates a separate Note Payment Fund. In addition to any other Accounts deemed necessary by the Trustee, the Indenture establishes within the Note Payment Fund the following:

An Interest Account for each Series of Notes, into which will be deposited all amounts (i) received as accrued interest upon the sale and delivery of any Notes of such Series and (ii) received as the interest portion of Financing Payments (including any prepayments of the interest portion of Financing Payments).

A Principal Account for each Series of Notes, into which will be deposited all amounts (i) transferred from the account in the Project Fund for such Series of Notes to pay principal of and premium, if any, on the Notes of such Series due at maturity, on a Redemption Date or upon acceleration; (ii) received as the principal portion of Financing Payments (including any prepayments of the principal portion of Financing Payments); and (iii) representing proceeds of and premium, if any, on Notes of such Series to pay principal of such Notes at maturity on a Redemption Date, or upon acceleration.

Amounts in the Interest Accounts are required to be used to pay interest on the related Series of Notes. Amounts in the Principal Accounts will be used to pay principal of and premium, if any, on the related Series of Notes.

The Indenture requires the Trustee to transmit to any Paying Agent, as appropriate, from moneys in the Note Payment Fund applicable thereto, amounts sufficient to make timely payments of principal of, interest on and premium, if any, on the Notes to be made by such Paying Agent and then due and payable. (Section 5.05)

Project Fund. The Indenture establishes and creates a trust fund to be designated the Project Fund and a separate account therein for the 2007 A Notes and each series of Additional Notes, which are required to be accounts in the Commonwealth's management administrative and reporting system. The Project Fund and the accounts therein are required to be separately identified from all other accounts in the Commonwealth's management administrative and reporting system and are required to be used solely for the purposes provided in the Indenture. The proceeds of the issuance and delivery of the 2007 A

Notes in an amount not more than the amount authorized for the Project by the Budget Act, are required to be deposited in the Project Fund. Under the Indenture, the Treasurer makes disbursements from the Project Fund on a first-in-first-out basis in accordance with and as required by the provisions of requisitions filed from time to time by an Authorized Officer of the University and in accordance with the provisions of the Financing Agreement. The University is required to keep and maintain adequate records pertaining to the Project Fund and all disbursements therefrom. All of the income derived from investment of the Project Fund will, at the option of the University, be transferred as received to the Note Payment Fund and disbursed therefrom on the next succeeding Interest Payment Date or held in the Project Fund and used for the purposes thereof. If any amount remains in the Project Fund after an Authorized Officer of the University certifies that the Project has been completed, such amount shall be transferred to the Interest Account of the Note Payment Fund. (Section 5.06)

Rebate Fund. The Indenture establishes and creates a trust fund to be designated the Rebate Fund, which is established and maintained under the Indenture or under any laws governing the creation and use of funds by the Commission. If a Series of Notes is determined to be subject to the "rebate" requirements in favor of the United States of America imposed by the Code, there will be deposited in the Rebate Fund such amounts as are required to be deposited therein pursuant to the related Memorandum of Instructions. Subject to the transfer provisions provided in Section 5.07 of the Indenture, all money at any time deposited in the Rebate Fund will be held by the Trustee in trust, to the extent required to satisfy the Rebate Amount (as defined in the Memorandum of Instructions), for payment to the federal government of the United States of America, and neither the Commission, nor the owner of any Notes will have any rights in or claim to such money. All amounts deposited into or on deposit in the Rebate Fund will be governed by Article V of the Indenture, and by the Memorandum of Instructions. The Trustee will be deemed conclusively to have complied with such provisions if it follows the directions of the Commission including supplying all necessary information in the manner provided in the Memorandum of Instructions, and will have no liability or responsibility to enforce compliance by the Commission with the terms of the Memorandum of Instructions.

Upon the Commission's written direction, an amount is required to be deposited to the Rebate Fund by the Trustee from deposits by the Commission, if and to the extent required, so that the balance of the Rebate Fund after such deposit equals the Rebate Amount for the Bond Year (as such term is defined in the Memorandum of Instructions) calculated as of the most recent Calculation Date (as defined in the Memorandum of Instructions). Computations of the Rebate Amount are required to be furnished by or on behalf of the Commission in accordance with the Memorandum of Instructions.

The Trustee will have no obligation to rebate any amounts required to be rebated pursuant to Section 5.07 of the Indenture, other than from moneys held in the Funds and Accounts or from other moneys provided to it by the Commission.

The Trustee is required to, upon written direction, invest all amounts held in the Rebate Fund, subject to the restrictions set forth in the Indenture for investments in other funds established in the Indenture and in the Memorandum of Instructions. The Trustee will retain all earnings (calculated by taking into account net gains or losses on sales or exchanges and taking into account amortized discount or premium as a gain or loss, respectively) on investments held in the Rebate Fund in the Rebate Fund. Moneys will not be transferred from the Rebate Fund except as provided in the following paragraph.

Upon receipt of the Commission's written directions, the Trustee shall remit part or all of the balances in the Rebate Fund to the United States, as so directed. In addition, if the Commission so directs, the Trustee will deposit moneys into or transfer moneys out of the Rebate Fund from or into such account or funds as directed by the Commission's written directions. Any funds remaining in the Rebate Fund after redemption and payment of all of the Notes and payment and satisfaction of any Rebate Amount, or provision made therefore satisfactory to the Trustee shall be withdrawn and remitted to, or at the direction of, the Commission.

Notwithstanding any other provision of the Indenture, the obligation to remit the Rebate Amounts to the United States and to comply with all other requirements of Section 5.07 of the Indenture and the Memorandum of Instructions will survive the defeasance or payment in full of the Notes. (Section 5.07)

Investment of Funds. The Indenture requires amounts on deposit in any Fund or Account to be invested in Eligible Investments, and for the Trustee to sell at the best price reasonably obtainable, or present for redemption or exchange, any Eligible Investments purchased by it as an investment pursuant to the Indenture whenever it will be necessary in order to provide moneys to meet any payment or transfer from the Fund or Account from which such investment was made. Except as otherwise provided in the Indenture, earnings and losses on Eligible Investments are required to be credited to the Fund or Account with respect to which such investments were made (or pro-rated thereto) and will become a part thereof for all purposes, except as otherwise provided in the Indenture. (Section 5.08)

Further Assurance. The Indenture requires the Commission, so far as it may be authorized by law, to pass, make, do, execute, acknowledge and deliver, all and every such further resolutions, acts, deeds, conveyances, assignments, transfers and assurances as may be necessary or desirable for the better assuring, conveying, granting, assigning and confirming all and singular the rights, assets and revenues pledged and assigned, or intended so to be, or which the Commission may become bound to pledge or assign. (Section 6.04)

Powers as to Notes and Pledge. Under the Indenture, the Commission is authorized to issue the Notes and execute and deliver the Indenture and pledge the income, revenues and assets pledged by the Indenture in the manner and to the extent provided in the Indenture. The income, revenues and assets pledged are and will be free and clear of any pledge, lien, charge or encumbrance thereon or with respect thereto prior to, or of equal rank with, the pledge created by the Indenture, and all official action on the part of the Commission to that end has been or will be duly and validly taken. The Notes and the provisions of the Indenture are and will be the valid and legally enforceable obligations of the Commission in accordance with their terms and the terms of the Indenture. The Budget Act includes authorization for the issuance of "bonds" (being the Notes) for the Project and includes adequate funds for the payment of Financing Payments and Additional Payments under the Financing Agreement. The Commission is required to at all times, to the extent permitted by law, defend, preserve and protect the pledge of the incomes, revenues and assets pledged under the Indenture and all the rights of the Holders under the Indenture against all claims and demands therefore of all persons whomsoever. (Section 6.05)

Covenants as to Financing Payments and Additional Payments. The Indenture establishes that the Financing Agreement will continue to be maintained by the Commission. In the event the University for any reason whatsoever fails to pay any Financing Payments or Additional Payments specified in the Financing Agreement, the Commission will use its best efforts to make or cause to be made payments of Financing Payments or Additional Payments so that the aggregate of the gross receipts and revenues from the Financing Agreement at all times will be sufficient to make such prescribed payments into the Note Payment Fund; provided, however, that in the event of any failure of the University to make its payments as aforesaid, no action shall be taken which, in Counsel's opinion, would have the effect of materially altering the federal income tax status of the interest earned on the Notes.

If, at any time, the prescribed Financing Payments under the Financing Agreement are not sufficient to pay the principal of and the interest on the Notes authorized in the Indenture or Additional Payments are not sufficient to pay fees and expenses related to the Notes, in accordance with the provisions of the Indenture, such Financing Payments or Additional Payments are required to be immediately adjusted in order to produce sufficient revenues for such purposes. (Section 6.08)

Covenant to Confer with Appropriate Officials Concerning Biennial Budget. The Commission will, prior to the beginning of each fiscal biennium confer with the proper officials of the University to induce the University to include in its budget such provisions and arrangements as may be required and appropriate to continue to pay the prescribed Financing Payments and Additional Payments during such biennial period. (Section 6.09)

Covenant to Enforce the Financing Agreement. So long as any of the Notes are Outstanding and unpaid as to either principal or interest, the Commission will continuously enforce the Financing Agreement to the maximum extent permitted by law, and will not consent to any modification of the Financing Agreement which would in any particular way impair the security created for the holders of the Notes. (Section 6.10)

Tax Covenant. The Commission is required to do and perform all acts and things permitted by law and necessary or desirable in order to assure that interest paid by the Commission on the 2006 A Notes and 2007 A Notes will, for the purposes of federal income taxation, be excludable from gross income under any valid provision of law including but not limited to, provisions of the Code and Section 122 of Title 23, as applicable.

The Commission will not permit at any time or times any of the proceeds of the 2006 A Notes or 2007 A Notes to be used to acquire or to replace funds which were used directly or indirectly to acquire any securities or obligations which are "higher yielding investments" (as defined in the Code), the acquisition of which would cause any 2006 A Note or 2007 A Note to be an "arbitrage bond" as defined in Sections 103(b)(2) and 148 of the Code as then in effect, unless, under any valid provision of law hereafter enacted (i) such action would not cause arbitrage bond status to occur, or (ii) the interest paid by the Commission on the 2006 A Notes and 2007 A Notes will be excludable from the gross income of a recipient thereof for federal income tax purposes without regard to compliance with the provisions of Section 103(a) of the Code.

In order to assure compliance with Section 6.11 of the Indenture, thereby better securing and protecting the 2006 A Notes and 2007 A Notes, the Commission from the date of adoption of the Indenture will not:

(1) make or cause to be made any investment of proceeds of the 2006 A Notes and 2007 A Notes that produces a yield in excess of such applicable maximum yield as may be permitted by the Code, and

(2) invest or cause the Trustee (or the Treasurer, as the case may be) to, and the Trustee (or the Treasurer, as the case may be) shall not, independent of any direction of the Commission, invest monies in any fund created under the Indenture in investment obligations that produce a yield in excess of such applicable maximum yield as may be permitted by the Code.

The Commission prior to the issuance of any of the Notes and as a condition precedent to such issuance, the Commission is required to certify by issuance of a certificate by an Authorized Officer having responsibility for the receipt, disbursement, use and investment of the proceeds of the Notes that, on the basis of the facts, estimates and circumstances in existence on the date of issue of the Notes it is not expected that the proceeds of the 2006 A Notes and 2007 A Notes will be used in a manner that would cause such obligations to be arbitrage bonds.

The Commission is required to pay from time to time all amounts required to be rebated to the United States pursuant to Section 148(f) of the Code and any temporary, proposed or final Treasury Regulations as may be applicable to the 2006 A Notes and 2007 A Notes from time to time. This requirement will survive payment in full or defeasance of the Notes. The Commission is required to pay or cause to be paid to the United States at the times and in the amounts determined under Section 5.07 of the Indenture the Rebate Amounts, as described in the Memorandum of Instructions. The Trustee is required to comply with all instructions of the Commission given in accordance with the Memorandum of Instructions.

Notwithstanding any provision described under this heading, if the Commission will provide to the Trustee a Counsel's opinion to the effect that any action required under Sections 6.11 and 5.07, of the Indenture is no longer required, or to the effect that some further action is required, to maintain the exclusion from gross income of the interest on the 2006 A Notes and 2007 A Notes pursuant to Section 103(a) of the Code, the Commission and the Trustee may rely conclusively on such opinion in complying with those provisions. (Section 6.11)

Supplemental Trust Indentures Effective Without Consent of Holders. The Indenture prescribes procedures whereby the Commission may, with the written consent of the Trustee, execute and deliver at any time from time to time Supplemental Trust Indentures for any one or more of the following purposes; to further secure the payment of the Notes; to further limit and restrict the issuance of Notes and the incurring of indebtedness by the Commission; to surrender any right, power or privilege reserved to or conferred upon the Commission by the terms of the Indenture, to confirm any pledge under and the subjection to any lien, claim or pledge created or to be created by the provisions of the Indenture; to modify any of the provisions of the Indenture in any other respects (provided that such modifications will not be effective until after all Notes outstanding as of the date of execution and delivery of such Supplemental Trust Indenture cease to be Outstanding); to cure any ambiguity or defect or inconsistent provision; and for any other purpose provided that, in the opinion of Counsel, any such amendment or modification does not materially adversely affect the rights of Holders affected thereby.

A Supplemental Trust Indenture for the purposes described above, becomes effective upon the execution thereof by the Commission and the Trustee and delivery thereof to the Trustee. At any time thereafter, notice stating in substance that the Supplemental Trust Indenture has been delivered to the Trustee and is effective pursuant to the Indenture, is required to be given to Holders by the Commission by mailing such notice to Holders by regular United States mail. (Section 7.01)

Supplemental Trust Indentures Effective with Consent of Holders. The Indenture may also be modified or amended at any time or from time to time by a Supplemental Trust Indenture, subject to the written consent of the Holders in accordance with and subject to the provisions of Article VIII of the Indenture. (Section 7.02)

Supplemental Trust Indentures Effective with Counsel's Opinion. A copy of every Supplemental Trust Indenture adopted by the Commission when filed with the Trustee is required to be accompanied by a Counsel's Opinion stating that such Supplemental Trust Indenture has been duly and lawfully adopted in accordance with the provisions of the Indenture, is authorized or permitted by the Indenture and is valid and binding upon the Commission and enforceable in accordance with its terms. (Section 7.03)

Limitations on Powers of Amendment. Any modification or amendment of the Trust Indenture and of the rights and obligations of the Commission and of the Holders of the Notes made with the consent of the Holders of the Notes may be made by a Supplemental Trust Indenture, with the written consent given by the Holders of at least a majority in principal amount of the Notes Outstanding at the time such consent is given. No modification or amendment may permit a change in the terms of redemption or maturity of the principal of any Outstanding Note or of any installment of interest thereon or a reduction in the principal amount thereof or in the rate of interest thereon without the consent of the Holder of such Note, or reduce the percentages or otherwise affect the classes of Notes the consent of the Holders of which is required to effect any such modification or amendment. (Section 8.01)

Consent of Holders. A copy of a Supplemental Trust Indenture requiring consent of the Holders, or summary thereof, together with a request to the Holders must be mailed to the Holders. Such Supplemental Trust Indenture will not be effective unless and until (a) there shall have been filed with the Trustee (i) the written consents of the proper percentage of Holders and (ii) a Counsel's Opinion, and (b) notice thereof must have been mailed to all Holders. Any such consent will be binding upon the Holder of the Notes giving such consent and, upon any subsequent Holder of such Notes and of any Notes issued in exchange therefore (whether or not such subsequent Holder thereof has notice thereof), unless such consent is revoked in writing by the Holder of such Notes giving such consent or a subsequent Holder thereof by filing with the Trustee, prior to the time when the written statement of the Trustee described in this paragraph is filed, such revocation.

At any time thereafter, notice, stating in substance that the Supplemental Trust Indenture (which may be referred to as a Supplemental Trust Indenture adopted by the Commission on a stated date, a copy of which is on file with the Trustee) has been consented to by the Holders of the required percentages of Notes and will be effective as described in this paragraph, is required to be given to the Holders by the Commission by mailing such notice to the Holders. A transcript, consisting of the papers described in this paragraph to be filed with the Trustee, will be proof of the matters therein stated. Such Supplemental Trust Indenture making such amendment or modification will be deemed conclusively binding upon the Commission, the Fiduciaries and the Holders of all Notes. (Section 8.02)

Events of Default. Each of the following events shall constitute an "Event of Default":

(1) payment of any principal on any Note shall not be made when and as the same shall become due or upon call for redemption or otherwise; or

(2) payment of any installment of interest on any Note shall not be made when and as the same shall become due; or

(3) the Commission shall fail or refuse to comply with the provisions of the Act, or shall default in the performance or observance of any other of the covenants, agreements or conditions on its part contained in the Indenture or the Notes and such failure, refusal or default shall continue for a period of 45 days after written notice thereof by the Trustee or the Holders of not less than 5% in principal amount of the Outstanding Notes. (Section 9.02)

Acceleration. Subject to provisions described in this paragraph and upon the occurrence of an Event of Default as specified in paragraphs (1) or (2) above, the Trustee is required to declare, by a notice in writing delivered to the Commission, the principal of all Notes then outstanding (if not then due and payable), together with interest accrued thereon, to be due and payable immediately. Upon the occurrence of any other Event of Default, the Trustee may, or at the direction of the Holders of not less than 25% of the Notes Outstanding is required to, declare, by a notice in writing delivered to the Commission, the principal of all Notes then outstanding (if not then due and payable), together with interest accrued thereon, to be due and payable immediately.

Any such declaration is required to be by notice in writing to the Commission, and, upon said declaration, principal and interest on all Notes will become and be immediately due and payable. The Trustee immediately upon such declaration is required to give notice thereof in the same manner as provided in the Indenture with respect to the redemption of the Notes without regard to the times stated for notice of redemption that the payment of principal and interest will be tendered immediately to the Holders of the Notes and that interest has ceased to accrue as of the date of such declaration of acceleration. Nothing contained in the Indenture shall be construed to permit the acceleration of any payments of Financing Payments or Additional Payments by the University beyond the current term of the Financing Agreement. (Section 9.03)

Other Remedies. Upon the occurrence of an Event of Default specified in paragraphs (1) or (2) above, the Trustee is required to proceed, or upon the happening and continuance of any other Event of Default specified in paragraph (3) above, the Trustee may proceed, and upon the written request of the Holders of not less than 25% of the Outstanding Notes is required to proceed, in its own name, subject to the provisions described in this paragraph, to protect and enforce its rights and the rights of the Holders by such suits, actions or special proceedings in equity or at law, or by proceedings in the office of any board or officer having jurisdiction, whether for the specific performance of any covenant or agreement contained in the Indenture or in aid of the execution of any power granted therein or in the Act or for the enforcement of any legal or equitable rights or remedies as the Trustee, being advised by its counsel, will deem most effectual to protect and enforce such rights or to perform any of its duties under the Indenture.

In the enforcement of any rights and remedies under the Indenture, the Trustee will be entitled to sue for, enforce payment on and receive any and all amounts then or during any default becoming, and at any time remaining, due and unpaid from the Commission for principal, interest or otherwise, under any provision of the Indenture or of the Notes, with interest on overdue payments at the rate or rates of interest specified in such Notes, together with any and all costs and expenses of collection and of all proceedings under the Indenture and under the Notes, without prejudice to any other right or remedy of the Trustee or of the Holders, and to recover and enforce a judgment or decree against the Commission, but solely as provided in the Indenture and in the Notes for any portion of such amounts remaining unpaid, with interest, costs and expenses, and to collect in any manner provided by law, the moneys adjudged or decreed to be payable. (Section 9.04.)

Priority of Payments After Default. In the event that upon the happening and continuance of any Event of Default the funds held by the Fiduciaries are insufficient for the payment of principal and interest then due on the Notes, such funds (other than funds held for the payment or redemption of particular Notes which have theretofore become due at maturity or by call for redemption) and any other moneys received or collected by the Trustee acting pursuant to the Act and the Indenture, after making provision (i) for the payment of any expenses necessary in the opinion of the trustee to protect the interests of the Holders of the Notes and (ii) for the payment of the charges and expenses and liabilities incurred and advances made by the Fiduciaries in the performances of their respective duties under the Trust Indenture, will be applied as follows:

(1) Unless the principal of all of the Notes shall have become or have been declared due and payable:

First: To the payment to the persons entitled thereto of all installments of interest then due in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full any installments, then to the payment thereof ratably, according to the amounts due on such installments, to the persons entitled thereto, without any discrimination or preference; and

Second: To the payment to the persons entitled thereto of the unpaid principal of any Notes which shall have become due, whether at maturity or by call for redemption, in the order of their due dates and, if the amounts available shall not be sufficient to pay in full all the Notes due on any date, then to the payment thereof ratably, according to the amounts of the principal due on such date, to the persons entitled thereto, without any discrimination or preference.

(2) If the principal of all of the Notes shall have become or have been declared due and payable, to the payment of the principal and interest due and unpaid upon the Notes without preference or priority of principal over interest or of interest over principal, or of any installment of interest over any other installment of interest, or of any Note over any other Note, ratably, accordingly to the amounts due respectively for principal and interest, to the persons entitled thereto, without any discrimination or preference except as to any difference in the respective rates of interest specified in the Notes.

Whenever moneys are to be applied by the Trustee as described herein, such moneys are required to be applied by the Trustee at such times, and from time to time, as the Trustee in its sole discretion shall determine, having due regard to the amount of such moneys available for application and the likelihood of additional money becoming available for such application in the future. The deposit of such moneys with the Fiduciaries, or otherwise setting aside such moneys in trust for the proper purpose, shall constitute proper application by the Trustee, and the Trustee will incur no liability whatsoever to the Commission, to any Holder or to any other person for any delay in applying any such moneys, so long as the Trustee acts with reasonable diligence, having due regard for the circumstances, and ultimately applies the same in accordance with such provisions of the Trust Indenture as may be applicable at the time of application by the Trustee. Whenever the Trustee exercises such discretion in applying such moneys, it will fix the date (which shall be an Interest Payment Date unless the Trustee shall deem another date more suitable) upon which such application is to be made and upon such date interest on the amounts of principal to be paid on such date shall cease to accrue. The Trustee is required to give such notice as it may deem appropriate for the fixing of any such date. The Trustee is not required to make payment to the Holder of any unpaid Note unless such Note shall be presented to the Trustee for appropriate endorsement or for cancellation if fully paid. (Section 9.05)

Direction of Proceedings. Anything in the Indenture to the contrary notwithstanding, the Holders of the majority in principal amount of Notes then Outstanding will have the right by an instrument or concurrent instruments in writing executed and delivered to the Trustee, to direct the method of conducting all remedial proceedings to be taken by the Trustee under the Indenture, provided that such direction will not be otherwise than in accordance with law or the provisions of the Indenture, and that the Trustee will have the right to decline to follow any such direction which in the opinion of the Trustee would be unjustly prejudicial to Holders not parties to such direction. (Section 9.07)

Limitation on Rights of Holders. No Holder of any Note will have any right to institute any suit, action, mandamus or other proceeding in equity or at law under the Indenture, or for the protection or enforcement of any right under the Indenture or any right under the law unless such Holder has given to the Trustee written notice of the Event of Default or breach of duty on account of which such suit, action or proceeding is to be taken, and unless the Holders of not less than 25% of the Notes then Outstanding have made written request of the Trustee after the right to exercise such powers or right of action, as the case may be, have occurred, and have afforded the Trustee a reasonable opportunity either to proceed to exercise the powers granted in the Indenture or granted under the law or to institute such action, suit or proceeding in its name and unless, also, there shall have been offered to the Trustee reasonable security and indemnity against the cost, expenses (including reasonable legal expenses) and liabilities to be incurred therein or thereby, and the Trustee shall have refused or neglected to comply with such request within a reasonable time, it being understood that the Trustee is required to make all payments on the Notes as provided in the Indenture (to the extent funds are available for such purpose) and declare the Notes due and payable as provided in the Indenture, regardless of having received any indemnity or security; and such notification, request and offer of indemnity are in every such case, at the option of the Trustee, to be conditions precedent to the execution of the powers under the Indenture or for any other remedy under the Indenture or under law. It is understood and intended that no one or more Holders of the Notes will have any right in any manner whatever by his or their action to affect, disturb or prejudice the security of the Indenture, or to enforce any right under the Indenture or under law with respect to the Notes or the Indenture, except in the manner provided in the Indenture, and that all proceedings at law or in equity shall be instituted, had and maintained in the manner provided in the Indenture and for the benefit of all Holders. Nothing in the Article contained will affect or impair the right of any Holder to enforce the payment of the principal of and interest on its Notes, or the obligation of the Commission to pay the principal of and interest on each Note issued under the Indenture to the Holder thereof at the time and place stated in said Note.

Anything in the Indenture to the contrary notwithstanding, each Holder of any Note by his acceptance thereof will be deemed to have agreed that any court in its discretion may require, in any suit for the enforcement of any right or remedy under the Indenture or in any suit against the Trustee for any action taken or omitted by it as Trustee, the filing by any party litigant in such suit of an undertaking to pay the reasonable cost of such suit, and that such court may in its discretion assess reasonable costs, including reasonable attorneys' fees, against any party litigant in any such suit, having due regard to the merits and good faith of the claims or defenses made by such party litigant; but the provisions described in this paragraph will not apply to any suit instituted by the Trustee, to any suit instituted by any Holder, or group of Holders, holding at least 25% of the Notes Outstanding, or to any suit instituted by any Holders for the enforcement of the payment of the principal of, premium, if any, or interest on any Note on or after the respective due date thereof expressed in such Note. (Section 9.08)

Trustee. Prior to the occurrence of an Event of Default, the Trustee is required to perform only those duties specifically set forth in the Indenture. If an Event of Default, of which the Trustee has received notice, has occurred and is continuing, the Trustee is required to exercise its rights and powers and use the same degree of care and skill as a prudent man would exercise under the circumstances in the conduct of his own affairs. (Section 10.01)

Evidence on Which Fiduciaries May Act. Each Fiduciary will be protected in acting upon any notice, resolution, request, consent, order, certificate, report, opinion, note, or other paper or document believed by it to be genuine, and to have been signed or presented by the proper party or parties. Each Fiduciary may consult with counsel, who may or may not be of counsel to the Commission, and the opinion of such counsel will be full and complete authorization and protection in respect of any action taken or suffered by it under the Indenture in good faith and in accordance therewith. Whenever any Fiduciary will deem necessary or desirable that a matter be proved or established prior to taking or suffering any action under the Indenture, including payment of moneys out of any Fund or Account, such matter (unless other evidence in respect thereof be specifically prescribed in the Indenture) may be deemed to be conclusively proved and established by a certificate signed by an Authorized Officer of the Commission, and such certificate will be full warrant for any action taken or suffered in good faith under the provisions of the Trust Indenture in which said Fiduciary has accepted said trust upon the faith thereof, but in its discretion the Fiduciary may in lieu thereof accept other evidence of such fact or matter or may require such further or additional evidence as to it may deem reasonable. Except as otherwise expressly provided in the Indenture, any request, order, notice or other direction required or permitted to be furnished pursuant to any provision of the Indenture by the Commission to any Fiduciary is required to be sufficiently executed if executed in the name of the Commission by an Authorized Officer of the Commission. (Section 10.04)

Permitted Acts and Functions. The Trustee and any Paying Agent may become the owner of any Note, with the same rights it would have if it were not such Fiduciary. Any Fiduciary may act as depository for, and permit any of its officers or directors to act as a member of, or in any other capacity with respect to, any committee formed to protect the rights of Holders or to effect or aid in any reorganization growing out of the enforcement of the Notes or the Indenture, whether or not any such committee is required to represent the Holders of a majority in principal amount of the Notes then outstanding. (Section 10.06)

Resignation of Trustee. The Trustee may at any time resign and be discharged of the duties and obligations created by the Trust Indenture by giving not less than 60 days' written notice to the Commission and by mailing notice (specifying the date such resignation is to take effect) through regular United States mail, postage prepaid, to each Holder of Notes, and such resignation will take effect upon the day specified in such notice unless (i) no successor has been appointed as proved in the Indenture, or (ii) previously a successor shall have been appointed, as provided in the Indenture, in which event such resignation will take effect immediately on the appointment of such successor. If a successor trustee is not appointed within 60 days, the Trustee will be entitled to petition a court of competent jurisdiction to appoint a successor Trustee. (Section 10.07)

Removal of Trustee. The Trustee may and, if at any time so requested by an instrument or concurrent instruments in writing (filed with the Trustee and the Commission, and signed by the Holders of a majority in principal amount of the Notes then Outstanding or their attorneys-in-fact duly authorized, excluding any Notes held by or for the account of the Commission), shall, be removed by the Commission (so long as no Event of Default has occurred and is continuing) by an instrument or concurrent instruments in writing, filed with the Trustee and the Commission and signed by the Commission or the Holders of Notes, as appropriate. No such removal will be effective until a successor Trustee has been appointed and assumed the duties of Trustee as provided in the Indenture. (Section 10.08)

Appointment of Successor Trustee. In case at any time the Trustee shall resign or shall be removed or shall become incapable of acting, or shall be adjudged bankrupt or insolvent, or if a receiver, liquidator or conservator of the Trustee, or of its property, shall be appointed, or if any public officer shall take charge or control of the Trustee, or of its property or affairs, the Commission covenants and agrees that it will thereupon appoint a successor Trustee. The Commission is required to provide notice of any such appointment made by it within 20 days after such appointment to Holders of Notes.

If no appointment of a successor Trustee shall be made pursuant to the foregoing provisions within 45 days after the Trustee shall have given to the Commission written notice, as provided above in the paragraph titled "Resignation of Trustee", or after a vacancy in the office of the Trustee shall have occurred by reason of its removal or inability to act, the Trustee or the Holder of any Note may apply to any court of competent jurisdiction to appoint a successor Trustee. Said court may thereupon, after such notice, if any, as such court any deem proper and prescribe, appoint a successor Trustee.

Any Trustee appointed in succession to the Trustee is required to be a trust company or bank having the powers of a trust company within or outside the Commonwealth, having a capital and surplus aggregating at least $75,000,000 if there be such a trust company or bank willing and able to accept the office on reasonable and customary terms and authorized by law to perform all duties imposed upon it by the Indenture. (Section 10.09)

Defeasance. Notes or interest installments of particular Notes for the payment or redemption of which moneys will have been set aside and shall be held in trust by Fiduciaries will, at the maturity or date of redemption thereof, be deemed to have been paid within the meaning and with the effect expressed above. Particular Notes will, prior to the maturity or redemption thereof, be deemed to have been paid within the meaning and with the effect expressed above, if (a) in case any of said Notes are to be redeemed on any date prior to their maturity, the Commission will have given to the Trustee in form satisfactory to it irrevocable instructions to provide notice of redemption in the manner prescribed in the Indenture, (b) there will have been deposited with the Trustee either moneys in an amount which shall be sufficient, or Defeasance Obligations, the principal of and the interest on which when due will provide moneys which, together with the moneys, if any, deposited with the Trustee at the same time, will be sufficient, to pay when due the principal and interest due and to become due on said Notes on and prior to the Redemption or maturity date thereof, as the case may be, (c) in the event said Notes are not subject to redemption within the next 60 days, the Commission will have given the Trustee in form satisfactory to it irrevocable instructions to notify the Holders of such Notes of such redemption in the manner herein provided for giving notice of redemption and (d) a Counsel's Opinion that the defeasance will not adversely affect any exclusion from gross income for federal income tax purposes of interest on the Notes. Neither Defeasance Obligations or moneys deposited with the Trustee as described in this paragraph, nor principal or interest payments on any such obligations, may be withdrawn or used for any purpose other than, and must be held in trust for, the payment of the principal and interest on said Notes.

Anything in the Indenture to the contrary notwithstanding, any moneys held by a Fiduciary in trust for the payment and discharge of any of the Notes which remain unclaimed for six years after the date when all of the Notes have become due and payable, either at their stated maturity dates or by call for earlier redemption, if such moneys were held by the Fiduciary at such date, or for six years after the date of deposit of such moneys if deposited with the Fiduciary after said date when all of the Notes became due and payable, will (subject to the provisions of Article V of the Indenture), at the written request of the Commission, be repaid by the Fiduciary to the Commission, as its absolute property and free from trust, and the Fiduciary will thereupon be released and discharged.

"Defeasance Obligations" means and includes any of the following:

(1) Direct and general non-callable obligations of the United States of America, backed by the full faith and credit of the United States of America or obligations that are unconditionally

guaranteed as to principal and interest by the United States of America. The obligations described in this paragraph are called "United States Obligations".

(2) Prerefunded municipal obligations rated "AAA" by each Rating Service then rating the Notes and meeting the following conditions:

(a) the municipal obligations are (i) not to be redeemed prior to maturity or the Trustee has been given irrevocable instructions concerning their calling and redemption and (ii) the issuer has covenanted not to redeem such municipal obligations other than as set forth in such instructions;

(b) the municipal obligations are secured by cash or United States Obligations that may be applied only to interest, principal, and premium payments of such municipal obligations;

(c) the principal of and interest on the United States Obligations (plus any cash in the escrow fund) are sufficient to meet the liabilities on the municipal obligations;

(d) the United States Obligations serving as security for the municipal obligations are held by an escrow agent or trustee;

(e) the United States Obligations (plus any cash in the escrow fund) are not available to satisfy any other claims, including those against the trustee or escrow agent; and

if the redemption date for the Notes to be discharged by the deposit of Defeasance Obligations is no later than ninety (90) days from the date of such deposit, "Defeasance Obligations" shall also include direct and general non-callable obligations of any Federally sponsored enterprise, including Federal Home Loan Mortgage Corporation, Federal National Mortgage Association, Federal Farm Credit Banks, Federal Intermediate Credit Banks, Federal Land Banks, Federal Home Loan Banks, Bank for Cooperatives and any other similar institution. (Section 11.01)

The Financing Agreement

The Commission, the Cabinet and the University have entered into the Financing Agreement which provides for (i) financing of the Project by issuance of the Notes by the Commission; and (ii) the leasing of the Project from the Commission to the University to provide revenues for amortization of the Notes. As required by the Act, the Cabinet is also a party to the Financing Agreement.

Financing Payments. The Commission has agreed to provide financing for the Project to the University. The University has the right to continue the Financing Agreement until the final maturity date for the Notes. The University is required to pay, as Financing Payments, the Debt Servicing Obligation relating to the Notes so long as any Notes are Outstanding.

Additional Payments. The University covenants and agrees to pay "Additional Payments" for the term of the Financing Agreement and for any Renewal Term during which Notes are outstanding, as follows:

(1) To the Trustee, when due, all fees of the Trustee for services rendered, all fees and charges of any Paying Agent, Registrar, counsel, accountants, and others incurred in the performance on request of the Trustee of services for which the Trustee and such other persons are entitled to payment or reimbursement which are not paid as Financing Payments; and

(2) To the Commission, upon demand, all reasonable expenses incurred by it in relation to the Project which are not otherwise specifically identified and required to be paid by the Commission under the terms of the Financing Agreement.

Financing Agreement an Obligation. The University has authorized and entered into the Trust Agreement. It is the intent of the University that the Financing Agreement constitute an Obligation within the meaning of the Trust Agreement, it is declared that the Financing Agreement is issued and delivered by the University in accordance with the terms of the Trust Agreement, and the Commission is granted all rights and privileges as Holder, as defined in the Trust Agreement, with respect to the Obligation (being the Financing Agreement), for all purposes under the Trust Agreement, subject to the terms of the Trust Agreement.

Events of Default. Each of the following events constitute an "event of default":

(1) default in the due and punctual payment of any Financing Payments or Additional Payments; or

(2) default in the performance of any of the covenants, terms, and conditions of the Financing Agreement, and failure to remedy such default within thirty (30) days after written receipt thereof if the default relates to matters other than the payment of Financing Payments or Additional Payments (but the University will not be deemed to be in default if the University commences to remedy said defaults other than related to payment of Financing Payments or Additional Payments within said 30 day period, and proceed to and do remedy said default with due diligence).

If an event of default occurs, the Commission, in addition to all other remedies given to the Commission at law or in equity, may by written notice to the University terminate the Financing Agreement. No termination of the Financing Agreement will deprive the Commission of any of its remedies or actions against the University.

Provisions of the Financing Agreement Benefit of the Holders of the Notes. All of the provisions contained in the Financing Agreement, are made for the benefit of each of the holders of the Notes. Each and all of the holders of the Notes, and the Trustee on behalf of the holders of the Notes, have the rights of third party beneficiaries to enforce all of the provisions of the Financing Agreement; subject, however, to the provisions of the Indenture with respect to enforcement of rights.

Security and Assignment. The Financing Agreement secures (i) the payment of Financing Payments and Additional Payments, and (ii) the payment of the Notes in the aggregate principal amount which may from time to time be outstanding under the Indenture, with interest thereon at the rates per annum borne by such Notes.

The Financing Agreement is given subject to all of the terms, conditions and provisions of the Indenture. In the event that any conflict should exist or appear to exist between the provisions of the Financing Agreement and the Indenture, the provisions of the Indenture will prevail. (Financing Agreement Section 12.01)

Amendment. The Financing Agreement may be amended or supplemented from time to time by a writing duly executed by the parties thereto; subject, however, to the condition that any such amendment or supplement will be consistent with the terms and conditions of the Indenture and not diminish the Financing Payments or Additional Payments payable under the provisions of the Financing Agreement for so long as any Notes are Outstanding.

VERIFICATION OF MATHEMATICAL CALCULATIONS

Prior to the delivery of the Notes, The Arbitrage Group, Inc. will deliver a report on the mathematical accuracy of certain computations contained in schedules provided to them by the Underwriters. These computations will relate to (i) the computation of the anticipated receipts of principal and interest on the Eligible Investments held in the Escrow Fund and the anticipated payments or principal and interest to redeem the Refunded Bonds, and (ii) the examination by The Arbitrage Group, Inc. of the computation of the yields on the Refunding Bonds and the Eligible Investments held in the Escrow Fund. Such computations were based solely upon assumptions and information supplied by the Underwriters. The Arbitrage Group, Inc. has restricted its procedures to examining the arithmetical accuracy of certain computations and has not made any study or evaluation of the assumptions and information upon which the computations are based and, accordingly, has not expressed an opinion on the data used, the reasonableness of the assumptions, or the achievability of future events.

TAX MATTERS

General

In the opinion of Kutak Rock LLP, Bond Counsel, to be delivered at the time of original issuance of the Series 2006 A Notes, under existing laws, regulations, rulings and judicial decisions, interest on the Series 2006 A Notes (a) is excluded from gross income for federal income tax purposes and (b) is not a specific item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. In the preliminary opinion of Bond Counsel, to be delivered concurrently with its opinion regarding the 2006 A Notes, under existing laws, regulations, rulings and judicial decisions, interest on the 2007 A Notes, were such 2007 A Notes delivered on the date of such preliminary opinion, (x) would be excluded from gross income for federal income tax purposes and (y) would not be a specific item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. Interest on the 2006 A Notes and the 2007 A Notes (collectively, the "Tax Exempt Notes"), however, will be included in the "adjusted current earnings" (i.e., alternative minimum taxable income as adjusted for certain items, including those items that would be included in the calculation of a corporation's earnings and profits under Subchapter C of the Internal Revenue Code of 1986, as amended (the "Code")) of certain corporations and such corporations are required to include in the calculation of alternative minimum taxable income 75% of the excess of each such corporation's adjusted current earnings over its alternative minimum taxable income (determined without regard to this adjustment and prior to reduction for certain net operating losses).

The future issuance of the 2007 A Notes is subject to the ability of Bond Counsel to deliver its opinion letter on the date of issuance of the 2007 A Notes confirming the preliminary opinions as described above. Bond Counsel is unaware of any existing reason why it would not be able to deliver its confirming opinion letter on the date of issuance of the 2007 A Bonds, but there can be no assurance that such a reason will not arise.

The Commission and the University have each covenanted to comply with all requirements that must be satisfied in order for the interest on the Tax Exempt Notes to be excludible from gross income for federal tax purposes. The opinions set forth above, and the ability of Bond Counsel to deliver its opinion of the date of issuance of the 2007 A Notes confirming its preliminary opinion, are subject to continuing compliance by the Commission and the University and others with such covenants. Failure to comply with such covenants could cause interest on the Tax Exempt Notes to be included in gross income retroactive to the respective dates of issue of the Tax Exempt Notes.

The accrual or receipt of interest on the Tax Exempt Notes may otherwise affect the federal income tax liability of certain recipients such as banks, thrift institutions, property and casualty insurance companies, corporations (including S corporations and foreign corporations operating branches in the United States), Social Security or Railroad Retirement benefit recipients, taxpayers otherwise entitled to claim the earned income credit or taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, among others. The extent of these other tax consequences will depend upon the recipients' particular tax status or other items of income or deduction. Bond Counsel expresses no opinion regarding any such consequences and investors should consult their own tax advisors regarding the tax consequences of purchasing or holding the Tax Exempt Notes.

In Bond Counsel's further opinion, under the existing laws of the Commonwealth, interest on the 2006 A Notes and the 2006 B Notes is excluded from the gross income of the recipients thereof for Kentucky income tax purposes and such Notes are exempt from ad valorem taxes by the Commonwealth and all political subdivisions thereof. In Bond Counsel's further preliminary opinion, under the existing laws of the Commonwealth, interest on the 2007 A Notes, if issued on the date of such preliminary opinion, would be excluded from the gross income of the recipients thereof for Kentucky income tax purposes and such 2007 A Notes would be exempt from ad valorem taxes by the Commonwealth and all political subdivisions thereof.

Bond Counsel expresses no opinion as to the federal income tax treatment of the interest on the 2006 B Notes, or as to any tax consequences of purchasing or holding the 2006 B Notes. Investors should consult their own tax advisors regarding any such tax consequences.

Future Legislation or Regulation

From time to time, there are legislative proposals in Congress that, if enacted, could alter or amend the federal tax matters referred to above or adversely affect the market value of the Tax Exempt Notes. It cannot be predicted whether or in what form any such proposal might be enacted or whether if enacted, it would apply to bonds issued prior to enactment. Each purchaser of the Tax Exempt Notes should consult his or her own tax advisor regarding any pending or proposed federal tax legislation. Bond Counsel expresses no opinion regarding any pending or proposed federal tax legislation.

Tax Law Risk

Subject to certain additional conditions (see "CERTAIN FORWARD DELIVERY CONSIDERATIONS"), the Forward Delivery Note Purchase Agreement related to the 2007 A Notes obligates the Commission to deliver and the Underwriter to acquire the 2007 A Notes if the Commission delivers a confirming opinion of Bond Counsel substantially in the form and to the effect as set forth in "APPENDIX F-3—FORM OF BOND COUNSEL OPINIONS FOR THE NOTES" to this Official Statement. During the Delayed Delivery Period, new legislation, new court decisions, new regulations, or new rulings may be enacted, promulgated or interpreted that might prevent Bond Counsel from rendering its opinion or otherwise affect the substance of such opinion. Notwithstanding that the enactment of new legislation, new court decisions or the promulgation of new regulations or rulings might diminish the value of, or otherwise affect, the exclusion of interest on the 2007 A Notes for purposes of federal income taxation payable on "state or local bonds," the Commission might be able to satisfy the requirements for the delivery of the 2007 A Notes. In such event, the purchasers would be required to accept delivery of the 2007 A Notes. Prospective purchasers are encouraged to consult their tax advisors regarding the likelihood of any changes in tax law and the consequences of such changes to such purchasers.

Tax Treatment of Original Issue Discount

The Tax Exempt Notes that have an original yield above their interest rate, as shown on the cover, are being sold at a discount (the "Discounted Obligations"). The difference between the initial public offering prices, as set forth on the inside cover page hereof, of the Discounted Obligations and their stated amounts to be paid at maturity or upon prior redemption, constitutes original issue discount treated as interest which is not includible in gross income for federal income tax purposes.

In the case of an owner of a Discounted Obligation, the amount of original issue discount which is treated as having accrued with respect to such Discounted Obligation is added to the cost basis of the owner in determining, for federal income tax purposes, gain or loss upon disposition of a Discounted

Obligation (including its sale, redemption or payment at maturity). Amounts received upon disposition of a Discounted Obligation which are attributable to accrued original issue discount will be treated as tax-exempt interest, rather than as taxable gain, for federal income tax purposes.

Original issue discount is treated as compounding semiannually, at a rate determined by reference to the yield to maturity of each individual Discounted Obligation, on days which are determined by reference to the maturity date of such Discounted Obligation. The amount treated as original issue discount on a Discounted Obligation for a particular semiannual accrual period is equal to (a) the product of (i) the yield to maturity for such Discounted Obligation (determined by compounding at the close of each accrual period) and (ii) the amount which would have been the tax basis of such Discounted Obligation at the beginning of the particular accrual period if held by the original purchaser, (b) less the amount of any interest payable for such Discounted Obligation during the accrual period. The tax basis is determined by adding to the initial public offering price on such Discounted Obligation the sum of the amounts which have been treated as original issue discount for such purposes during all prior periods. If a Discounted Obligation is sold between semiannual compounding dates, original issue discount which would have been accrued for that semiannual compounding period for federal income tax purposes is to be apportioned in equal amounts among the days in such compounding period.

The Code contains additional provisions relating to the accrual of original issue discount in the case of owners of a Discounted Obligation who purchase such Discounted Obligations after the initial offering. Owners of Discounted Obligations including purchasers of the Discounted Obligations in the secondary market should consult their own tax advisors with respect to the determination for federal income tax purposes of original issue discount accrued with respect to such obligations as of any date and with respect to the state and local tax consequences of owning a Discounted Obligation.

Tax Treatment of Premium

The Tax Exempt Notes that have an original yield below their interest rate, as shown on the cover, are being sold at a premium (collectively, the "Premium Obligations"). An amount equal to the excess of the issue price of a Premium Obligation over its stated redemption price at maturity constitutes premium on such Premium Obligation. An initial purchaser of such Premium Obligation must amortize any premium over such Premium Obligation’s term using constant yield principles, based on the purchaser's yield to maturity (or, in the case of Premium Obligations callable prior to their maturity, by amortizing the premium to the call date, based upon the purchaser's yield to the call date and giving effect to any call premium). As premium is amortized, it offsets the interest allocable to the corresponding payment period and the purchaser’s basis in such Premium Obligation is reduced by a corresponding amount resulting in an increase in the gain (or decrease in the loss) to be recognized for federal income tax purposes upon a sale or disposition of such Premium Obligation prior to its maturity. Even though the purchaser's basis may be reduced, no federal income tax deduction is allowed. The same treatment is afforded to Tax Exempt Notes purchased at a premium in the secondary market. Purchasers of Premium Obligations should consult with their own tax advisors with respect to the determination and treatment of amortizable premium for federal income tax purposes and with respect to the state and local tax consequences of owning such Premium Obligations.

Delayed Settlement; Delivery of Opinion of Bond Counsel

The 2007 A Notes will be sold pursuant to the terms of the Forward Delivery Note Purchase Contract (the "Forward Purchase Contract") pursuant to which the Commission will agree to execute and deliver to Morgan Stanley & Co. Incorporated as the underwriter of the 2007 A Notes (the "2007 A Underwriter"), and the 2007 A Underwriter will agree to accept and purchase from the Commission, the 2007 A Notes on the delivery date specified in the Forward Purchase Contract, subject to the satisfaction of certain conditions provided in the Forward Purchase Contract. Bond Counsel expects to be able to deliver on the delivery date its confirming opinion with respect to the exclusion of interest on the 2007 A Notes from gross income for federal income tax purposes and from State personal income taxes and, assuming no material adverse changes in fact or in federal or State law and based upon certain representations, certifications and covenants of the Commission, all as set forth in the Forward Purchase Contract (see "CERTAIN FORWARD DELIVERY CONSIDERATIONS" below), it will render an opinion substantially in the form and to the effect set forth in APPENDIX F-3. The issuance and delivery of the 2007 A Notes on the delivery date will be subject to, among other things, receipt of such opinion of Bond Counsel.

LITIGATION

There is no controversy or litigation of any nature now pending or threatened restraining or enjoining the issuance, sale, execution or delivery of the Notes, or in any way contesting or affecting the validity of the Notes or any proceedings of the Commission taken with respect to the issuance or sale thereof, or the pledge or application of any monies or security provided for the payment of the Notes or due existence or powers of the Commission.

APPROVAL OF LEGALITY

Certain legal matters incident to the authorization, issuance, sale and delivery of the Notes are subject to the unqualified approving opinion of Kutak Rock LLP, Bond Counsel to the Commission. Certain other legal matters will be passed on by Thompson Hine LLP, Cincinnati, Ohio, counsel to the Underwriter.

RATINGS

Moody's Investors Service, Inc. ("Moody's") and Standard & Poor's Ratings Services, a Division of The McGraw-Hill Companies, Inc. ("S&P") have given the Notes the ratings of "Aaa" and "AAA", respectively, each with the understanding that upon delivery of the Series 2006 Notes and the 2007 Notes, the 2006 Bond Insurance Policy and the 2007 Bond Insurance Policy, respectively, will be issued by the Bond Insurer. The underlying ratings for the Notes are "Aa3" and "AA-" from Moody's and S&P, respectively. Each rating reflects only the views of the respective Rating Agency. Explanations of the significance of the ratings may be obtained from each Rating Agency as follows: Moody's Investors Service, Inc., 99 Church Street, New York, New York 10007, (212) 553-0300; and Standard & Poor's Ratings Services, a Division of the McGraw-Hill Companies, 55 Water Street, New York, New York 10041 (212) 438-2124. A rating is a not recommendation to buy, sell or hold the Notes, and there is no assurance that any rating will be maintained for any given period of time by a Rating Agency or that it will not be revised or withdrawn entirely by such Rating Agency, if in its judgment circumstances so warrant. Any such revision or withdrawal of a rating may have an adverse affect on the market price of the Notes.

CONTINUING DISCLOSURE

The Commission will comply with the requirements of the Securities and Exchange Commission regarding secondary market disclosure as set forth in Rule 15c2-12 (the "Rule"), as amended, under the Securities Exchange Act of 1934. Specifically, the Commission will enter into a Continuing Disclosure Agreement in which it will covenant to provide notice in a timely manner to each nationally recognized municipal securities depository or the Municipal Securities Rulemaking Board, and the appropriate state information depository, if any, of any of the following types of events with respect to the Notes, if material: (i) principal and interest payment delinquencies; (ii) non-payment related defaults; (iii) unscheduled draws on debt service reserves reflecting financial difficulties; (iv) unscheduled draws on credit enhancements reflecting financial difficulties; (v) substitution of credit or liquidity providers or their failure to perform; (vi) adverse tax opinions or events affecting the tax-exempt status of the securities; (vii) modifications to rights of security holders; (viii) bond calls; (ix) defeasances; (x) release, substitution, or sale or property securing repayment of the securities; and (xi) rating changes. The Commission is already providing ongoing market disclosure as required by Rule 15c2-12 pursuant to agreements entered into in connection with other outstanding securities.

UNDERWRITING

Morgan Stanley & Co. Incorporated, as representative of the underwriters set forth on the cover page hereof (the "Underwriters"), has agreed to purchase the 2006 Notes for a purchase price of $69,907,600.53, which is an amount equal to the par amount of such Notes, plus net premium of $1,701,130.60, less Underwriters' discount of $318,530.07. The Underwriters are committed to purchase all of the 2006 A Notes and 2006 B Notes if any are purchased. Morgan Stanley & Co. Incorporated, as sole underwriter, has agreed to purchase the 2007 A Notes for a purchase price of $82,400,143.73, which is an amount equal to the par amount of the Notes, plus net premium of $4,890,544.80, less underwriter's discount of $395,401.07. Morgan Stanley & Co. Incorporated is committed to purchase all of the 2007 A Notes if any are purchased.

The Underwriters have advised the Commission that they intend to make a public offering of the Notes at the initial public offering prices or yields set forth on the inside cover page hereof; provided, however, that the Underwriters have reserved the right to make concessions to dealers and to change such initial public offering prices as the Underwriters deem necessary in connection with the marketing of the Notes.

CERTAIN FORWARD DELIVERY CONSIDERATIONS

The Commission expects to issue and deliver the 2007 A Notes on a forward delivery date, which is expected to be on or about November 1, 2007 (the “Settlement Date”). Each investor placing an order for the 2007 A Notes which is accepted by the 2007 A Underwriter will be required to execute a forward delivery contract (a “Delivery Contract”), in substantially the form set forth in APPENDIX H. The Commission has entered into a Forward Purchase Contract with the 2007 A Underwriter for the sale and purchase of the 2007 A Notes on the 2007 A Delivery Date.

The following discussion summarizes certain provisions of the Delivery Contract and of the Forward Purchase Contract. A prospective investor should read the entire Delivery Contract.

Forward Delivery Contract with Prospective Bondholders

In the Delivery Contract, the investor acknowledges review of this Official Statement in its entirety and that its order was placed with full knowledge and understanding of the forward closing conditions and risks; the investor also agrees that it is obligated to purchase the 2007 A Notes that are the subject of the order, so long as the conditions of the Forward Purchase Contract for the forward delivery of the 2007 A Notes are satisfied.

Settlement

On or about the 2007 A Delivery Date, or on such date as may be mutually agreed upon by the Commission and the 2007 A Underwriter, the Commission will, subject to the terms and conditions of the Forward Purchase Contract, deliver the 2007 A Notes to the 2007 A Underwriter and deliver or cause to be delivered to the 2007 A Underwriter the other documents, opinions, certificates, and instruments required by the Forward Purchase Contract (the “Settlement Documents”), including an updated Official Statement (the “Supplement to Official Statement”) relating to the 2007 A Notes. Subject to the terms and conditions of the Forward Purchase Contract, the 2007 A Underwriter will accept such delivery and pay the purchase price for the 2007 A Notes. All the foregoing described transactions are referred to herein as the “Settlement,” and the date upon which such transactions are consummated is referred to herein as the “Settlement Date.”

The Commission will have no obligation to issue, sell, and deliver the 2007 A Notes, and the 2007 A Underwriter will have no obligation to purchase the 2007 A Notes if a Change in Law (defined below) occurs. In such event, the Commission will have no liability whatsoever for its failure to issue, sell, and deliver the 2007 A Notes, and the 2007 A Underwriter will have no liability for their failure to purchase the 2007 A Notes.

In addition, as described below under "CERTAIN FORWARD DELIVERY CONSIDERATIONS – Termination of Forward Purchase Contract," the 2007 A Underwriter may terminate the Forward Purchase Contract, without liability, by notification to the Commission, if at any time on or prior to the Settlement Date there occurs an event comprising a Change in Law.

Conditions to Settlement

The Settlement and the issuance of the 2007 A Notes will not require further action by the Commission other than the satisfaction of the specific conditions of the Forward Purchase Contract, including delivery of the Settlement Documents. The Settlement Documents include, among other items, the confirming opinion of Bond Counsel in substantially the form set forth in APPENDIX F-3, certain other opinions of Bond Counsel and the Counsel to the 2007 A Underwriter, and certificates of the Commission as to the completeness and accuracy of the Supplement to Official Statement. The Forward Purchase Contract requires the Commission to prepare the Supplement to Official Statement as of the date between October 1, 2007 and October 29, 2007 and to furnish it to the 2007 A Underwriter.

THE FORWARD PURCHASE CONTRACT DOES NOT PERMIT THE 2007 A UNDERWRITER TO REFUSE TO ACCEPT DELIVERY OF AND PAY FOR THE 2007 A NOTES BECAUSE OF ANY ADVERSE CHANGE IN THE FINANCIAL CONDITION OR OPERATIONS OF THE COMMISSION OR THE UNIVERSITY; RATHER, IT PERMITS SUCH REFUSAL ONLY IF ANY SUCH CHANGE HAS NOT BEEN ACCURATELY AND COMPLETELY DESCRIBED IN THE SUPPLEMENT TO OFFICIAL STATEMENT OR IN A SUPPLEMENT OR AMENDMENT TO THE SUPPLEMENT TO OFFICIAL STATEMENT OR IF SUCH CHANGE WOULD CAUSE THE COMMISSION OR ANOTHER PARTY TO BE UNABLE TO DELIVER ANY OF THE SETTLEMENT DOCUMENTS IN THE FORM AND SUBSTANCE PROVIDED FOR IN THE FORWARD PURCHASE CONTRACT.

FAILURE TO COMPLETE THE REQUIREMENTS OF THE SETTLEMENT, INCLUDING FAILURE OF THE COMMISSION TO DELIVER ANY OF THE SETTLEMENT DOCUMENTS IN THE FORM AND SUBSTANCE PROVIDED FOR IN THE FORWARD PURCHASE CONTRACT (UNLESS SUCH FAILURE IS WAIVED BY THE 2007 A UNDERWRITER), WILL MEAN THAT THE 2007 A NOTES WILL NOT BE ISSUED AND DELIVERED. THE 2007 A UNDERWRITER HAS THE RIGHT, BUT IT IS UNDER NO OBLIGATION, TO WAIVE ANY SUCH FAILURE.

Issuance of Legal Opinions

It is a condition to the issuance of the 2007 A Notes on the Settlement Date that Bond Counsel deliver its opinion, confirming its preliminary opinion delivered on the date of delivery of the 2006 Notes in substantially the form attached hereto as APPENDIX F-3, as described under the heading "CERTAIN FORWARD DELIVERY CONSIDERATIONS – Conditions to Settlement."

The ability of Bond Counsel to deliver such an opinion on the Settlement Date is subject to its review and analysis at that time of certain matters, including, among others, the application of the proceeds of the 2007 A Notes and pertinent provisions of the Act, federal income tax and securities laws, regulations, rulings, and court decisions, including, but not necessarily limited to, state law and securities laws then in effect or proposed to be effect. Bond Counsel has advised the Commission and the 2007 A Underwriter that, assuming satisfaction by the Commission and the 2007 A Underwriter of their respective obligations to be satisfied in the Forward Purchase Contract, and the issuance of the 2007 A Notes, and no change in any applicable law, regulations or rulings, or in interpretations thereof, or in any other facts or circumstances (tax or otherwise) which in Bond Counsel's view, affect or are material to its opinion (including without limitation, the existence of any litigation), Bond Counsel expects to be able to issue, on the Settlement Date, an opinion substantially in the form set forth in APPENDIX F-3.

In addition, to deliver such opinion, Bond Counsel will require appropriate certifications and representations to establish the Commission's reasonable expectations. Although the Commission is not aware, as of the date of this Official Statement, of any information that would lead it to believe that it will be unable to satisfy its obligations under the Forward Purchase Contract on the Settlement Date, no assurances can be made that there will be no change in any applicable law, regulations, or rulings, or in interpretations thereof, prior to the Settlement Date. Furthermore, no assurance can be made that the facts and circumstances that are material to such confirming opinion will not differ, as of the Settlement Date, from those that are currently expected, or that such certifications and representations will be delivered and made in connection with the issuance of the 2007 A Notes. As a consequence of any of the foregoing, such confirming opinion of Bond Counsel may not be rendered.

As described above, the Forward Purchase Contract does not permit the 2007 A Underwriter to refuse to accept delivery of and pay for the 2007 A Notes because of any adverse change in the financial condition or operations of the Commission. Accordingly, it is not a condition to the Settlement that any of the rating agencies confirm any ratings of the Commission or the University.

Termination of Forward Purchase Contract

The 2007 A Underwriter may terminate the Forward Purchase Contract, without liability, by notification to the Commission if, at any time on or before the Settlement Date, there occurs an event comprising a Change in Law.

A "Change in Law" is defined in the Forward Purchase Contract and in the Delivery Contract as:

(i) any change in or addition to applicable federal or state law, whether statutory or as interpreted by the courts, including any changes in or new rules, regulations, or other pronouncements or interpretations by federal or state agencies;

(ii) any legislation enacted by the Congress of the United States or introduced therein or recommended for passage by the President of the United States (if such enacted, introduced or recommended legislation has a proposed effective date which is on or before the Settlement Date);

(iii) any rule or regulation proposed or enacted by any governmental body, department, or agency (if such proposed or enacted rule or regulation has a proposed effective date which is on or before the Settlement Date); or

(iv) any judgment, ruling or order issued by any court or administrative body;

which in any such case, would:

(A) as to the 2007 A Underwriter, legally prohibit (or have the retroactive effect of prohibiting, if enacted, adopted, passed or finalized) the 2007 A Underwriter from

(1) accepting delivery of and paying for the 2007 A Notes in accordance with the provisions of the Forward Purchase Contract or

(2) selling the 2007 A Notes or beneficial ownership interests therein to bona fide purchasers; or

(B) as to the Commission,

(1) make the issuance, sale, or delivery of the 2007 A Notes illegal (or have the retroactive effect of making such issuance, sale, or delivery illegal, if enacted, adopted, passed, or finalized);

(2) eliminate the exclusion from gross income for federal or Kentucky income tax purposes of interest on the 2007A Notes or otherwise adversely affect the tax treatment of ownership of the 2007 A Notes (or have any such effect retroactively if enacted, adopted, passed, or finalized); or

(3) require the 2007 A Notes to be registered under the Securities Act of 1933, as amended, or the Indenture or Resolution to be qualified under the Trust Indenture Act of 1939; or

(C) as to the University, diminish in any way the obligations of the University under the Financing Agreement as the Financing Agreement relates to the Notes;

provided, however, that such change in or addition to law, legislation, rule or regulation, or judgment, ruling, or order shall have become effective, been enacted, introduced, or recommended, or been proposed or been issued, as the case may be, subsequent to the date of the Forward Purchase Contract. IF A CHANGE OR ADDITION TO LAW, LEGISLATION, RULE OR REGULATION, OR JUDGMENT, RULING, OR ORDER INVOLVES THE ENACTMENT OF LEGISLATION WHICH ONLY DIMINISHES THE VALUE OF, AS OPPOSED TO ELIMINATING THE EXCLUSION FROM GROSS INCOME FOR FEDERAL INCOME TAX PURPOSES, INTEREST PAYABLE ON "STATE OR LOCAL BONDS," THE COMMISSION MAY, NONETHELESS, BE ABLE TO SATISFY THE REQUIREMENTS FOR THE DELIVERY OF THE PURCHASED 2007 A NOTES. IN SUCH EVENT, THE PURCHASER WOULD BE REQUIRED TO ACCEPT DELIVERY OF THE PURCHASED 2007 A NOTES.

Other Investment Considerations

Events which may occur prior to the Settlement Date may have significant consequences to investors who have agreed to purchase the 2007 A Notes on the Settlement Date. The values of the 2007 A Notes of each maturity on the Settlement Date will likely be greater or less than, the purchase prices therefor, and such differences may be substantial. Several factors may adversely affect such values including, but not limited to , a general increase in interest rates for all obligations and other indebtedness, any threatened or adopted change in the federal income tax laws affecting the relative benefits of owning tax-exempt securities versus other types of investments, such as fully taxable obligations, or any adverse development with respect to the Commission's results of operations, financial condition, or prospects or with respect to the ratings of the Commission's results of operations, financial condition, or prospects or with respect to the ratings of the Commission's general obligations or the 2007 A Notes. In addition, changes or proposed changes in federal income tax laws or regulations or interpretations thereof could affect the market value of tax-exempt securities generally, including, without limitation, the 2007 A Notes, without preventing the delivery of the 2007 A Notes at the Settlement.

Secondary Market Risk

The 2007 A Underwriter is not obligated to make a secondary market in the 2007 A Notes. No assurance is given that a secondary market will exist for the 2007 A Notes before the Settlement Date, and investors should assume that those notes will be illiquid during that period.

Market Value Risk

The market value of the 2007 A Notes on the Settlement Date could be greater or less than the purchase price paid by an investor, and the difference could be substantial. Changes in market value of the 2007 A Notes could result from general market conditions or other factors, including changes in the financial condition or operations of the commission. Neither the 2007 A Underwriter nor the Commission make any representation as to the market price of the 2007 A Notes as of the Settlement Date.

MISCELLANEOUS

Any statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Official Statement is not to be construed as a contract or agreement between the Commission and the purchasers or Holders of any of the Notes.

KENTUCKY ASSET/LIABILITY COMMISSION

By: /s/ John R. Farris
Chairman

By: /s/ F. Thomas Howard
Secretary

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APPENDIX A

INFORMATION PERTAINING TO THE UNIVERSITY OF KENTUCKY

This APPENDIX A contains certain financial and operating information regarding the University. Reference is made to APPENDIX C for additional financial and operating information. For additional information about the University of Kentucky, please refer to www.uky.edu.

GENERAL

Located in Lexington, the University of Kentucky is the Commonwealth of Kentucky's flagship institution of higher education. As a land grant institution, the University is dedicated to enriching people's lives through excellence in teaching, research and service and plays a critical leadership role for the state by promoting human and economic development that improves lives within Kentucky's borders and beyond.

The University has a presence in all 120 counties – through its Agricultural Extension Service— with an impact nationwide and abroad. Total enrollment is over 27,000 students, representing all Kentucky counties, every state in the nation, and 118 countries. In academic year 2005 - 2006, the University conferred nearly 5,500 degrees among its comprehensive academic programs. About 1,900 full-time faculty and 9,500 full-time staff are employed by the University.

The University consists of 16 colleges, plus the Graduate School. With 93 undergraduate programs, master's degrees in 99 fields, doctoral degrees in 66 programs, and four professional programs, the colleges include: Agriculture, Arts and Sciences, Business and Economics, Communications and Information Studies, Dentistry, Design, Education, Engineering, Fine Arts, Health Sciences, Law, Medicine, Nursing, Pharmacy, Public Health and Social Work. The University boasts more than 80 national rankings for academic excellence.

The University's William T. Young Library is among the world's leading research libraries; its book endowment is the largest among public universities and ranks second only to Harvard University among all universities. Its broad scope of technology offers students, faculty and Kentucky residents access to the most up-to-date information from online journals, government publications, and private studies, as well as more traditional materials.

The UK Chandler Medical Center, which opened in 1960, is considered one of the nation's finest academic medical centers. The faculty, students and staff take pride in achieving excellence in education, patient care, research, and community service. As one of two Level 1 Trauma Centers in the state and the first health-care facility in Central and Eastern Kentucky to obtain distinction as a Primary Stroke Center, UK Chandler Medical Center cares for the most critically injured and ill patients in the region. The 473-bed UK Chandler Medical Center and UK Children's Hospital (together, the "Hospital) are supported by more than 500 faculty physicians and dentists, 400 resident physicians, and a staff of 3,300 health professionals committed to high-quality patient care.

Research at the University is a dynamic enterprise encompassing both traditional scholarship and emerging technologies. The Advanced Science and Technology Commercialization Center, for example, is a hub for multidisciplinary research collaboration. It is just one of more than 50 research centers and institutes across campus, including the highly acclaimed Sanders-Brown Center on Aging, Morris K. Udall Parkinson's Disease Research Center of Excellence, and Markey Cancer Center, where University researchers are discovering and developing new treatments to improve health care, providing a rich training ground for the next generation of researchers, and advancing the State's economic growth.

During Fiscal Year 2006, the University faculty received a record-breaking total of $290.4 million in extramural funding for grants and contracts. The achievement marked an increase of six percent from last Fiscal Year and the fifth year in a row the University exceeded the $200 million level in sponsored project awards.

The University is committed to strong public service, reaching out to communities across the Commonwealth, sharing knowledge and making a difference in the towns, cities, and lives of all Kentuckians. An example is Health Education through Extension Leadership, a partnership between the College of Public Health, the College of Dentistry, the College of Agriculture, and the Cooperative Extension Service to enhance extension agents' capacity to deliver valuable health and wellness information throughout the state.

The University's agenda is simple – to be a catalyst for a new Commonwealth, one that is healthier, more prosperous and economically secure and that educates the state's best and brightest. The University is accelerating the movement toward academic excellence, becoming known worldwide for the quality of its academic programs, its commitment to undergraduates, its success in building a diverse community, and its engagement with the larger society.

The University operates on a fiscal year (the "Fiscal Year") that begins on July 1 and ends on June 30 and any reference to a particular fiscal Year means the Fiscal Year that ends on June 30 in the indicated year.

NOTE: Effective January 14, 1998, the Board of Trustees pursuant to the direction of the General Assembly (The Kentucky Postsecondary Education Improvement Act of 1997) delegated to the Board of Regents of the Kentucky Community and Technical College System (KCTCS), the management responsibilities for the University of Kentucky Community College System (UKCC) except for the Lexington Community College. This delegation of management responsibilities to KCTCS includes management of facilities and grounds, assets, liabilities, revenues, personnel, programs, financial and accounting services and support services. Governmental Accounting and Financial Reporting Standards provide that the financial operations of the UKCC no longer be included in the University financial reports as of July 1, 1997. Therefore, in general, statistical information in this Official Statement does not include Community Colleges (other than Lexington Community College).

Effective July 1, 2004, the Board of Trustees, pursuant to the direction of the Kentucky General Assembly, delegated to the Board of Regents of KCTCS the management of Lexington Community College. Therefore, in general, statistical information in this Official Statement does not include Lexington Community College for the Fiscal Years after 2004.

Governing Board

The governing body of the University is the Board consisting of twenty members, sixteen appointed by the Governor of the Commonwealth of Kentucky; two faculty members elected by the faculty; one student member, who is the President of the student body, or if he or she is not a full-time student who maintains permanent residence in the Commonwealth, a full-time student who does maintain permanent residency in the Commonwealth elected by the student body; and one member of the University staff. Pursuant to Section 164.160 of the Kentucky Revised Statutes, the Board is a body corporate with the powers usually vested in corporations and, as such, subject to the statutes of the Commonwealth, has control and management of the University, together with the properties and funds thereof.

Administrative Officers

The President of the University is Dr. Lee T. Todd, Jr.; the Provost is Kumble R. Subbaswamy; the Executive Vice President for Finance and Administration is Frank Butler; the Executive Vice President for Health Affairs is Dr. Michael Karpf; and the Treasurer of the University is Henry Clay Owen.

FISCAL YEAR 2007 BUDGET

The Fiscal Year 2007 budget for the University is $1,837,896,600, an increase of $147,004,500 from the final Fiscal Year 2006 budget.

OPERATIONS

Summary of Revenues, Expenses and Changes in Net Assets

The following is a summary of the University's revenues, expenses and changes in net assets for the most recent three Fiscal Year periods available:

	Fiscal Year (Dollars in Thousands)		
	2004	2005	2006[1]
Operating revenue	$1,060,909	$1,186,978	$1,327,407
Operating expenses	1,383,699	1,468,205	1,632,721
Operating loss	(322,790)	(281,227)	(305,314)
Non-operating revenue, including state appropriations	423,111	405,906	540,510
Increase in net assets	$100,321	$124,679	$235,196

[1]Preliminary

Enrollment

The following schedule indicates the Fall Semester head count and full-time equivalent enrollment at the University for each of the academic years 1997-98 through 2006-07. The full-time enrollment calculation is made in accordance with the method used by the United States Department of Education.

Academic Year[1]	Community College Head Count[3]	Community College Full-Time Equivalent[2,3]	Main Campus Head Count	Main Campus Full-Time Equivalent[2]	Total Head Count	Total Full-Time Equivalent[2]
1997-98	5,558	3,658	24,171	20,307	29,729	23,965
1998-99	6,118	4,035	24,394	20,729	30,512	24,764
1999-00	6,807	4,461	23,742	20,128	30,549	24,589
2000-01	7,150	4,685	23,816	20,150	30,966	24,835
2001-02	7,793	5,871	23,901	20,878	31,694	26,749
2002-03	8,270	6,251	24,985	21,872	33,255	28,122
2003-04	8,672	6,517	25,398	22,310	34,070	28,827
2004-05	N/A	N/A	26,545	22,604	26,545	22,604
2005-06	N/A	N/A	26,439	23,628	26,439	23,628
2006-07[4]	N/A	N/A	27,240	24,183	27,240	24,183

[1] Enrollment does not include the Community Colleges except for Lexington Community College.
[2] Full-time and part-time enrollment equated to full-time enrollment.
[3] As of June 30, 2004, Lexington Community College is part of KCTCS.
[4] Preliminary.

In reviewing enrollment projections, consideration has been given to planning for adequate academic and housing accommodations for future enrollments. The programs will be developed so that academic and housing facilities will not be limiting factors on the enrollment growth projected. The enrollment projection for the University is set forth in the following tabulations:

Academic Year	Main Campus Fall Semester Student Enrollment (Full-Time Equivalent)[1]
2007-2008[1]	24,250
2008-2009	24,500
2009-2010	25,000
2010-2011	25,500
2011-2012	26,000

[1] Projections based on 2006-2007 data

Approximately 23% of the students enrolled in the University are non-residents of Kentucky and it is anticipated that the percentage of non-resident enrollments will remain at this level in future years.

Admissions Information – Fall Semester
Undergraduate Admissions

The following is a summary of certain undergraduate admission information for the most recent five years:

	2002	2003	2004	2005	2006[1]
Number of Applications	8,879	9,418	10,604	10,515	10,024
Number Approved for Enrollment	7,250	7,603	8,353	8,123	8,073
Number Enrolled	3,718	3,688	3,961	3,844	4,192
Average ACT Scores (First time full-time Freshman)	24.03	24.5	24.2	24.745	24.6

[1] Preliminary

State Appropriations

The following is a summary of the University's General Fund state appropriations for the most recent ten Fiscal Years:

Fiscal Year	Appropriation
1998	$278,934,000 [1]
1999	286,475,000 [1]
2000	290,640,000 [1]
2001	307,821,000 [1]
2002	303,639,000 [1]
2003	304,735,000 [1]
2004	302,539,000 [1]
2005	295,807,600 [2, 3]
2006	314,293,600 [3, 4]
2007	318,567,900 [3,5]

[1] Does not include the Community Colleges appropriations except for Lexington Community College.
[2] Includes $7,749,500 in Fiscal Year 2005 for debt service.
[3] Does not include the Community Colleges appropriations except for Lexington Community College debt service appropriation.
[4] Includes $7,960,400 in Fiscal Year 2006 for debt service.
[5] Includes $6,622,600 in Fiscal Year 2007 for debt service.

The amount of funds appropriated has been based in part on the debt service on the University's outstanding Consolidated Educational Buildings Revenue Bonds. The amounts set forth above, except for Fiscal Year 2007, are amounts actually received, which, in certain years, have been less than amounts included in the original state budget for that year. The Board presently intends, but is not obligated, to continue to seek to have funds appropriated by the General Assembly to partially support the operations of the University. THE GENERAL ASSEMBLY IS NOT NOW OBLIGATED, NOR WILL THERE BE AN OBLIGATION IN THE FUTURE TO MAKE APPROPRIATIONS TO THE UNIVERSITY. IN ADDITION, THERE CAN BE NO ASSURANCE THAT IN THE PERFORMANCE OF HIS OR HER OBLIGATION TO BALANCE THE STATE BUDGET ANNUALLY, THE GOVERNOR WILL NOT REDUCE OR ELIMINATE ANY APPROPRIATIONS WHICH ARE MADE.

Grants and Contracts

The following is a summary of the University's grant and contract amounts for the most recent ten Fiscal Years:

Fiscal Year	Amount
1997	$114,686,921
1998	119,852,159
1999	124,819,725 [1]
2000	128,116,917 [1]
2001	146,914,931 [1]
2002	170,378,424 [1]
2003	197,651,327 [1]
2004	218,890,770 [1]
2005	250,381,051 [1]
2006	271,367,504 [2, 3]

[1] Does not include Community Colleges Student Financial Aid except for Lexington Community College.
[2] Does not include any Community College Student Financial Aid
[3] Preliminary

Student Financial Aid

The following is a summary of the University's student financial aid for the most recent ten Fiscal Years:

Fiscal Year	Amount
1997	$139,075,157
1998	146,673,202
1999	108,902,995 [1]
2000	110,992,616 [1]
2001	129,340,356 [1]
2002	139,411,538 [1]
2003	167,461,348 [1]
2004	184,255,947 [1]
2005	171,972,107 [2]
2006	173,241,037 [2, 3]

[1] Does not include Community Colleges Student Financial Aid except for Lexington Community College.
[2] Does not include Community Colleges Student Financial Aid or Lexington Community College.
[3] Preliminary

Comparative Report of Student Financial Aid

The following is a comparative summary of the University's student financial aid for the two most recent Fiscal Years:

	Fiscal Year	
	2005	2006[1]
Scholarships & Grants	$35,212,154	$31,242,484
Federal Grants		
Pell	9,564,371	8,837,607
Supplemental Educational Opportunity Grant (SEOG)	1,114,501	671,917
College Work Study	1,150,954	1,158,491
Financial Aid from Outside Agencies		
Federal Grants (FAFSA)	1,060,162	1,052,338
State Grants	19,459,771	20,710,532
Agency Scholarships	9,096,170	6,187,044
Loans		
National Direct Student Loans (Perkins)	3,567,381	3,318,690
Health Professions	544,720	421,200
Guaranteed Student Loans – Outside Agencies	84,663,694	89,587,843
Other	6,538,229	10,052,891
Total Program Expenditures	$171,972,107	$173,241,037

[1] Preliminary

The University of Kentucky Hospital

History and Background. The Hospital is an organizational unit of the University. It holds a position of leadership as a statewide, regional, and national tertiary referral hospital. Initial funds for the University Hospital were appropriated by the 1956 General Assembly, and the first patients were admitted to the University Hospital in 1962.

In its commitment to quality care, the Hospital and the Hospital's medical staff representing all medical and surgical specialties, provides a full scope of services, such as extensive pediatric services offering sophisticated neonatal intensive care, renal, bone marrow and solid organ transplant programs, and comprehensive high-risk obstetrical services. The Hospital and its staff are leaders in developing and refining new technology including imaging and comprehensive medical, surgical, cancer, geriatric, cardiac, and burn specialty programs. Patients benefiting from these services come from all of Kentucky's counties, contiguous states, other states, and many foreign countries.

Relationship to Other Units of the Medical Center. Within the Albert B. Chandler Medical Center, along with the Hospital, there are the Colleges of Medicine, Nursing, Dentistry, Pharmacy, Public Health, and Health Sciences.

In its support of the Medical College, the Hospital provides a facility for teaching and research. The medical college annually graduates approximately 95 physicians and supervises the clinical experience of 490 post-graduate physicians each year. The facilities at the medical school adjoin the Hospital containing lecture halls, classroom space, offices, and laboratories.

The primary function of the College of Medicine is the education of physicians through a four-year doctor of medicine degree (M.D.) program and three to seven year residency programs which are offered in 29 medical and surgical subspecialties. In addition, masters (M.S.), doctoral (PhD), and post-doctoral programs are offered in five basic science areas. The College of Medicine also operates the Sanders Brown Research Center on Aging, which is among the nation's leaders in Alzheimer's disease research. The Center is engaged in the multi-disciplinary study of the problems of aging. Both inpatient hospital and ambulatory patient care services are provided by the faculty of the College of Medicine within the Medical Center, as well as a number of clinical practice settings principally in Eastern Kentucky in conjunction with the University's four Area Health Education Center Affiliations in Berea, Hazard, Williamstown and Morehead.

The other colleges within the Medical Center, Nursing, Dentistry, Pharmacy, Public Health, and Health Sciences also use the University Hospital as a prime teaching site for students and residents and patient care facility to carry out their mission of research and education.

Hospital Mission, Vision And Critical Success Factors. The Hospital recognizes the need for organizational planning to maintain its position as a quality health care provider. The Hospital's mission is to help people of the Commonwealth and beyond gain and retain good health through creative leadership and quality initiatives in patient care, education and research. To achieve this Mission the Hospital has set a Vision of being a top 20 public academic health center, recognized nationally and internationally for excellence in patient care, education and research.

Hospital Administration. The Executive Vice President for Health Affairs is Michael Karpf; the Vice President for Health Affairs and CFO of the HealthCare Enterprise is Sergio Melgar; the Chief Medical Officer is Richard P. Lofgren, M.D., M.P.H.; the Chief Information Officer for the UK Healthcare Enterprise is Zed E. Day; the Associate Vice President for Medical Center Operations is Murray B. Clark, Jr.; and the Chief Nursing Officer/Associate Hospital Director is Karen Stefaniak, RN, Ph.D.

Hospital Operating Results and Financial Condition.

Statement of Revenue, Expenses and Changes In Net Assets. The following is a summary of the University Hospital's revenue, expenses and changes in net assets for each of Fiscal Years 2004, 2005 and 2006.

	2004	2005	2006[1]
	(Dollars in Thousands)		
Operating revenue	$371,982	$441,935	$514,819
Operating expenses	341,323	404,777	484,245
Operating income	30,659	37,158	30,574
Net non-operating revenue (expenses)	(2,985)	8,502	45,782
Net income before other revenues, expenses, gains or losses	27,674	45,660	76,356
Transfer to University	(9,478)	(17,305)	(11,156)
Net loss from discontinued operations	(109)	(40)	(43)
Increase in net assets	$18,087	$28,315	$65,157

Certain Operating Information

	2004	2005	2006[1]
Average Licensed Beds	473	473	473
Available Beds	406	436	462
Patient Days	112,575	122,704	134,520
Patient Days Equivalents[2]	172,046	191,892	206,672
Admissions	19,677	22,312	24,754
Discharges	19,644	22.269	24,760
Average Length of Stay (days)	5.72	5.51	5.43
Occupancy	75.37%	77.13%	79.69%
Emergency Visits	40,320	42,909	44,646
Outpatient Visits with Hospital Charge	246,546	266,245	275,608

[1] Preliminary
[2] Total patient activity computed by converting outpatient activity to an inpatient equivalent.

OUTSTANDING BONDS OF THE UNIVERSITY OF KENTUCKY

The University will have the following bonds outstanding as of October 18, 2006 after giving effect to the issuance of the 2006 Notes and the refunding of the Refunded Bonds.

Consolidated Educational Buildings Revenue Bonds

	Year of Issue	Amount of Issue	Amount Outstanding	Year Of Final Maturity
Series M (2nd Series)	1998	$4,695,000	$3,740,000	2011
Series N (2nd Series)	2001	18,795,000	11,465,000	2012
Series K (3rd Series)	2003	5,115,000	3,020,000	2010
Series S	2003	29,775,000	27,635,000	2024
Series T	2003	17,635,000	16,005,000	2023
Series O (2nd Series)	2003	9,335,000	7,355,000	2015
Series E, J & L (3rd Series)	2004	19,520,000	11,260,000	2011
Series P, Q & R (2nd Series)	2004	52,110,000	47,475,000	2021
Series U	2005	11,495,000	11,215,000	2025
TOTAL		$168,475,000	$139,170,000	

Library Bonds (issued by the Lexington-Fayette Urban County Government)

	Year of Issue	Amount of Issue	Amount Outstanding	Year of Final Maturity
1998 Series	1998	$43,420,000	$40,250,000	2025

Obligations Outstanding Under the Trust Agreement

	Year of Issue	Amount of Issue	Amount Outstanding	Year of Final Maturity
Kentucky Asset/Liability Commission General Receipts Project Notes, 2005 Series A	2005	$107,540,000	$107,540,000	2025
Kentucky Asset/Liability Commission General Receipts Refunding Project Notes, 2006 Series A	2006	66,305,000	66,305,000	2022
Kentucky Asset/Liability Commission General Receipts Taxable Refunding Project Notes, 2006 Series B	2006	2,220,000	2,220,000	2007
Total ALCo Notes*		$176,065,000	$176,065,000	
University of Kentucky, General Receipts Bonds				
2005 Series A Bonds	2005	7,160,000	6,915,000	2025
2006 Series A Bonds	2006	24,325,000	24,325,000	2026
Total UK Bonds		$31,485,000	$31,240,000	
Total Under Trust Agreement		$207,550,000	$207,305,000	

Please refer to the financial statements included in "APPENDIX C" for additional obligations of the University.

*Excludes the 2007 A Notes to be delivered on or about November 1, 2007.

TOTAL ANNUAL DEBT SERVICE REQUIREMENTS

Year Ending June 30	Existing Debt Service*	Principal	Interest	Total	Total Debt Service*
2007	$27,372,549.93	$150,000.00	$1,346,996.91	$1,496,996.91	$28,869,546.84
2008	25,716,485.04	2,745,000.00	4,524,595.85	7,269,595.85	32,986,080.89
2009	25,735,278.77	2,870,000.00	6,672,037.52	9,542,037.52	35,277,316.29
2010	30,097,311.27	3,005,000.00	6,540,312.52	9,545,312.52	39,642,623.79
2011	29,304,905.02	5,875,000.00	6,335,162.52	12,210,162.52	41,515,067.54
2012	26,616,303.15	6,655,000.00	6,066,312.52	12,721,312.52	39,337,615.67
2013	24,383,271.26	6,965,000.00	5,756,787.52	12,721,787.52	37,105,058.78
2014	24,375,126.26	7,300,000.00	5,423,387.52	12,723,387.52	37,098,513.78
2015	24,380,515.01	7,635,000.00	5,081,312.52	12,716,312.52	37,096,827.53
2016	23,433,353.76	8,010,000.00	4,710,825.02	12,720,825.02	36,154,178.78
2017	23,440,202.51	8,395,000.00	4,325,437.52	12,720,437.52	36,160,640.03
2018	23,443,933.76	8,800,000.00	3,921,390.64	12,721,390.64	36,165,324.40
2019	22,950,980.63	9,220,000.00	3,502,446.88	12,722,446.88	35,673,427.51
2020	25,370,336.25	9,645,000.00	3,069,887.50	12,714,887.50	38,085,223.50
2021	20,585,550.63	10,110,000.00	2,612,662.50	12,722,662.50	33,308,213.13
2022	19,054,191.26	9,775,000.00	2,152,512.50	11,927,512.50	30,981,703.76
2023	19,043,481.26	10,235,000.00	1,689,500.00	11,924,500.00	30,967,981.26
2024	17,735,187.51	5,240,000.00	1,321,000.00	6,561,000.00	24,296,187.51
2025	18,776,775.01	5,510,000.00	1,052,250.00	6,562,250.00	25,339,025.01
2026	11,492,740.63	5,795,000.00	769,625.00	6,564,625.00	18,057,365.63
2027	1,830,275.00	6,090,000.00	472,500.00	6,562,500.00	8,392,775.00
2028		6,405,000.00	160,125.00	6,565,125.00	6,565,125.00
Total	$465,138,753.92	$146,430,000.00	$77,507,067.96	$223,937,067.96	$689,075,821.88

*Does not include rental payments due under capital leases with State Property and Buildings Commission. Also excludes debt service on all Refunded Bonds.

PLEDGED REVENUES – GENERAL RECEIPTS
UNIVERSITY OF KENTUCKY
FISCAL YEAR ENDING JUNE 30, 2005

Revenue Type	2005 Amount (000's)	Pledged (000's)	Prior Pledge Debt Service (000's)	Net General Receipts Pledged Revenues (000's)
Student tuition and fees	$133,389	$133,389	$19,364	$114,025
Nongovernmental grants and contracts	30,113	5,326		5,326
Recoveries of facilities and administrative costs	40,333	40,333		40,333
Sales and services	38,857	38,857		38,857
Hospital patient services	440,609	440,609		440,609
Auxiliary enterprises - housing and dining	32,142	32,142	6,314	25,828
Auxiliary enterprises - other	20,699	20,699		20,699
Other operating revenue	465	465		465
State appropriations	287,897	287,897		287,897
Gifts and grants	24,638	709		709
Investment income	56,517	13,638		13,638
TOTAL	$1,105,659	$1,014,064	$25,678	$988,386

PLEDGED REVENUES – GENERAL RECEIPTS
UNIVERSITY OF KENTUCKY
FISCAL YEAR ENDING JUNE 30, 2006[1]

Revenue Type	2006 Amount (000's)	Pledged (000's)	Prior Pledge Debt Service (000's)	Net General Receipts Pledged Revenues (000's)
Student tuition and fees	$147,267	$147,267	$18,162	$129,105
Nongovernmental grants and contracts	33,531	7,543		7,543
Recoveries of facilities and administrative costs	43,303	43,303		43,303
Sales and services	42,826	42,826		42,826
Hospital patient services	511,441	511,441		511,441
Auxiliary enterprises - housing and dining	40,781	40,781	6,314	34,467
Auxiliary enterprises - other	20,633	20,633		20,633
Other operating revenue	2,222	2,222		2,222
State appropriations	314,294	314,294		314,294
Gifts and grants	32,189	1,123		1,123
Investment income	115,495	51,632		51,632
TOTAL	$1,303,982	$1,183,065	$24,476	$1,158,589

[1] Preliminary

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APPENDIX B

SUMMARY OF THE TRUST AGREEMENT

The following is a summary of certain provisions of the Trust Agreement dated as of November 1, 2005, between the University and U.S. Bank National Association, as Trustee. This summary is not to be regarded as a complete statement of the Trust Agreement to which reference is made for a complete statement of the actual terms thereof. Copies of the Trust Agreement are on file with the Trustee.

Defined Terms

The terms defined below are among those used in the Official Statement and in this summary of the Trust Agreement. Except where otherwise indicated or provided, words in the singular number include the plural as well as the singular number and vice versa.

"Act" means Sections 162.340 to 162.380 of the Kentucky Revised Statutes, Chapter 56 of the Kentucky Revised Statutes and Sections 58.010 to 58.140 of the Kentucky Revised Statutes as the same may be amended, modified, revised, supplemented, or superseded from time to time.

"Additional Obligation Instruments" means agreements providing for the repayment of money that the University may, from time to time, be authorized to enter into under the laws of the Commonwealth. The definition of Additional Obligation Instruments does not include "Bond" or "Bonds," "Note" or "Notes," Financing Agreements or SPBC Leases.

"ALCo" means the Kentucky Asset/Liability Commission and any successor thereto.

"Authenticating Agent" means the Trustee and the Registrar for the series of Obligations and any bank, trust company or other Person designated as an Authenticating Agent for such series of Obligations by or in accordance with the Trust Agreement.

"Beneficial Owner" means, with respect to the Obligations, a Person owning a Beneficial Ownership Interest therein, as evidenced to the satisfaction of the Trustee.

"Beneficial Ownership Interest" means the beneficial right to receive payments and notices with respect to a series of Obligations which are held by a Depository under a Book Entry System.

"Board" means the Board of Trustees of the University, or if there shall be no such Board of Trustees, such Person or body which, pursuant to law or the organizational documents of the University, is vested with the power to direct the management and policies of the University, and shall include any committee empowered to act on behalf of such board or body.

"Bond" or "Bonds" means any bond, or all of the bonds, or an issue or series of bonds, as the case may be, as so identified in the certificate of the Fiscal Officer, of the University issued pursuant to the 2005 General Bond Resolution, a Series Resolution and the Trust Agreement. The definition of Bond and Bonds does not include "Note" or "Notes," Financing Agreements, SPBC Leases or Additional Obligation Instruments.

"Bond Counsel" means an attorney or firm of attorneys of nationally recognized standing on the subject of municipal bonds selected by the University or its counsel and acceptable to the Trustee.

"Book Entry Form" or "Book Entry System" means, with respect to the Obligations, a form or system, as applicable, under which (a) the Beneficial Ownership Interests may be transferred only through a book entry and (b) physical Obligation certificates in fully registered form are registered only in the name of a Depository or its nominee as Holder, with the physical Obligation certificates "immobilized" in the custody of the Depository. The Book Entry System maintained by and the responsibility of the Depository and not maintained by or the responsibility of the University or the Trustee is the record that identifies, and records the transfer of the interests of, the owners of book entry interests in the Obligations.

"Business Day" means a day of the year, other than a Saturday or Sunday, on which banks located in the city in which the principal corporate trust office of the Trustee is located are not required or authorized to remain closed or a day on which The New York Stock Exchange is not closed.

"Certificate of Award" means, with respect to any series of Obligations, the Certificate of Award for such series, if any, authorized in the applicable Series Resolution or the contract of purchase for such series of Obligations.

"Commonwealth" means the Commonwealth of Kentucky.

"Costs of University Facilities" means the costs of or related to University Facilities, and the financing thereof, for the payment of which Obligations may be issued under the Act.

"Credit Support Instrument" means an irrevocable letter of credit, line of credit, standby bond purchase agreement, insurance policy, guaranty or surety bond or similar instrument providing for the payment of or guaranteeing the payment of principal or purchase price of and interest on Obligations when due, either to which the University is a party or which is provided at the request of the University.

"Credit Support Provider" means the provider of a Credit Support Instrument.

"Debt Service Charges" means, generally, for any applicable time period, (i) the principal (including any Mandatory Sinking Fund Requirements), interest and redemption premium, if any, required to be paid by the University on Obligations pursuant to any Series Resolution, less any capitalized interest for such time period and accrued interest on deposit in the Debt Service Payment Account; (ii) any amounts due to a Credit Support Provider to the extent as set forth in a Credit Support Instrument; and (iii) any amounts due to a Hedge Provider to the extent as set forth in an Interest Rate Hedge Agreement.

"Debt Service Fund" means the Debt Service Fund authorized and created pursuant to the Trust Agreement.

"Debt Service Payment Account" means the Debt Service Payment Account within the Debt Service Fund authorized and created pursuant to the Trust Agreement.

"Debt Service Reserve Account" means the Debt Service Reserve Account authorized and created pursuant to the Trust Agreement.

"Depository" means any securities depository that is a clearing agency under federal law operating and maintaining, together with its participants a Book Entry System to record beneficial ownership of a series of Obligations, and to effect transfers of such Obligations, in Book Entry Form, and includes the Depository Trust Company (a limited purpose trust company), New York, New York.

"Direct Participant" means a Participant as defined in the Letter of Representations.

"Eligible Investments" means any investment authorized by Section 42.500 and 56.520(5) of the Kentucky Revised Statutes, as the same may be amended, modified, revised, supplemented, or superseded from time to time.

"Extraordinary Services" and "Extraordinary Expenses" means all services rendered and all reasonable expenses (including counsel fees) properly incurred by the Trustee under the Trust Agreement, other than Ordinary Services and Ordinary Expenses. Extraordinary Services and Extraordinary Expenses shall specifically include services rendered or expenses incurred by the Trustee in connection with, or in contemplation of, an Event of Default.

"Event of Default" means an Event of Default as defined at the caption "Events of Default" in this Appendix B.

"Financial Statements" means the University's Annual Consolidated Financial Statements.

"Financing Agreement" means a "Financing Agreement" as defined in Chapter 56 of the Kentucky Revised Statutes between the University and ALCo or the applicable state agency as then provided by law. The definition of Financing Agreement does not include "Bond" or "Bonds," "Note" or "Notes" or Additional Obligation Instruments, but may also mean an SPBC Lease.

"Fiscal Officer" means either the Treasurer of the University or such other person designated by the Chairman of the Board to act as Fiscal Officer for purposes of the Trust Agreement.

"Fiscal Year" means a period of twelve consecutive months constituting the fiscal year of University commencing on the first day of July of any year and ending on the last day of June of the next succeeding calendar year, both inclusive, or such other consecutive twelve month period as hereafter may be established from time to time for budgeting and accounting purposes of the University by the Board to be evidenced, for purposes of the Financing Agreement, by a certificate of a Fiscal Officer filed with the Trustee.

"Fitch" means Fitch Ratings.

"General Receipts" means, as reported in the Financial Statements (having the designations, to the extent not otherwise defined in the Financing Agreement, set forth in the Financial Statements or such successor designations that may hereafter be used in Financial Statements):

> (a) certain operating and non-operating revenues of the University, being (i) Student Registration Fees, (ii) nongovernmental grants and contracts, (iii) recoveries of facilities and administrative costs, (iv) sales and services, (v) Hospital Revenues, (vi) Housing and Dining Revenues, (vii) auxiliary enterprises – other auxiliaries, (viii) other operating revenues, (ix) state appropriations (for general operations), (x) gifts and grants, (xi) investment income, (xii) other nonoperating revenues and (xiii) other;

> (b) but excluding (i) any receipts described in clause (a) which are contracts, grants, gifts, donations or pledges and receipts therefrom which, under restrictions imposed in such contracts, grants, gifts, donations or pledges, or, which as a condition of the receipt thereof or of amounts payable thereunder are not available for payment of Debt Service Charges, (ii) federal grants and contracts, (iii) state and local grants and contracts, (iv) federal appropriations, (v) county appropriations, (vi) professional clinical service fees, (vii) auxiliary enterprises – athletics; (viii) capital appropriations, (ix) capital grants and gifts, and (x) additions to permanent endowments, including research challenge trust funds;

provided, however, that General Receipts may

> (c) include any other receipts that may be designated as General Receipts from time to time by a resolution of the Board delivered to the Trustee; and

(d) exclude any receipts not pledged under the Trust Agreement, which may be designated from time to time by a resolution of the Board delivered to the Trustee;

(e) exclude any receipts pledged under the Trust Agreement, which may be designated from time to time by a resolution of the Board delivered to the Trustee and each Rating Service then rating any Obligations, but only if each such Rating Service confirms in writing to the University that the exclusion of any such receipt would not cause a reduction or withdrawal of the then current rating on any Outstanding Obligations.

"Government Bonds" means (a) direct obligations of the United States of America for the payment of which the full faith and credit of the United States of America is pledged, (b) obligations issued by a Person controlled or supervised by and acting as an instrumentality of the United States of America, the payment of the principal of, premium, if any, and interest on which is fully guaranteed as a full faith and credit obligation of the United States of America (including any securities described in (a) or (b) issued or held in book-entry form on the books of the Department of Treasury of the United States of America or Federal Reserve Bank), and (c) securities which represent an interest in the obligations described in (a) and (b) above.

"Hedge Provider" means the provider of an Interest Rate Hedge Agreement.

"Holder" means any Person in whose name a registered Obligation is registered; provided that ALCo, or its assignee, shall be the Holder of any Financing Agreement and SPBC, or its assignee, shall be the Holder of any SPBC Lease.

"Hospital Revenues" means operating revenues having the designation "hospital services" in the Financial Statements or any successor designation or designations for such receipts that may hereafter be used in Financial Statements.

"Housing and Dining Bonds" means Obligations, the proceeds of which will be used to pay Costs of University Facilities which constitute Housing and Dining Facilities.

"Housing and Dining Facilities" means Housing and Dining Facilities, as defined in the Prior Housing Indenture.

"Housing and Dining Revenues" means operating revenues (auxiliary enterprises) having the designation "housing and dining" in the Financial Statements or any successor designation or designations for such receipts that may hereafter be used in Financial Statements.

"Indirect Participant" means a Person utilizing the Book Entry System of the Depository by, directly or indirectly, clearing through or maintaining a custodial relationship with a Direct Participant.

"Interest Payment Dates" means the dates specified in the applicable Series Resolution or Certificate of Award on which interest on the Obligations or any series of Obligations is to be paid.

"Interest Rate Hedge Agreement" means an interest rate swap, an interest rate cap or other such arrangement obtained, either directly by the University (or the Trustee on behalf of the University) or through ALCo, with the goal of lowering the effective interest rate to the University on Obligations or hedging the exposure of the University with respect to its obligations on the Obligations against fluctuations in prevailing interest rates.

"Letter of Representations" means the Blanket Letter of Representations from the University to the Depository.

"Mandatory Sinking Fund Requirements" means amounts required by any Series Resolution or the Certificate of Award to be deposited to the Debt Service Payment Account in any fiscal year for the purpose of retiring principal maturities of Obligations which by the terms of such Obligations are due and payable, if not called for prior redemption, in any subsequent fiscal year.

"Maximum Annual Debt Service" means the highest amount of (i) Debt Service Charges plus (ii) the principal of and interest on all Prior Obligations that are outstanding under the terms of the Prior Basic Resolution or the Prior Housing Indenture, for the current or any future Fiscal Year.

"Moody's" means Moody's Investors Service, Inc., a Delaware corporation, and its successors and assigns.

"Notes" or "Note" means any note or all of the notes, or an issue of notes, as the case may be, as so identified in the certificate of the Fiscal Officer issued by the University in anticipation of the issuance of Obligations or receipt of grants or appropriations to pay Costs of University Facilities, or to pay costs of refunding or retirement of Notes previously issued pursuant to the Act, the 2005 General Bond Resolution, a Series Resolution and the Trust Agreement. The definition of Note and Notes does not include "Bond" or "Bonds," Financing Agreements, SPBC Leases or Additional Obligation Instruments.

"Obligations" means Bonds, Notes, Financing Agreements, SPBC Leases and Additional Obligation Instruments.

"Ordinary Services" and "Ordinary Expenses" means those services normally rendered and those expenses (including counsel fees) normally incurred by a trustee under instruments similar to the Trust Agreement.

"Original Purchaser" means, as to any Obligations, the Person or Persons expressly named in the applicable Series Resolution or the Certificate of Award as the original purchaser of those Obligations from the University.

"Outstanding" means, as of any date, Notes and Bonds which have been authenticated, and with respect to all Obligations, have been delivered, or are then being delivered, by the Trustee or the University under the Trust Agreement except:

(a) Obligations surrendered for exchange or transfer or canceled because of payment or redemption at or prior to such date;

(b) Obligations for the payment, redemption or purchase for cancellation of which sufficient moneys have been deposited prior to such date with the Trustee or Paying Agents (whether upon or prior to the maturity or redemption date of any such Obligations), or which are deemed to have been paid and discharged pursuant to the provisions of the Trust Agreement; provided that if such Obligations are to be redeemed prior to the maturity thereof, notice of such redemption shall have been given or arrangements satisfactory to the Trustee shall have been made therefor, or waiver of such notice satisfactory in form to the Trustee shall have been filed with the Trustee, and provided, further, that if such Obligations are to be purchased for cancellation, a firm offer for sale stating the price has been received and accepted; and

(c) Lost, stolen, mutilated or destroyed Obligations in lieu of which others have been authenticated, if applicable, (or payment, when due, of which is made without replacement) under the Trust Agreement.

"Paying Agents" means any banks or trust companies designated as the paying agencies or places of payment for Obligations by or pursuant to the applicable Series Resolution, and their successors designated pursuant to the Trust Agreement, and shall also mean the Trustee when so designated for such purpose.

"Person" means an individual, a corporation, a partnership, an association, a joint stock company, a joint venture, a trust, an unincorporated organization, or a government or any agency or political subdivision thereof.

"Predecessor Obligation" of any particular Obligation means every previous Obligation evidencing all or a portion of the same debt as that evidenced by the particular Obligation. For the purposes of this definition, any Bond or Note authenticated and delivered under the Trust Agreement in lieu of a lost, stolen or destroyed Bond or Note shall, except as otherwise provided in the Trust Agreement, be deemed to evidence the same debt as the lost, stolen or destroyed Bond or Note.

"Prior Basic Resolution" means the resolution adopted by the Board on September 20, 1960, that has provided for the issuance of Consolidated Educational Buildings Revenue Bonds of the University.

"Prior Financing Documents" means, collectively, the Prior Basic Resolution and the Prior Housing Indenture.

"Prior Funds" means all funds and accounts created by the Prior Financing Documents that are pledged as security and a source of payment of bonds and notes issued thereunder.

"Prior Housing Indenture" the Trust Indenture and Supplemental Trust Indenture dated as of June 1, 1965 (and all supplemental indentures related thereto) between the University and Farmers' Bank & Capital Trust Company that, has provided for the issuance of Housing and Dining Bonds.

"Prior Obligations" means any notes or bonds that are outstanding under the Prior Financing Documents.

"Prior Pledged Funds" means, collectively, all funds and accounts created under the Prior Financing Documents.

"Prior Pledged Revenues" means amounts required to be deposited in the "Revenue Fund" created by the Prior Basic Resolution and in the "System Revenue Fund" created by the Prior Housing Indenture.

"Project Fund" means the Project Fund created pursuant to the Trust Agreement.

"Purchase Price" means, as to any series of Obligations, the amount provided for in the Series Resolution and the Certificate of Award authorized thereby, plus accrued interest, if any, on the aggregate principal amount of those Obligations from their date to the date of their delivery to the Original Purchaser and payment therefor.

"Rating Service" means Fitch, Moody's, S&P or any other nationally recognized rating service.

"Redemption and Purchase Account" means the Redemption and Purchase Account authorized and created pursuant to the Trust Agreement.

"Register" means the books kept and maintained by the Registrar for the registration and transfer of Obligations pursuant to the Trust Agreement.

"Registrar" means, with respect to a series of Obligations, the keeper of the Register for those Obligations, which shall be the Trustee except as may be otherwise provided by or pursuant to the Series Resolution for those Obligations, each of which shall be a transfer agent registered in accordance with Section 17(A)(c) of the Securities Exchange Act of 1934.

"Regular Record Date" means, with respect to any Obligation and unless otherwise provided in the Series Resolution authorizing the particular series of Obligations, the fifteenth day of the calendar month next preceding an Interest Payment Date applicable to that Obligation.

"Reimbursement Agreement" means, with respect to a series of Obligations, any agreement or agreements between one or more Credit Support Providers and the University under or pursuant to which a Credit Support Instrument for such series of Obligations is issued or provided and which sets forth the respective obligations of the University and of the Credit Support Provider.

"Remarketing Agent" means any entity which acts as the remarketing agent with respect to a series of Obligations.

"Revenue Fund" means the Revenue Fund authorized and created pursuant to the Trust Agreement.

"S&P" means Standard & Poor's Rating Services, a Division of The McGraw Hill Companies, and its successors and assigns.

"Series Resolution" means a Resolution of the Board authorizing one or more series of Obligations and the execution and delivery of a Supplemental Trust Agreement, all in accordance with the 2005 General Bond Resolution and the Trust Agreement.

"SPBC" means the State Property and Buildings Commission of the Commonwealth and any successor thereto.

"SPBC Lease" means a lease between the University and SPBC or the applicable state agency as then provided by law. The definition of SPBC Lease does not include "Bond" or "Bonds," "Note" or "Notes" or Additional Obligation Instruments, but may also mean a Financing Agreement.

"Special Funds" means the Debt Service Fund and accounts therein and any other funds or accounts permitted by, established under, or identified in the Trust Agreement or a Series Resolution and designated as Special Funds. The Revenue Fund shall not be a Special Fund.

"Student Registration Fees" means operating revenues having the designation "student tuition and fees" in the Financial Statements or any successor designation or designations for such receipts that may hereafter be used in Financial Statements.

"Subordinated Indebtedness" means obligations which, with respect to any issue thereof, are secured by a pledge of the General Receipts which is subordinate to that of the holders of Obligations and which are evidenced by instruments, or issued under an indenture or other document, containing provisions for the subordination of such obligations.

"Supplemental Trust Agreement" means any one or more of Supplemental Trust Agreements entered into by the parties pursuant to the Trust Agreement and a Series Resolution.

"Tender Agent" means any entity which acts as a tender agent for a series of Obligations.

"Trust Agreement" means the Trust Agreement, dated as of November 1, 2005, between the University and the Trustee, as the same may be duly amended, modified or supplemented in accordance with its terms.

"Trustee" means the Trustee at the time serving under the Trust Agreement, originally U.S. Bank National Association and any successor Trustee as determined or designated under or pursuant to the Trust Agreement.

"2005 General Bond Resolution" means the resolution of the Board adopted on September 20, 2005, authorizing the execution and delivery of the Trust Agreement.

"University" means the University of Kentucky, a public body corporate, and an educational institution and agency of the Commonwealth of Kentucky, and every part and component thereof as from time to time existing, and when the context requires, includes the Board.

"University Facilities" means buildings and appurtenances to be used in connection with the University for educational purposes, including, but not limited to any Authorized Project, any Building, any Building project and any Public project, as those terms are defined in the Act, and further includes any one, part of, or any combination of such facilities, and further includes site improvements, utilities, machinery, furnishings and any separate or connected buildings, structures, improvements, sites, open space and green space areas, utilities or equipment to be used in, or in connection with the operation or maintenance of, or supplementing or otherwise related to the services or facilities to be provided by such facilities.

Any reference in the Financing Agreement to the University, the Board, or to any officers or to other public boards, commissions, departments, institutions, agencies, bodies, entities or officers, shall include those which succeed to their functions, duties or responsibilities pursuant to or by operation of law or who are lawfully performing their functions. Any reference to a section or provision of the Kentucky Revised Statutes or to the laws of Kentucky shall include such section or provision and such laws as from time to time amended, modified, revised, supplemented, or superseded, provided that no such amendment, modification, revision, supplementation, or super session shall alter the obligation to pay the Debt Service Charges in the amount and manner, at the times, and from the sources provided in this Resolution, the applicable Series Resolution, and the Trust Agreement, except as otherwise permitted in the Trust Agreement.

Debt Service Fund and Other Special Funds

The Trustee will hold and administer the Debt Service Fund and any other Special Fund created under the Trust Agreement, together with the accounts contained therein, upon the terms and conditions, including, without limitation, the terms and conditions set forth in the Trust Agreement and the applicable Series Resolution and/or Supplemental Trust Agreement for the investment of moneys deposited in such Funds, set forth in the applicable Series Resolution and the Trust Agreement.

There will be maintained in the Debt Service Fund the following Accounts: the Debt Service Payment Account, the Debt Service Reserve Account and the Redemption and Purchase Account. The Trustee will maintain a separate subaccount within the Debt Service Payment Account for each series of Obligations and each separate subaccount will secure only the particular series of Obligations to which it is related. (Section 4.01)

Use of Debt Service Payment Account; Intercept

The Debt Service Account is pledged to and will be used solely for the payment of Debt Service Charges as they fall due. Payments sufficient in an amount to pay the Debt Service Charges as they become due will be paid by the University directly to the Trustee, and deposited in the Debt Service Payment Account to the extent moneys in the Debt Service Payment Account are not otherwise available therefore. Upon the occurrence and during the continuation of an Event of Default described in the Trust Agreement with respect to a specific series of Obligations, if a subaccount in the Debt Service Reserve Account has been created to secure such series of Obligations, moneys in the applicable subaccount of the Debt Service Reserve Account may be transferred by the Trustee to the Debt Service Payment Account to be used to pay Debt Service Charges with respect to such series of Obligations pursuant to the Trust Agreement. Except as provided in the Trust Agreement, moneys in the Debt Service Payment Account shall be used solely for the payment of Debt Service Charges on the Obligations, for the redemption of

Obligations prior to maturity, for the payment of any amounts due to a Credit Support Provider to the extent as set forth in a Credit Support Instrument, for the payment of any amounts due to a Hedge Provider to the extent as set forth in an Interest Rate Hedge Agreement and as otherwise provided in the Trust Agreement and the 2005 General Bond Resolution.

If, ten days prior to any date that the payment of Debt Service Charges are due, sufficient funds are not on deposit in the Debt Service Payment Account to enable the Trustee to pay such Debt Service Charges, or if the Trustee shall have transferred funds from a Debt Service Reserve Account to the Debt Service Payment Account to forestall a default in the payment of Debt Service Charges, then in each such instance the Trustee shall immediately notify the Treasurer of the University and the Secretary of the Finance and Administration Cabinet of the Commonwealth in writing of such event and request that amounts be remitted to the Trustee pursuant to the then applicable provisions of Section 164A.608 of the Kentucky Revised Statutes to cure such deficiency or to restore the amount transferred from the Debt Service Reserve Account. (Section 4.02)

Debt Service Reserve Account

The Trustee will hold and administer a Debt Service Reserve Account to be used, solely for the payment of Debt Service Charges with respect to any series of Obligations for which a reserve fund has been mandated pursuant to the Series Resolution which authorized the issuance of such series of Obligations. A separate subaccount shall be created in the Supplemental Debt Service Reserve Account for each series of Obligations for which a reserve fund has been mandated by the Series Resolution which authorized such series of Obligations and each separate subaccount shall secure only the particular series of Obligations to which it is related.

If, on the date upon which Debt Service Charges on any Obligations which are secured by a Debt Service Reserve Account or subaccount held by the Trustee fall due, the subaccount within the Debt Service Payment Account related to such Obligations is insufficient to meet such Debt Service Charges to be paid therefrom on such date, the Trustee will immediately transfer from the appropriate subaccount of the Debt Service Reserve Account an amount sufficient to make up such deficiency in the subaccount of the Debt Service Payment Account. Except as may be provided in the applicable Series Resolution or Supplemental Trust Agreement, if on the day upon which amounts are due to a Hedge Provider under an Interest Rate Hedge Agreement or are due to a Credit Support Provider in reimbursement for amounts provided under a Credit Support Instrument, the amount in the subaccount within the Debt Service Payment Account related to such Debt Service Charges (other than from any amounts provided under an Interest Rate Hedge Agreement or Credit Support Instrument) is insufficient to pay such amounts to such Hedge Provider or Credit Support Provider on that date, the Trustee, without necessity for any further order of the University or officer thereof, will make available for such reimbursement any amounts in the related subaccount of the Debt Service Reserve Account for the series of Obligations to which the Interest Rate Hedge Agreement or Credit Support Instrument applies that are necessary to make up that insufficiency. The amount so transferred will be applied only to the payment of Debt Service Charges on the Obligations to which that Debt Service Reserve Account pertains or for the payment of any amounts due to a Hedge Provider under an Interest Rate Hedge Agreement or to a Credit Support Provider as reimbursement of draws under a Credit Support Instrument in connection with the Obligations to which that Debt Service Reserve Account pertains.

Subject to the foregoing, any amount in a subaccount of the Debt Service Reserve Account in excess of the amount required to be maintained therein pursuant to the Series Resolution which created such subaccount or the Certificate of Award (the "Required Amount") will be transferred to the Debt Service Payment Account or to the Redemption and Purchase Account for the purposes thereof, if and to the extent ordered by the Fiscal Officer. Such excess will be determined by calculating the Required Amount with reference to Outstanding Obligations of the particular series only, excluding any Obligations for the redemption or purchase of which such excess is being transferred to the Redemption and Purchase Account.

Within one hundred eighty (180) days after the end of each Fiscal Year, the University shall, from General Receipts, restore to the various subaccounts within the Debt Service Reserve Account any amounts transferred therefrom or any decrease in value determined pursuant to the Trust Agreement in such Fiscal Year so that the amounts in such subaccounts are at least equal to the various Required Amounts. (Section 4.03)

Redemption and Purchase Account

There will be deposited in the Redemption and Purchase Account that portion (if any) of the proceeds of refunding Obligations, as provided in the Series Resolution authorizing their issuance, allocated to the payment of the principal, interest and redemption premium, if any, or purchase price of the Obligations to be refunded, funded or retired through the issuance of such refunding Obligations; amounts to be transferred thereto from the Debt Service Reserve Account by order of the Fiscal Officer as set forth under the caption "Debt Service Reserve Account" above; and any other amounts made available by the University for the purposes of the Redemption and Purchase Account. Amounts for the redemption of Obligations to be provided pursuant to the mandatory sinking fund requirements of the Series Resolution authorizing such Obligations will not be deposited to the credit of the Redemption and Purchase Account, but shall be deposited to the credit of the Debt Service Payment Account.

Any amounts in the Redemption and Purchase Account may be committed, by Series Resolution or other action by the Board, for the retirement of and for Debt Service Charges on specified Obligations and, so long as so committed, will be used solely for such purposes whether directly or through transfer to the Debt Service Fund. Subject to the foregoing provisions of the Trust Agreement, the Fiscal Officer may cause moneys in the Redemption and Purchase Account to be used to purchase any Obligations for cancellation and to redeem any Obligations in accordance with the redemption provisions of the applicable Series Resolution. From moneys in the Redemption and Purchase Account, the Trustee will transmit or otherwise disburse such amounts at such times as required for the redemption or purchase for cancellation of Obligations, and Debt Service Charges, in accordance with the applicable Series Resolution, or other action by the Board or order of the Fiscal Officer not inconsistent therewith. Any amounts in the Redemption and Purchase Account not required for the purposes thereof pursuant to a commitment theretofore made, may be transferred to the Debt Service Payment Account or the Debt Service Reserve Account upon order of the Fiscal Officer. (Section 4.04)

Project Fund

Upon the issuance and delivery of Obligations, the proceeds of which will be used to pay Costs of University Facilities, there is to be created and the Treasury of the State is to hold and administer a fund designated the "University of Kentucky Project Fund" with an additional series identification for each series of Obligations.

Amounts in a Project Fund will be disbursed therefrom by the Treasurer of the State according to such inspection, audit, and disbursement procedures as may from time to time be provided by law, for the purpose of paying Costs of University Facilities as identified in the related Series Resolution or Supplemental Trust Agreement and to reimburse the University for any payments which may have been made from other available resources in anticipation of the issuance of such Obligations.

Any balance remaining in a Project Fund after the final payment of all Costs of University Facilities for which such Project Fund was created, will be deposited in the Debt Service Fund and (i) credited to the related subaccount, if any, within the Debt Service Reserve Account if and to the extent that such subaccount of the Debt Service Reserve Account contains less than the Required Amount, and/or (ii) either applied as a credit against the next deposit required to be made into the Debt Service Payment Fund, or used to purchase Obligations in the open market at a purchase price not exceeding par plus accrued interest, as may be directed by the Fiscal Officer; provided that, if proceedings are then pending or imminently contemplated for incurring additional Costs of University Facilities which are or will be paid from the proceeds of Obligations, any such unexpended balance may be taken into account in determining the amount of Obligations to be authorized for such purpose, or may otherwise be applied to such Costs of University Facilities, in which event such unexpended balance may be transferred to a Project Fund created for such purpose.

If so provided in any Series Resolution or a Supplemental Trust Agreement, to the extent permitted by law, a Project Fund may be held and disbursed by the Trustee. Furthermore, if the Obligations with respect to which a Project Fund is created are Financing Agreements, SPBC Leases or Additional Obligation Instruments, a Project Fund may be created in accordance with the requirements of such Financing Agreements, SPBC Leases or Additional Obligation Instruments. (Section 4.05)

General Covenant

So long as any Obligations are Outstanding pursuant to the Trust Agreement, the University covenants and agrees: (i) to fix, make, adjust and collect such fees, rates, rentals, charges and other items of General Receipts so that there shall inure to the University General Receipts, in view of other revenues and resources available to the University, sufficient: to pay Debt Service Charges then due or to become due in the current Fiscal Year; to pay any other costs and expenses payable under the Trust Agreement; and to pay all other costs and expenses necessary for the proper maintenance and successful and continuous operation of the University; and (ii) that it will include in its budget for each Fiscal Year the amount required to be paid to the Debt Service Fund established under the Trust Agreement, during such Fiscal Year. (Section 4.12)

Investment of Debt Service Fund and Project Fund

Except as provided in the Trust Agreement, moneys in the Debt Service Fund and the Project Fund shall be invested and reinvested by the Trustee (or the Fiscal Officer, as applicable) in Eligible Investments at the oral or written direction of the University, but if oral, confirmed promptly in writing. Investment of moneys in the Debt Service Fund shall mature or be redeemable at the times and in the amounts necessary to provide moneys to pay Debt Service Charges as they become due at stated maturity, by redemption or pursuant to any mandatory sinking fund requirements. Each investment of moneys in the Debt Service Fund and the Project Fund will mature or be redeemable without penalty at such time as may be necessary to make payments when necessary from such fund. In the absence of any written direction from the Fiscal Officer, the Trustee will invest all funds in sweep accounts, money-market funds and similar short-term investments, provided that all such investments shall constitute Eligible Investments. The Trustee may trade with itself or its affiliates in the purchase and sale of securities for such investments.

Subject to any directions from the University with respect thereto, the Trustee may sell at the best price reasonably obtainable Project Fund investments and reinvest the proceeds therefrom in Eligible Investments maturing or redeemable as aforesaid. Any of those investments may be purchased from or sold to the Trustee, the Registrar, an Authenticating Agent, a Paying Agent, or any bank, trust company or savings and loan association affiliated with any of the foregoing. The Trustee will sell or redeem investments credited to the Debt Service Fund to produce sufficient moneys applicable under the Trust Agreement to and at the times required for the purposes of paying Debt Service Charges when due as aforesaid, and shall do so without necessity for any order on behalf of the University and without restriction by reason of any order. An investment made from moneys credited to the Debt Service Fund and the Project Fund will constitute part of that respective fund, and each respective fund will be credited with all proceeds of sale and income from investment of moneys credited thereto.

For purposes of qualifying any investment as an Eligible Investment, where such qualification is dependent upon the rating assigned to such investment by a Rating Service, such qualification will be determined as of the date of purchase of such investment or deposit thereof with the Trustee, whichever is later. (Section 4.15)

Revenue Fund

So long as any Obligations remain Outstanding, there will be maintained a Revenue Fund, which, to the extent required by law, may be a fund (and accounts) in the Commonwealth's management administrative and reporting system. There will be maintained in the Revenue Fund the following Accounts: a "Student Registration Fees Account," a "Hospital Revenues Account" and a "Housing and Dining Revenues Account." The "Revenue Fund" created pursuant to the Prior Bond Resolution will continue to be maintained so long as any bonds remain outstanding under the Prior Bond Resolution, such Revenue Fund will constitute the Student Registration Fees Account of the Revenue Fund until there are no bonds outstanding under the Prior Bond Resolution and all Student Registration Fees will be deposited therein. The "Revenue Fund" created pursuant to a Master Resolution adopted by the Board on June 25, 1986 will continue to be maintained as the Hospital Revenues Account of the Revenue Fund and all Hospital Revenues shall be deposited therein. The "System Revenue Fund" created pursuant to the Prior Housing Indenture will continue to be maintained so long as any bonds remain outstanding under the Prior Housing Indenture, such System Revenue Fund will constitute the Housing and Dining Revenues Account of the Revenue Fund until there are no bonds outstanding under the Prior Housing Indenture and all Housing and Dining Revenues will be deposited therein. (Section 4.16)

Maintenance of Pledge

The University will not make any pledge or assignment of or create or suffer any lien or encumbrance upon the Debt Service Fund and, except for the existing pledges under the Prior Basic Resolution and Prior Housing Indenture, the University will not make any pledge or assignment of or create or suffer any lien or encumbrance upon the General Receipts prior to or on a parity with the pledge thereof under the Trust Agreement, except as authorized or permitted under the Trust Agreement. The University will issue no additional bonds or notes under the Prior Basic Resolution. The University will issue no additional bonds or notes under the Prior Housing Indenture unless, with respect to a series of Housing and Dining Bonds, (i) such bonds or notes could be issued as Obligations under the Trust Agreement within the limitations set forth in the Trust Agreement and (ii) it is provided in the supplemental indenture authorizing such notes or bonds that on the date no Housing and Dining Bonds are outstanding under the Prior Housing Indenture, other than notes or bonds issued in accordance with the provisions of the Trust Agreement summarized in this paragraph, the lien securing such Housing and Dining Bonds created by the Prior Housing Indenture will terminate and such Housing and Dining Bonds will continue as Obligations under the Trust Agreement on a parity with all other Obligations. (Section 4.18)

Events of Default

Events of Default under the Trust Agreement include:

(a) Failure to pay any Debt Service Charges when and as the same becomes due and payable;

(b) Failure to pay the principal of or any premium on any Prior Obligations when and as the same becomes due and payable, whether at the stated maturity thereof or by redemption or acceleration or pursuant to any mandatory sinking fund requirements;

(c) Failure by the University to perform or observe any other covenant, agreement or condition on the part of the University contained in the Trust Agreement or in the Obligations, which failure or Event of Default shall have continued for a period of 30 days after written notice, by registered or certified mail, given to the University by the Trustee, specifying the failure or Event of Default and requiring the same to be remedied, which notice shall be given by the Trustee upon the written request of the Holders of not less than 25% in aggregate principal amount of the Obligations then Outstanding; provided that the Person or Persons requesting such notice may agree in writing to a 90-day extension of such period prior to the expiration of the initial 30-day period; provided further, however, that if the University will proceed to take curative action which, if begun and prosecuted with due diligence, cannot be completed within a period of 90 days, then such period shall be increased without such written extension up to 180 days as will be necessary to enable the University to diligently complete such curative action;

(d) The University will (i) admit in writing its inability to pay its debts generally as they become due, (ii) have an order for relief entered in any case commenced by or against it under federal bankruptcy laws, as now or hereafter in effect, (iii) commence a proceeding under any federal or state bankruptcy, insolvency, reorganization or similar laws, or have such a proceeding commenced against it and have either an order of insolvency or reorganization entered against it or have the proceeding remain undismissed and unstayed for 90 days, (iv) make an assignment for the benefit of creditors, or, (v) have a receiver or trustee appointed for it or for the whole or substantial part of its property. (Section 6.01)

Supplemental Trust Agreements Not Requiring Consent of Holders

The University and the Trustee without the consent of, or notice to, any of the Holders, may enter into indentures supplemental to the Trust Agreement and other instruments evidencing the existence of a lien as shall not, in the opinion of the Trustee, be inconsistent with the terms and provisions of the Trust Agreement for any one or more of the following purposes:

(a) To cure any ambiguity, inconsistency or formal defect or omission in the Trust Agreement or in any Supplemental Trust Agreement;

(b) To grant to or confer upon the Trustee for the benefit of the Holders any additional rights, remedies, powers or authority that may lawfully be granted to or conferred upon the Holders or the Trustee;

(c) To subject additional revenues or property to the lien and pledge of the Trust Agreement;

(d) To add to the covenants and agreements of the University contained in the Trust Agreement other covenants and agreements thereafter to be observed for the protection of the Holders, or, if in the judgment of the Trustee such is not to the prejudice of the Trustee or the Holders, to surrender or limit any right, power or authority reserved to or conferred upon the University in the Trust Agreement, including the limitation of rights of redemption so that in certain instances Obligations of different series will be redeemed in some prescribed relationship to one another;

(e) To evidence any succession to the University and the assumption by such successor of the covenants and agreements of the University contained in the Trust Agreement or other instrument providing for the operation of the University or University Facilities, and the Obligations;

(f) In connection with the issuance of Obligations in accordance with the Trust Agreement;

(g) To permit the Trustee to comply with any obligations imposed upon it by law;

(h) To permit the exchange of Obligations, at the option of the Holder or Holders thereof, for coupon Obligations of the same series payable to bearer, in an aggregate principal amount not exceeding the unmatured and unredeemed principal amount of the Predecessor Obligations, bearing interest at the same rate or rates and maturing on the same date or dates, with coupons attached representing all unpaid interest due or to become due thereon if, in the opinion of nationally recognized Bond Counsel selected by the University and acceptable to the Trustee, that exchange would not result in the interest on any of the Obligations Outstanding becoming subject to federal income taxation;

(i) To specify further the duties and responsibilities of, and to define further the relationship among, the Trustee, the Registrar and any Authenticating Agents or Paying Agents;

(j) To achieve compliance of the Trust Agreement with any applicable federal or Kentucky laws, including tax laws;

(k) To modify any provisions of the Trust Agreement in order to obtain a Credit Support Instrument or Interest Rate Hedge Agreement, so long as such modifications affect only the Obligations to which such Credit Support Instrument or Interest Rate Hedge Agreement relate; and

(l) In connection with any other change to the Trust Agreement which, in the judgment of the Trustee, is not to the material prejudice of the Trustee or the Holders of the Obligations.

The provisions of (g) and (j) above will not be deemed to constitute a waiver by the Trustee, the Registrar, the University or any Holder of any right which it may have in the absence of those provisions to consent to the application of any change in law to the Trust Agreement or the Obligations. (Section 7.01)

Supplemental Trust Agreements Requiring Consent of Holders

Exclusive of supplemental indentures summarized under the heading "Supplemental Trust Agreements Not Acquiring Consent of Holders", above, and subject to the terms and provisions and limitations contained in this paragraph, and not otherwise, the Holders of a majority in aggregate principal amount of the Obligations then Outstanding shall have the right, from time to time, anything contained in the Trust Agreement to the contrary notwithstanding, to consent to and approve the execution by the University and the Trustee of such other indenture or indentures supplemental to the Trust Agreement as shall be deemed necessary and desirable by the University for the purpose of modifying, altering, amending, adding to or rescinding, in any particular, any of the terms or provisions contained in the Trust Agreement; provided that nothing in this paragraph or in the Trust Agreement will permit, or be construed as permitting, a Supplemental Trust Agreement providing for (a)(i) a reduction in the percentage of Obligations the consent of the Holders of which are required to consent to such Supplemental Trust Agreement or (ii) a preference or priority of any Obligation or Obligations over any other Obligation or Obligations, without the consent of the Holders of all Obligations then Outstanding, (b) effect a change in the times, amount or currency of payment of the principal of, premium, if any, on or interest on any Obligation or a reduction in the principal amount or redemption price of any Obligation or the rate of interest thereon, without the consent of the Holder of each such Obligation so affected or (c) modify the right of the Holders of not less than 25% in aggregate principal amount of the Obligations then Outstanding and in default as to payment of principal, premium or interest to compel the Trustee to declare the principal of all Obligations to be due and payable, without the consent of the Holders of a majority in aggregate principal amount of the Obligations then Outstanding.

If at any time the University requests the Trustee to enter into any such Supplemental Trust Agreement for any of the purposes summarized under this subheading, the Trustee, upon being satisfactorily indemnified with respect to expenses, shall cause notice of the proposed execution of such Supplemental Trust Agreement to be mailed by first class mail, postage prepaid, to all Holders of Obligations then Outstanding at their addresses as they appear on the Registrar at the close of business on the Business Day immediately preceding that mailing. The Trustee will not, however, be subject to any liability to any Holder by reason of its failure to mail, or the failure of such Holder to receive, the notice required by the Trust Agreement, and any such failure shall not affect the validity of such Supplemental Trust Agreement when consented to and approved in accordance with the procedures described under this subheading. Such notice will briefly set forth the nature of the proposed Supplemental Trust Agreement and will state that copies thereof are on file at the principal corporate trust office of the Trustee for inspection by all Holders.

If within such period, not exceeding one year, as prescribed by the University, following the mailing of such notice, the Trustee receives an instrument or instruments purporting to be executed by the Holders of a majority in aggregate principal amount of the Obligations then Outstanding, which instrument or instruments shall refer to the proposed Supplemental Trust Agreement described in such notice and will specifically consent to and approve the execution thereof in substantially the form of the copy thereof referred to in such notice as on file with the Trustee, thereupon, but not otherwise, the Trustee will execute such Supplemental Trust Agreement in substantially such form; without liability or responsibility to any Holder of any Obligation, whether or not such Holder will have consented thereto.

Any such consent is binding upon the Holder of the Obligation giving such consent, upon any subsequent Holder of such Obligation and upon the Holder of any Obligation issued in exchange therefor (whether or not such subsequent Holder thereof has notice thereof), unless such consent is revoked in writing by the Holder of such Obligation giving such consent or by a subsequent Holder thereof by filing with the Trustee, prior to the execution by the Trustee of such Supplemental Trust Agreement, such revocation and, if such Obligation or Obligations are transferable by delivery, proof that such Obligations are held by the signer of such revocation in the manner permitted by the Trust Agreement. At any time after the Holders of the required percentage of the Obligations shall have filed their consents to the Supplemental Trust Agreement, the Trustee shall make and file with the University a written statement that the, Holders of such required percentage of the Obligations have filed such consents. Such written statement shall be conclusive evidence that such consents have been so filed.

If the Holders of the required percentage in aggregate principal amount of the Obligations shall have consented to and approved the execution thereof as provided in the Trust Agreement, no Holder of any Obligation has any right to object to the execution of such Supplemental Trust Agreement, to object to any of the terms and provisions contained therein or the operation thereof, or in any manner to question the propriety of the execution thereof or to enjoin or restrain the Trustee or the University from executing the same or from taking any action pursuant to the provisions thereof.

Authorization to the Trustee; Effect of Supplemental Trust Agreements

The Trustee is authorized to join with the University in the execution of any such Supplemental Trust Agreement provided for in the Trust Agreement and to make the further agreements and stipulations which may be contained therein. Any Supplemental Trust Agreement executed in accordance with the provisions of the Trust Agreement will thereafter form a part of the Trust Agreement, all the terms and conditions contained in any such Supplemental Trust Agreement as to any provision authorized to be contained therein will be deemed to be part of the terms and conditions of the Trust Agreement for any and all purposes, the Trust Agreement will be and be deemed to be modified and amended in accordance therewith, and the respective rights, duties and obligations under the Trust Agreement of the University, the Trustee, the Registrar, the Authenticating Agents, the Paying Agents and all Holders of Obligations then Outstanding will thereafter be determined, exercised and enforced thereunder, subject in all respects to such modifications and amendments. Express reference to such executed Supplemental Trust Agreement may be made in the text of any Obligations issued thereafter, if deemed necessary or desirable by the Trustee or the University. There will be no modification, change or amendment to the Trust Agreement or any other document related to the Obligations which affects the rights, duties or obligations of the Trustee thereunder, without the Trustee's prior written consent.

Opinion of Counsel

The Trustee is entitled to receive, and shall be fully protected in relying upon, the opinion of any counsel approved by it, who may be counsel for the University, as conclusive evidence that any such proposed Supplemental Trust Agreement complies with the provisions of the Trust Agreement and that it is proper for the Trustee, under the provisions of the Trust Agreement, to join in the execution of such Supplemental Trust Agreement. (Section 7.04)

Modification by Unanimous Consent

Notwithstanding anything contained elsewhere in the Trust Agreement, the rights and obligations of the University and of the Holders of the Obligations, and the terms and provisions of the Obligations and the Trust Agreement or any Supplemental Trust Agreement, may be modified or altered in any respect with the consent of the University and the consent of the Holders of all of the Obligations then Outstanding and the Trustee. (Section 7.05)

Release of Trust Agreement

If the University pays or cause to be paid and discharged, or there shall otherwise by paid to the Holders of the Outstanding Obligations all Debt Service Charges due or to become due thereon and provision shall also be made for paying all other sums payable under the Trust Agreement, then and in that event the Trust Agreement (except for the provisions summarized under the captions "Use of Debt Service Payment Account; Intercept," "Redemption and Purchase Account," "Project Fund," "Payment and Discharge of Obligations" and "Survival of Certain Provisions" in this Appendix B") will cease, determine and become null and void, and the covenants, agreements, and other obligations of the University under the Trust Agreement are discharged and satisfied, and thereupon the Trustee will release the Trust Agreement, including the cancellation and discharge of the lien thereof, and execute and deliver to the University such instruments in writing as required to satisfy and terminate the lien thereof and to enter on the records such satisfaction and discharge and to re-convey to the University the estate created by the Trust Agreement and such other instruments to evidence such release and discharge as may be reasonably required by the University, and the Trustee and Paying Agents will assign and deliver to the University any property at the time subject to the lien of the Trust Agreement which may then be in their possession, except amounts in the Debt Service Fund required to be held by the Trustee and Paying Agents under the Trust Agreement or otherwise for the payment of Debt Service Charges. (Section 8.01)

Payment and Discharge of Obligations

All the Outstanding Obligations of one or more series will be deemed to have been paid and discharged within the meaning of the Trust Agreement, including without limitation, the provisions of the Trust Agreement summarized under the immediately preceding heading, if either (i) the Trustee as paying agent and any Paying Agents are required to hold, in the Debt Service Payment Account in trust for and irrevocably committed thereto, sufficient moneys or (ii) the Trustee is required to hold, in the Debt Service Fund in trust for and irrevocably committed thereto, investments qualifying as Government Bonds as of the date of the determination required in provisions of the Trust Agreement summarized in this paragraph which are, in either case, certified by an independent public accounting firm of national reputation to be of such maturities and interest payment dates and to bear such interest as will, without further investment or reinvestment of either the principal amount thereof or the interest earnings therefrom (likewise to be held in trust and committed, except as provided in the Trust Agreement), be sufficient together with moneys referred to in clause (i) above, for the payment, at their maturity, redemption or due date, as the case may be, of all Debt Service Charges on those Obligations to their maturity, redemption or due date, as the case may be, or if Event of Default in such payment will have occurred on such date then to the date of the tender of such payment; provided that if any of such Obligations are to be redeemed prior to the maturity thereof, notice of such redemption will have been duly given or irrevocable provisions satisfactory to the Trustee have been duly made for the giving of such notice; provided that if the Obligations are to be redeemed prior to the maturity thereof, notice of such redemption shall have been duly given or irrevocable provision satisfactory to the Trustee shall have been duly made for the giving of such notice. (Section 8.02)

Survival of Certain Provisions

Notwithstanding the foregoing, those provisions of a Series Resolution and the Trust Agreement relating to the maturity of Obligations, interest payments and dates thereof, optional and mandatory redemption provisions, credit against Mandatory Sinking Fund Requirements, exchange, transfer and registration of Obligations, replacement of mutilated, destroyed, lost or stolen Obligations, the safekeeping and cancellation of Obligations, non-presentment of Obligations, the holding of moneys in trust, repayments to the University from the Special Funds and the rights, remedies and duties of the Trustee and the Registrar in connection with all of the foregoing, shall remain in effect and shall be binding upon the Trustee, the Registrar, the Authenticating Agent, Paying Agents and the Holders notwithstanding the release and discharge of the lien of the Trust Agreement. The provisions of the Trust Agreement described in this paragraph and under the two headings that immediately precede it shall survive the release and discharge of the Trust Agreement. (Section 8.03)

Limitation of Rights

With the exception of rights expressly conferred in the Trust Agreement, nothing expressed or mentioned in or to be implied from the Trust Agreement or the Obligations is intended or shall be construed to give to any Person other than the parties to the Trust Agreement, the University, any Credit Support Provider and the Holders of the Obligations any legal or equitable right, remedy or claim under or in respect to the Trust Agreement or any covenants, conditions and provisions in contained in the Trust Agreement; the Trust Agreement and all of the covenants, conditions and provisions of the Trust Agreement being intended to be and being for the sole and exclusive benefit of the parties hereto, the University, any Credit Support Provider and the Holders of the Obligations as provided in the Trust Agreement. (Section 9.02)

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APPENDIX C

UNIVERSITY OF KENTUCKY
CONSOLIDATED FINANCIAL STATEMENTS AS OF JUNE 30, 2006 (UNAUDITED)

And

UNIVERSITY OF KENTUCKY
ALBERT B. CHANDLER MEDICAL CENTER
UNIVERSITY HOSPITAL
CONSOLIDATED FINANCIAL STATEMENTS AS OF JUNE 30, 2006 (UNAUDITED)

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University of Kentucky
Consolidated Financial Statements

Management's Discussion and Analysis

The following Management's Discussion and Analysis, or MD&A, provides an overview of the financial position and activities of the University of Kentucky (the University) and its affiliated corporations for the years ended June 30, 2006 and 2005. Management has prepared this discussion, and we encourage you to read it in conjunction with the consolidated financial statements and the notes appearing in this report.

About the University of Kentucky

Located in Lexington, the University of Kentucky is the Commonwealth of Kentucky's flagship institution of higher education. As a land grant institution, the University is dedicated to enriching people's lives through excellence in teaching, research and service and plays a critical leadership role for the state by promoting human and economic development that improves lives within Kentucky's borders and beyond.

The University of Kentucky has a presence in all 120 counties – through its Agricultural Extension Service -- with an impact nationwide and abroad. Total enrollment is over 27,000 students, representing all Kentucky counties, every state in the nation, and 118 countries. In 2005 - 2006, the University conferred nearly 5,500 degrees among its comprehensive academic programs. Over 1,900 full-time faculty and 9,500 full-time staff are employed by the University.

The University consists of 16 colleges, plus the Graduate School. With 93 undergraduate programs, master's degrees in 99 fields, doctoral degrees in 66 programs, and four professional programs, the colleges include: Agriculture, Arts and Sciences, Business and Economics, Communications and Information Studies, Dentistry, Design, Education, Engineering, Fine Arts, Health Sciences, Law, Medicine, Nursing, Pharmacy, Public Health, and Social Work. The University boasts more than 80 national rankings for academic excellence.

The University's William T. Young Library is among the world's leading research libraries; its book endowment is the largest among public universities and ranks second only to Harvard University among all universities. Its broad scope of technology offers students, faculty and Kentucky residents access to the most up-to-date information from online journals, government publications, and private studies, as well as more traditional materials.

The UK Chandler Medical Center, which opened in 1960, is considered one of the nation's finest academic medical centers. The faculty, students and staff take pride in achieving excellence in education, patient care, research, and community service. As one of two Level 1 Trauma Centers in the state and the first health-care facility in Central and Eastern Kentucky to obtain distinction as a Primary Stroke Center, UK Hospital cares for the most critically injured and ill patients in the region. The 473-bed UK Hospital and UK Children's Hospital are supported by more than 500 faculty physicians and dentists, 400 resident physicians, and a staff of 3,300 health professionals committed to high-quality patient care.

Research at the University is a dynamic enterprise encompassing both traditional scholarship and emerging technologies. The Advanced Science and Technology Commercialization Center, for example, is a hub for multidisciplinary research collaboration. It is just one of more than 50 research centers and institutes across campus, including the highly acclaimed Sanders-Brown Center on Aging, Morris K. Udall Parkinson's Disease Research Center of Excellence, and Markey Cancer Center, where University researchers are discovering and developing new treatments to improve health care, providing a rich training ground for the next generation of researchers, and advancing the state's economic growth.

During fiscal year 2006, the University faculty received a record-breaking total of $290.4 million in extramural funding for grants and contracts. The achievement marked an increase of 6 percent from last fiscal year and the fifth year in a row the University exceeded the $200 million level in sponsored project awards. The majority of grants and contracts – 53.6 percent – were awarded by federal agencies and totaled $155.5 million, an increase of 2 percent.

The University is committed to strong public service, reaching out to communities across the Commonwealth, sharing knowledge and making a difference in the towns, cities, and lives of all Kentuckians. An example is Health Education through Extension Leadership, a partnership between the College of Public Health, the College of Dentistry, the College of Agriculture, and the Cooperative Extension Service to enhance extension agents' capacity to deliver valuable health and wellness information throughout the state.

The University's agenda is simple – to be a catalyst for a new Commonwealth, one that is healthier, more prosperous and economically secure and that educates the state's best and brightest. The University is accelerating the movement toward academic excellence, becoming known worldwide for the quality of its academic programs, its commitment to undergraduates, its success in building a diverse community, and its engagement with the larger society.

Research Challenge Trust Fund

In 1998, the Commonwealth of Kentucky initiated the Research Challenge Trust Fund (RCTF), an endowment match program. Since that time, the Commonwealth has appropriated more than $350 million to the public universities to be matched with private donations primarily to support chairs and professorships, fellowships and scholarships, and the research and graduate missions of the institutions. To date, the University of Kentucky has been allocated $202.2 million in RCTF funding.

Financial Highlights

The University's overall financial position remains strong with assets of $2.81 billion and liabilities of $709.9 million. Net assets, which represent the University's residual interest in assets after liabilities are deducted, were $2.10 billion or 75 percent of total assets.

- Total assets increased $363.2 million, or 15 percent, primarily due to increases in cash and cash equivalents and capital assets, net, from the proceeds of debt issued during the year, as well as increases in endowment investments and other increases in capital assets. During the year, $150.0 million of Hospital cash was invested in the University pooled endowment fund which accounted for a significant portion of the increase in endowment investments.

- Total liabilities increased $128.0 million, or 22 percent, primarily due to the issuance of additional debt, principally for the hospital patient care facility project.

- Total net assets increased $235.2 million, or 13 percent, due to an increase in net capital assets of $13.0 million; an increase in restricted net assets of $120.1 million, primarily due to gifts and other additions to endowments of $36.0 million, realized and unrealized gains on endowment investments, net of spending distributions, of $26.0 million, and capital grants from the Commonwealth of Kentucky restricted for building projects of $48.5 million; and an increase of $102.1 million in unrestricted net assets, primarily due to excess revenues over expenses in the hospital of $65.2 million and general funds revenues in excess of expenses.

- Operating revenues were $1.33 billion and operating expenses were $1.63 billion, resulting in a loss from operations of $305.4 million. Nonoperating revenues, including $314.3 million in state appropriations, net of nonoperating expenses, were $540.5 million, which, when combined with the loss from operations, resulted in an overall increase in net assets of $235.2 million.

Using the Consolidated Financial Statements

The University presents its financial reports in a "business type activity" format, in accordance with Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments* and GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities – an amendment of GASB Statement No. 34*. In addition to this MD&A section, the financial report includes a Statement of Net Assets, a Statement of Revenues, Expenses and Changes in Net Assets, a Statement of Cash Flows, and Notes to the Financial Statements. GASB requires that statements be presented on a consolidated basis to focus on the University as a whole.

Reporting Entity

The University of Kentucky is a component unit of the Commonwealth of Kentucky. The consolidated financial statements of the University include the operations of the University and the following entities:

- University of Kentucky Research Foundation, and its for-profit subsidiary, Kentucky Technology, Inc.
- University of Kentucky Athletic Association
- The Fund for Advancement of Education and Research in the University of Kentucky Medical Center
- University of Kentucky Business Partnership Foundation, Inc.
- University of Kentucky Center on Aging Foundation, Inc.
- University of Kentucky Gluck Equine Research Foundation, Inc.
- University of Kentucky Humanities Foundation, Inc.
- University of Kentucky Mining Engineering Foundation, Inc.
- Central Kentucky Management Services, Inc.
- Kentucky Medical Services Foundation, Inc.
- Kentucky Healthcare Enterprises, Inc., a for-profit subsidiary.

Consolidated Statement of Net Assets

The Consolidated Statement of Net Assets is the University's balance sheet. It reflects the total assets, liabilities and net assets (equity) of the University as of June 30, 2006, with comparative information as of June 30, 2005. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as non-current. Net assets, the difference between total assets and total liabilities, are an important indicator of the University's current financial condition, while the change in net assets is an indicator of whether the overall financial position has improved or worsened during the year. Generally, assets and liabilities are reported using current values. A major exception is capital assets, which are stated at historical cost, less accumulated depreciation. A summarized comparison of the University's assets, liabilities and net assets at June 30, 2006, 2005 and 2004 is as follows:

Condensed Consolidated Statement of Net Assets (in thousands)

	2006	2005	2004
ASSETS			
Current assets	$ 580,909	$ 542,273	$ 480,985
Capital assets, net of depreciation	1,081,156	1,028,064	982,366
Other noncurrent assets	1,146,233	874,771	844,098
Total Assets	2,808,298	2,445,108	2,307,449
LIABILITIES			
Current liabilities	229,343	213,913	204,913
Noncurrent liabilities	480,603	368,039	364,059
Total Liabilities	709,946	581,952	568,972
NET ASSETS			
Invested in capital assets, net of related debt	763,476	750,485	737,140
Restricted			
Nonexpendable	423,755	393,224	356,599
Expendable	307,195	217,643	204,049
Unrestricted	603,926	501,804	440,689
Total Net Assets	$ 2,098,352	$ 1,863,156	$ 1,738,477

Assets. As of June 30, 2006, total assets amounted to $2.81 billion. Of this amount, investment in capital assets (net of depreciation) of $1.08 billion, or 39 percent of total assets, represented the largest asset class. Endowment investments amounted to $767.7 million or 28 percent of total assets and cash and cash equivalents amounted to $541.7 million or 19 percent of total assets. During the year, total assets increased by $363.2 million primarily due to increases in cash and cash equivalents and capital assets, net, from the proceeds of debt issued during the year, as well as increases in endowment investments and other increases in capital assets.

Liabilities. As of June 30, 2006, total liabilities amounted to $709.9 million. Bonds payable and capital leases for educational buildings, the housing and dining system, the University hospital and the William T. Young library amounted to $436.7 million, or 62 percent of total liabilities. During the year, total liabilities increased by $128.0 million primarily due to the issuance of additional debt, principally for the hospital patient care facility project.

Net Assets. The equity of the University of $2.10 billion as of June 30, 2006 is reported on the Statement of Net Assets in four net asset categories: invested in capital assets, net of related debt, $763.5 million (36 percent), restricted-nonexpendable, $423.8 million (20 percent), restricted-expendable, $307.2 million (15 percent), and unrestricted, $603.9 million (29 percent).

Restricted net assets are subject to externally imposed restrictions governing their use. Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the unrestricted net assets have been internally designated for support of academic and research programs and initiatives, capital projects, and working capital requirements.

Total net assets increased by $235.2 million during the year ended June 30, 2006. Invested in capital assets, net of related debt, increased by $13.0 million, primarily due payment of current year maturities of principal on bonds and capital leases. Restricted net assets increased by $120.1 million, primarily due to gifts and other additions to endowments of $36.0 million, realized and unrealized gains on endowment investments, net of spending distributions, of $26.0 million, and capital grants from the Commonwealth of Kentucky restricted for building projects of $48.5 million. Unrestricted net assets increased $102.1 million, primarily due to excess revenues over expenses in the hospital of $65.2 million and general funds revenues in excess of expenses.

2005 Versus 2004. During the year ended June 30, 2005:

- Total assets increased by $137.7 million, primarily due to increases in cash and cash equivalents, endowment investments and capital assets.

- Liabilities increased by $13.0 million primarily due to the issuance of new capital debt, net of principal payments on bonds and capital lease obligations, and increases in self insurance reserves.

- Total net assets increased by $124.7 million. Invested in capital, net of related debt, increased by $13.3 million, primarily due to net additions to capital assets of $123.9 million offset by current year depreciation expense of $78.2 million. Restricted net assets increased by $50.2 million, primarily due to an increase in permanent endowments of $37.5 million and realized and unrealized gains on endowment investments of $26.7 million. Unrestricted net assets increased $61.1 million, primarily due revenues in excess of expenditures in hospital and general funds.

Consolidated Statement of Revenues, Expenses and Changes in Net Assets

The Consolidated Statement of Revenues, Expenses and Changes in Net Assets is the University's income statement. It details how net assets have increased (or decreased) during the year ended June 30, 2006, with comparative information for the year ended June 30, 2005. This statement is prepared on the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. All items that increase or decrease net assets must appear on the Consolidated Statement of Revenues, Expenses and Changes in Net Assets as revenues, expenses, gains or losses.

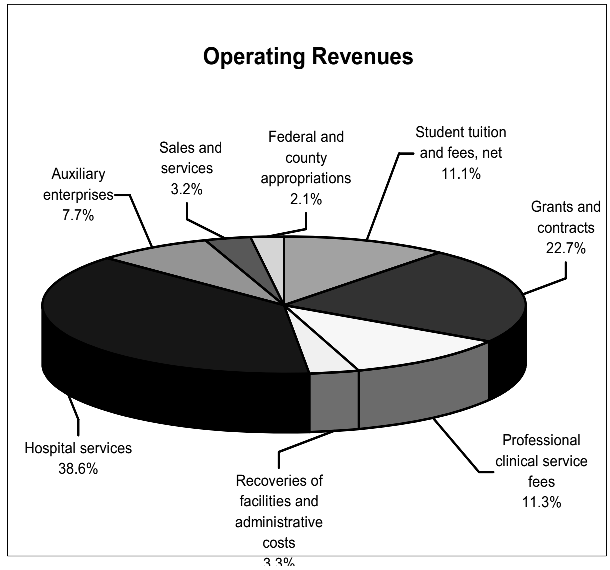
Financial activities are reported as either operating or nonoperating. GASB Statement No. 35 requires state appropriations, gifts, and investment and endowment income to be classified as nonoperating revenues. Accordingly, the University reports a net operating loss for the year prior to the addition of nonoperating revenues. The utilization of long-lived capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life. Tuition revenue is reduced by gift scholarships and institutional aid, and is reported net of scholarship allowances in the financial statements. A summarized comparison of the University's revenues, expenses and changes in net assets for the years ended June 30, 2006, 2005 and 2004 is as follows:

Condensed Consolidated Statement of Revenues, Expenses and Changes in Net Assets
(in thousands)

	2006	2005	2004
OPERATING REVENUES			
Student tuition and fees, net of scholarship allowances	$ 147,267	$ 133,389	$ 124,034
Grants and contracts	300,346	268,219	241,732
Hospital services	511,441	440,609	370,628
Professional clinical service fees	150,241	142,154	134,349
Auxiliary enterprises, net of scholarship allowances	102,080	95,249	84,447
Sales and services	42,826	38,857	42,587
Recoveries of facilities and administrative costs	43,303	40,332	37,122
Federal and county appropriations	27,681	27,703	25,707
Other operating revenue	2,222	466	303
Total operating revenues	1,327,407	1,186,978	1,060,909
OPERATING EXPENSES			
Educational and general, excluding depreciation	864,842	797,183	787,780
Clinical operations, excluding depreciation	119,910	116,852	115,279
Hospital, excluding depreciation	468,924	387,685	329,142
Auxiliary enterprises, excluding depreciation	94,824	87,885	80,334
Depreciation	83,761	78,219	70,888
Other	460	381	276
Total operating expenses	1,632,721	1,468,205	1,383,699
OPERATING LOSS	(305,314)	(281,227)	(322,790)
NONOPERATING REVENUES (EXPENSES)			
State appropriations	314,294	287,897	302,539
Capital appropriations	475	732	2,070
Capital grants and gifts	62,176	18,915	15,275
Gifts and grants	32,188	24,638	22,477
Investment income	115,495	56,517	78,102
Interest on capital asset - related debt	(13,497)	(13,062)	(11,970)
Additions to permanent endowments	24,336	33,650	21,036
Transfer of net assets of Lexington Community College	-	(4,968)	-
Other, net	5,043	1,587	(6,418)
Total nonoperating revenues (expenses)	540,510	405,906	423,111
Total increase in net assets	235,196	124,679	100,321
Net assets, beginning of year	1,863,156	1,738,477	1,638,156
Net assets, end of year	$ 2,098,352	$ 1,863,156	$ 1,738,477

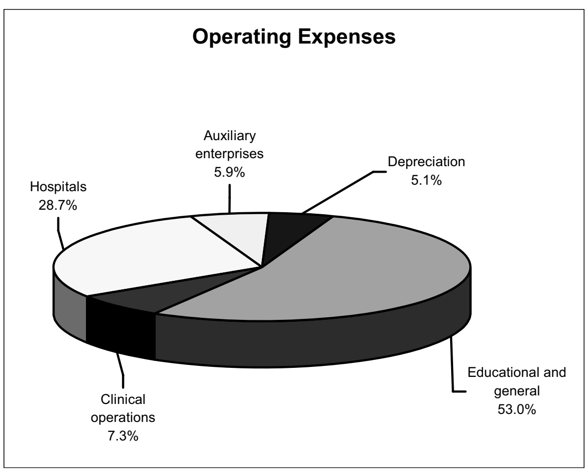
Total operating revenues were $1.33 billion for the year ended June 30, 2006, an increase of $140.4 million (12 percent). The primary components of operating revenues were student tuition and fees of $147.3 million; grants, contracts and recoveries of facilities and administrative costs of $343.6 million; hospital services of $511.4 million; and professional clinical fee income of $150.2 million.

The major increase was in hospital services revenue of $70.8 million, caused equally by an increase in inpatient volume, due to improved recruitment and retention of medical faculty and staff combined with an increase in available beds, and by rate increases for selected services, primarily outpatient services. Additional significant increases in operating revenues related to grants, contracts and recoveries of facilities and administrative costs of $32.1 million, due to the continued expansion of the research mission of the University, and in tuition and fees, net of $13.9 million due to tuition increases of approximately 12.5 percent.



Operating expenses totaled $1.63 billion, an increase of $164.5 million (11 percent). Of this amount, $864.8 million was expended for educational and general programs, including the functions of instruction, research and service. Hospital expenses, excluding depreciation, amounted to $468.9 million and clinical operations expenses, excluding depreciation, were $119.9 million. Depreciation expense for the year amounted to $83.8 million.

The most significant increase was in hospital expenses of $81.2 million (20 percent) due to increased usage of medical supplies and increased personnel costs due to higher utilization. Education and general expenses increased $67.7 million (8 percent) due primarily to increases in instruction, research and public service.



The net loss from operations for the year amounted to $305.3 million. Nonoperating revenues, net of expenses, amounted to $540.5 million, resulting in an increase in net assets of $235.2 million for the year. Nonoperating revenues include state appropriations of $314.3 million, an increase of $26.4 million.

2005 Versus 2004. Total operating revenues were $1.19 billion for the year ended June 30, 2005, including student tuition and fees of $133.4 million (11 percent), grants, contracts and recoveries of facilities and administrative costs of $308.6 million (26 percent), professional clinical service fees of $142.2 million (12 percent) and hospital services of $440.6 million (37 percent). Operating revenues for fiscal 2005 increased by $126.1 million or 12 percent over fiscal 2004, primarily due to increases in hospital services revenues of $70.0 million, in grants, contracts and recoveries of facilities and administrative costs of approximately $29.7 million and in student tuition and fees of $9.4 million.

Operating expenses totaled $1.47 billion. Of this amount, $797.2 million, or 54 percent, was expended for educational and general programs, including the functions of instruction, research and public service. Hospital expenses, excluding depreciation, amounted to $387.7 million, or 26 percent of the total expenses and clinical operations expenses, excluding depreciation, were $116.9 million, or 8 percent. Depreciation amounted to $78.2 million, or 5 percent. Operating expenses for fiscal 2005 increased by $84.5 million or 6 percent over fiscal 2004, primarily due to increases in hospital expenses of $58.5 million due increased usage of medical supplies and increased personnel costs due to higher utilization.

The net loss from operations for the year amounted to $281.2 million. Nonoperating revenues, net of expenses, amounted to $405.9 million, resulting in an increase in net assets of $124.7 million for the year. This compares with an increase in net assets for fiscal 2004 of $100.3 million. The most significant difference between fiscal 2004 and 2005 was a decrease in the loss from operations of $41.6 million, offset by decreases in investment income and state appropriations of $21.6 million and $14.6 million, respectively.

Consolidated Statement of Cash Flows

The Consolidated Statement of Cash Flows details how cash has increased (or decreased) during the year ended June 30, 2006, with comparative financial information for the year ended June 30, 2005. It breaks out the sources and uses of cash into the following categories:

- Operating activities
- Non-capital financing activities
- Capital financing activities
- Investing activities

Cash flows associated with the University's expendable net assets appear in the operating and non-capital financing categories. Capital financing activities include payments for capital assets, proceeds from long-term debt, and debt repayments. Purchases and sales of investments are reflected in investing activities.

The primary purpose of the Consolidated Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the University during the year that will allow financial statement readers to assess the institutions:

- Ability to generate future net cash flows,
- Ability to meet obligations as they become due, and
- The possible need for external financing.

A comparative summary of the University's consolidated statement of cash flows for the years ended June 30, 2006, 2005 and 2004 is as follows:

Condensed Consolidated Statement of Cash Flows (in thousands)

	2006	2005	2004
CASH PROVIDED (USED) BY:			
Operating activities	$ (227,208)	$ (203,467)	$ (228,809)
Noncapital financing activities	372,468	345,427	348,499
Capital and related financing activities	15,343	(118,891)	(79,170)
Investing activities	(58,743)	15,696	(6,490)
Net increase in cash and cash equivalents	101,860	38,765	34,030
Cash and cash equivalents, beginning of year	439,855	401,090	367,060
Cash and cash equivalents, end of year	$ 541,715	$ 439,855	$ 401,090

The University's cash and cash equivalents increased $101.9 million in 2006. Total cash provided by operating and non-capital financing activities was $145.3 million, up $3.3 million compared to 2005. Total cash provided by capital financing activities was $15.3 million, reflecting both capital funding sources (debt proceeds) and uses (purchases of capital assets and debt service). Total cash provided used by investing activities was $58.7 million, primarily due to the reinvestment of earnings on additional investments.

Major sources of cash received from operating activities are student tuition and fees of $144.5 million, hospital services of $509.2 million, grants, contracts and recoveries of facilities and administrative costs of $328.1 million and professional clinical service fees of $154.3 million. Major uses of cash for operating activities were payments to employees for salaries and benefits of $970.7 million and to vendors and contractors of $552.1 million.

Noncapital financing activities includes state appropriations from the Commonwealth of Kentucky of $314.3 million.

Capital and related financing activities include proceeds of capital debt of $126.1 million and capital grants and gifts of $55.3 million. Cash of $139.5 million was expended for construction and acquisition of capital assets and $35.8 million was expended for principal and interest payments on debt.

Investing activities include proceeds from sales and maturities of investments of $1.69 billion and interest and dividends on investments of $50.6 million. Cash of $1.80 billion was used to purchase investments.

2005 Versus 2004. Cash balances improved when comparing fiscal 2005 versus fiscal 2004 with a net increase in cash of approximately $38.8 million. The net increase in cash was due primarily to the excess funding provided by an increase in cash provided by investing activities of $22.2 million.

Capital Asset and Debt Administration

Capital Assets

Capital assets, net of accumulated depreciation, totaled $1.08 billion at June 30, 2006, an increase of $53.1 million. Capital assets as of June 30, 2006, and significant changes in capital assets during the years ended June 30, 2006, and 2005 are as follows (in millions):

	Balance June 30, 2004	Net Additions FY 04-05	Balance June 30, 2005	Net Additions FY 05-06	Balance June 30, 2006
Land and land improvements	$ 92	$ 6	$ 98	$ 14	$ 112
Buildings, fixed equipment and infrastructure	1,117	93	1,210	67	1,277
Equipment, vehicles and capitalized software	377	24	401	41	442
Library materials and art	122	10	132	6	138
Construction in progress	89	(34)	55	(12)	43
Accumulated depreciation	(815)	(53)	(868)	(63)	(931)
Total	$ 982	$ 46	$ 1,028	$ 53	$ 1,081

At June 30, 2006, the University has capital construction projects in progress totaling approximately $512 million in scope. Major projects include the hospital patient care facility, the new Biological Pharmaceutical Research building and the renovation of and addition to Memorial Coliseum.

Debt

At June 30, 2006, capital debt amounted to $436.7 million, summarized by trust indenture and type as follows (in millions):

	2006	2005	2004
General Receipts bonds and notes	$ 114.7		
Consolidated Educational Buildings Revenue Bonds	139.2	$ 141.6	$ 154.3
Housing and Dining System Revenue Bonds	74.0	77.0	79.3
Hospital Revenue Bonds	-	1.8	3.8
Commonwealth Library Project (W.T. Young Library) Bonds	40.2	41.4	42.5
Capital Lease Obligations	65.2	66.1	43.1
Notes Payable	3.4	3.1	3.5
Total	$ 436.7	$ 331.0	$ 326.5

Debt increased $105.7 million during the year primarily due to the issuance of debt for the construction of the hospital patient care facility.

Economic Factors That Will Affect the Future

Executive management believes that the University is well-positioned to maintain its strong financial condition and to continue providing excellent service to students, patients, the community and the Commonwealth of Kentucky. The University's strong financial condition, as evidenced by the receipt of credit ratings of Aa3 and AA- from Moody's Investors Service and Standard & Poor's Ratings Services, respectively, will provide a high degree of flexibility in obtaining funds on competitive terms. This flexibility, along with ongoing efforts toward revenue diversification and cost containment, will enable the University to obtain the necessary resources to sustain excellence. The following are known facts and circumstances that will affect future financial results:

- As a result of an improving economy, budgeted state appropriations will increase to $318.6 million and $335.0 million for fiscal years 2006-07 and 2007-08, respectively.
- Tuition rates for fiscal year 2007 will increase an average of approximately 12.4 percent for resident undergraduate students and 7.1 percent for non-resident undergraduate students. The tuition rate increases combined with stable enrollment are expected to generate additional operating revenues of approximately $16.4 million.
- As of June 30, 2006, grants and contracts of approximately $221 million had been awarded to the University, but not expended. These contracts will provide grant revenue to future periods. Research grants and contracts awarded to the University in fiscal year 2006 were a record high of $290.4 million.
- The University is conducting its Campaign for the University of Kentucky, a capital campaign with an expanded goal of $1 billion. As of June 30, 2006, approximately $910 million of gifts have been received or pledged toward this goal.
- A new hospital patient care facility with an estimated construction project cost of $450 million has been approved by the General Assembly. General Receipts Notes in the amount of $107.5 million were issued in fiscal year 2005-06 to provide initial funding for this project. An additional $150 million in related bond authority has been approved for the current biennium.
- The University will continue its long-term endowment investment strategy to maximize total returns, at an appropriate level of risk, while utilizing a spending rate policy to insulate programs funded by the endowment from temporary market volatility.
- The University does not record a liability for post-employment retiree health benefits. Governmental Accounting Standards require that this liability be recognized in the financial statements beginning June 30, 2008. The impact of implementing this change from a cash basis to an accrual basis for recognizing the cost of post employment retiree health benefits will increase the annual expense associated with providing this benefit from $7.7 million to $14.2 million per year beginning in fiscal year 2008.

Economic challenges will continue to impact the future. However, university management believes that the University of Kentucky will be able to sustain its sound financial position and continue its progress to become one of America's 20 best public research institutions.

UNIVERSITY OF KENTUCKY AND AFFILIATED CORPORATIONS
CONSOLIDATED STATEMENT OF NET ASSETS
JUNE 30, 2006 AND 2005

	2006	2005
ASSETS		
Current Assets		
Cash and cash equivalents	$ 369,087,885	$ 364,986,832
Notes, loans and accounts receivable, net	154,909,270	126,763,191
Investments	32,109,469	29,846,815
Inventories and other	24,802,495	20,675,672
Total current assets	580,909,119	542,272,510
Noncurrent Assets		
Restricted cash and cash equivalents	172,627,182	74,868,400
Endowment investments	767,693,088	555,365,026
Other long-term investments	172,127,484	213,472,794
Notes, loans and accounts receivable, net	32,122,190	31,065,483
Other noncurrent assets	1,662,816	-
Capital assets, net	1,081,156,203	1,028,063,986
Total noncurrent assets	2,227,388,963	1,902,835,689
Total assets	2,808,298,082	2,445,108,199
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	126,320,063	118,076,210
Deferred revenue	57,521,650	48,375,374
Long-term liabilities - current portion	45,501,341	47,460,973
Total current liabilities	229,343,054	213,912,557
Noncurrent Liabilities		
Long-term liabilities	480,602,627	368,039,152
Total liabilities	709,945,681	581,951,709
NET ASSETS		
Invested in capital assets, net of related debt	763,475,732	750,484,801
Restricted		
Nonexpendable		
Scholarships and fellowships	83,311,656	75,348,358
Research	194,070,426	179,061,853
Instruction	59,711,569	55,464,362
Academic support	82,115,782	78,868,428
Other	4,545,612	4,481,386
Total restricted nonexpendable	423,755,045	393,224,387
Expendable (See note 9.)		
Scholarships and fellowships	56,920,357	48,479,070
Research	63,706,209	46,552,512
Instruction	44,326,525	39,776,450
Academic support	29,671,893	22,309,913
Loans	8,972,452	8,726,094
Capital projects	63,829,016	14,529,112
Debt service	4,171,226	4,747,705
Other	35,597,314	32,522,210
Total restricted expendable	307,194,992	217,643,066
Total restricted	730,950,037	610,867,453
Unrestricted (See note 10.)	603,926,632	501,804,236
Total net assets	$ 2,098,352,401	$ 1,863,156,490

See notes to consolidated financial statements.

UNIVERSITY OF KENTUCKY AND AFFILIATED CORPORATIONS
CONSOLIDATED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
OPERATING REVENUES (See note 11)		
Student tuition and fees	$ 201,192,585	$ 178,587,240
Less: Scholarship allowances	(53,925,121)	(45,198,300)
Net tuition and fees	147,267,464	133,388,940
Federal grants and contracts	171,869,356	159,811,330
State and local grants and contracts	94,943,447	78,293,146
Nongovernmental grants and contracts	33,530,619	30,113,297
Recoveries of facilities and administrative costs	43,303,460	40,332,490
Sales and services	42,826,104	38,856,761
Federal appropriations	15,683,789	16,135,899
County appropriations	11,998,193	11,567,197
Professional clinical service fees	150,240,798	142,154,440
Hospital services	511,441,445	440,609,478
Auxiliary enterprises:		
Housing and dining	40,781,440	36,359,880
Less: Scholarship allowances	(4,396,917)	(4,217,608)
Net housing and dining	36,384,523	32,142,272
Athletics	45,062,540	42,408,397
Other auxiliaries	20,632,796	20,698,585
Other operating revenues	2,222,388	465,610
Total operating revenues	1,327,406,922	1,186,977,842
OPERATING EXPENSES		
Educational and general:		
Instruction	240,087,280	221,459,125
Research	236,140,895	226,870,110
Public service	164,011,041	137,286,741
Libraries	14,866,441	13,440,593
Academic support	61,655,329	56,337,386
Student services	21,578,839	18,862,683
Institutional support	50,211,186	48,183,547
Operations and maintenance of plant	53,047,615	45,577,213
Student financial aid	23,242,484	29,165,814
Depreciation	57,901,456	53,528,499
Total educational and general	922,742,566	850,711,711
Clinical operations (including depreciation of $807,937 in 2006 and $726,210 in 2005)	120,717,535	117,577,768
Hospital and clinics (including depreciation of $19,210,460 in 2006 and $19,265,277 in 2005)	488,133,619	406,949,935
Auxiliary enterprises:		
Housing and Dining (including depreciation of $3,366,341 in 2006 and $2,183,203 in 2005)	38,780,215	34,092,645
Athletics (including depreciation of $2,474,802 in 2006 and $2,515,907 in 2005)	47,810,546	44,472,780
Other auxiliaries	14,076,460	14,017,792
Other operating expenses	460,336	381,985
Total operating expenses	1,632,721,277	1,468,204,616
Net loss from operations	(305,314,355)	(281,226,774)
NONOPERATING REVENUES (EXPENSES) (See note 11)		
State appropriations	314,293,555	287,897,256
Gifts and grants	32,188,514	24,638,487
Investment income	115,494,681	56,517,381
Interest on capital asset-related debt	(13,497,227)	(13,062,343)
Other nonoperating revenues and expenses, net	2,769,041	3,343,018
Net nonoperating revenues (expenses)	451,248,564	359,333,799
Net gain (loss) before other revenues, expenses, gains, or losses	145,934,209	78,107,025
Capital appropriations	475,068	732,166
Capital grants and gifts	62,176,096	18,915,305
Additions to permanent endowments, including Research Challenge Trust Funds of $9,076,476 in 2006 and $14,519,692 in 2005	24,335,856	33,650,404
Transfer of net assets of Lexington Community College	-	(4,968,447)
Other, net	2,274,682	(1,756,512)
Total other revenues (expenses)	89,261,702	46,572,916
INCREASE IN NET ASSETS	235,195,911	124,679,941
NET ASSETS, beginning of year	1,863,156,490	1,738,476,549
NET ASSETS, end of year	$ 2,098,352,401	$ 1,863,156,490

See notes to consolidated financial statements.

UNIVERSITY OF KENTUCKY AND AFFILIATED CORPORATIONS
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Student tuition and fees	$ 144,545,367	$ 133,441,920
Grants and contracts	286,950,184	258,728,281
Recoveries of facilities and administrative costs	41,178,394	40,344,165
Sales and services	45,488,455	38,667,103
Federal appropriations	14,746,791	15,724,706
County appropriations	12,176,710	11,089,895
Payments to vendors and contractors	(552,055,367)	(548,680,341)
Student financial aid	(23,306,717)	(29,178,203)
Salaries, wages and benefits	(970,650,005)	(810,390,049)
Professional clinic service fees	154,322,459	149,498,425
Hospital services	509,198,455	441,273,315
Auxiliary enterprise receipts:		
Housing and Dining	36,405,967	32,062,046
Athletics	46,092,778	41,574,832
Other auxiliaries	20,003,727	20,479,035
Loans issued to students	(16,292,186)	(13,313,757)
Collection of loans to students	16,844,054	13,359,946
Self insurance receipts	38,995,996	32,957,622
Self insurance payments	(35,761,650)	(32,046,168)
Other receipts (payments), net	3,908,082	939,603
Net cash provided (used) by operating activities	(227,208,506)	(203,467,624)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	314,293,555	287,897,256
Gifts and grants received for other than capital purposes:		
Gifts received for endowment purposes	24,335,856	33,650,404
Gifts received for other purposes	30,407,311	25,612,601
Agency and loan program receipts	107,162,039	91,343,086
Agency and loan program payments	(106,656,275)	(96,238,768)
Other nonoperating receipts (payments), net	2,925,762	3,162,632
Net cash provided (used) by noncapital financing activities	372,468,248	345,427,211
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital appropriations	-	(4)
Capital grants and gifts	55,261,693	5,681,344
Purchases of capital assets	(139,469,861)	(112,885,265)
Proceeds from capital debt	126,143,236	29,651,354
Payments to refunding bond agents		(6,174,849)
Proceeds from sales of capital assets	10,400,000	10,089
Principal paid on capital debt and leases	(25,715,475)	(25,106,312)
Interest paid on capital debt and leases	(10,123,824)	(13,057,633)
Other capital and related financing receipts (payments), net	(1,152,936)	2,990,256
Net cash provided (used) by capital and related financing activities	15,342,832	(118,891,020)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	1,687,451,873	1,736,561,278
Interest and dividends on investments	50,560,596	26,415,348
Purchase of investments	(1,796,755,208)	(1,747,280,367)
Net cash provided (used) by investing activities	(58,742,739)	15,696,259
NET INCREASE IN CASH	101,859,835	38,764,826
CASH AND CASH EQUIVALENTS, beginning of year	439,855,232	401,090,406
CASH AND CASH EQUIVALENTS, end of year	$ 541,715,067	$ 439,855,232
Reconciliation of net loss from operations to net cash used by operating activities:		
Operating loss	$ (305,314,355)	$ (281,226,774)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation expense	83,760,995	78,219,096
Change in assets and liabilities:		
Notes, loans and accounts receivable, net	(25,801,876)	(6,912,821)
Inventories and other assets	(4,576,243)	(1,460,218)
Accounts payable and accrued liabilities	12,042,808	1,549,214
Deferred revenue	10,184,938	2,148,691
Long term liabilities	2,495,227	4,215,188
Net cash used by operating activities	$ (227,208,506)	$ (203,467,624)

See notes to consolidated financial statements.

UNIVERSITY OF KENTUCKY AND AFFILIATED CORPORATIONS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity
The University of Kentucky (the University) is a component unit of the Commonwealth of Kentucky and is included in the basic financial statements of the Commonwealth. The consolidated financial statements of the University include the operations of the University, its for-profit subsidiary (Kentucky Healthcare Enterprise, Inc.) and its affiliated non-profit corporations (entities for which the University is financially accountable as defined by Statement No. 14 and amended by Statement No. 39 of the Governmental Accounting Standards Board) as follows: The University of Kentucky Research Foundation and its for-profit subsidiary (Kentucky Technology, Inc.); The Fund for Advancement of Education and Research in the University of Kentucky Medical Center; University of Kentucky Athletic Association; Central Kentucky Management Services, Inc.; University of Kentucky Mining Engineering Foundation, Inc.; University of Kentucky Business Partnership Foundation, Inc.; University of Kentucky Gluck Equine Research Foundation, Inc.; University of Kentucky Humanities Foundation, Inc.; University of Kentucky Center on Aging Foundation, Inc.; and Kentucky Medical Services Foundation, Inc.

Basis of Presentation
The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). GASB establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following net assets categories:

- Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:
  Nonexpendable – Net assets subject to externally imposed stipulations that they be maintained permanently by the University. Such assets include the principal of the University's permanent endowment funds.

  Expendable – Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time.

- Unrestricted: Net assets whose use by the University is not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.

The financial statement presentation is intended to provide a comprehensive, entity-wide perspective of the University's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Summary of Significant Accounting Policies

Accrual Basis. The consolidated financial statements have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation has been incurred. The University reports as a Business Type Activity (BTA) as defined by GASB Statement No. 35. BTA's are those activities that are financed in whole or part by fees charged to external parties for goods and services.

Cash and Cash Equivalents. The University considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Noncurrent cash and cash equivalents includes plant funds allocated for capital projects and endowment fund cash pending transfer to the custodian for investment. Cash and cash equivalents held by the University's endowment fund managers are included in endowment investments.

Inventories. Inventories are stated principally at the lower of average cost or market.

Pooled Endowment Funds. The University employs the total return concept of investment management for setting investment objectives and determining investment performance. This concept recognizes dividends and interest, plus or minus realized and unrealized gains or losses, in determining the total return earned during any particular period. The market value method of accounting for pooled endowment funds is employed to ensure proper distribution of market price changes, realized gains (losses) on sales, accrued income earned, and distribution of investment earnings for expenditure by participating funds.

The Uniform Management of Institutional Funds Act (UMIFA), as adopted by the Commonwealth of Kentucky, permits the University to appropriate an amount of the realized and unrealized endowment appreciation to support current programs. Accordingly, spendable return from the endowment is determined using the total return philosophy. This philosophy recognizes a prudent amount of realized and unrealized gains as spendable return in addition to traditional yield. Distribution of investment earnings for expenditure by participating funds is supported first by traditional yield earned and, if necessary, a transfer from the endowment of any prior years' accumulated earnings (unexpended traditional yield) or net realized or unrealized gains. In fiscal years 2005-06 and 2004-05, the University's endowment spending rule provided for annual distributions of 4.75 percent and 5 percent, respectively, of the three-year moving average market value of fund units. For the years ended June 30, 2006 and 2005 approximately $10,498,000 and $11,481,000, respectively, was transferred from endowment realized and unrealized gains to support current programs in accordance with the University's endowment spending rule. Appreciation on endowments available to support future spending rule distributions amounted to approximately $123,774,000 at June 30, 2006.

The Investment Committee of the University's Board of Trustees has approved a spending rate distribution for fiscal year 2006-07 of 4.50 percent of the three-year moving average market value of fund units. Additionally, the University assesses eligible endowment accounts with a management fee to support fundraising and endowment administration. The management fee was .75 percent and 1 percent, respectively, of total asset value during the years ended June 30, 2006 and 2005. The Investment Committee has approved a management fee of .50 percent of total asset value for fiscal year 2006-07.

Investments. Investments in marketable securities are carried at fair value, as determined by the major securities markets. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the Statement of Revenues, Expenses and Changes in Net Assets.

Capital Assets. Capital assets are stated at cost at date of acquisition or, in the case of gifts, at fair market value at date of gift.

Equipment with a unit cost of $2,000 or more ($1,000 for computers) and having an estimated useful life of greater than one year, is capitalized. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred.

Depreciation of capital assets is computed on a straight-line basis over the estimated useful lives of the respective assets, generally 40 years for buildings, 10 – 25 years for land and building improvements and infrastructure, 10 years for library books and 5 – 20 years for equipment.

The University capitalizes, but does not depreciate, works of art and historical treasures that are held for exhibition, education, research and public service.

Deferred Revenue. Deferred revenue consists primarily of amounts received from grant and contract sponsors that have not yet been earned under the terms of the agreement. Deferred revenue also includes amounts received in advance of an event, such as advance athletic ticket sales relating to future fiscal years and unearned summer school revenue.

Student Tuition and Fees. Student tuition and fees are presented net of scholarship allowances applied to student accounts. Stipends and other payments made directly to students are presented as student financial aid expenses.

Hospital and Clinical Services Revenues. Hospital and clinical services revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including contractual allowances and estimated retroactive adjustments under reimbursement programs with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Income Taxes. The University is an agency and instrumentality of the Commonwealth of Kentucky, pursuant to Kentucky Revised Statutes sections 164.100 through 164.280. Accordingly, the University is excluded from Federal income taxes as an organization described in Section 115 of the Internal Revenue Code of 1986. The majority of the University's affiliated non-profit organizations have received a determination from the Internal Revenue Service granting exemption from federal income taxation pursuant to the provisions of Internal Revenue Code section 501(c)(3).

Restricted Asset Spending Policy. The University's policy is that restrictions on assets cannot be fulfilled by the expenditure of unrestricted funds for similar purposes. The determination on whether restricted or unrestricted funds are expended for a particular purpose is made on a case-by-case basis. Restricted funds remain restricted until spent for the intended purpose.

Operating Activities. The University defines operating activities, as reported on the Statement of Revenues, Expenses and Changes in Net Assets, as those that generally result from exchange transactions, such as payments received for providing goods and services and payments made for goods and services received. Nearly all of the University's expenses are from exchange transactions. Certain significant revenues relied upon for operations, such as state appropriations, gifts and investment income, are recorded as non-operating revenues, in accordance with GASB Statement No. 35.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to use estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The accompanying financial statements include estimates for items such as bad debt and contractual allowances, self-insurance reserves, accrued expenses and other liability accounts.

Recent Accounting Pronouncements. In June 2004, the GASB issued Statement No. 45, "Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions." This statement establishes standards for the measurement, recognition and display of other post employment benefit expenses/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information in the financial reports of employers subject to governmental accounting standards.

Statement No. 45 requires employers to record, as the annual cost of the plan, the actuarially determined Annual Required Contribution. The annual required contribution is calculated to include the normal annual cost for the year for current employees plus a component to amortize the unfunded actuarial accrued liabilities of the plan over a period not to exceed 30 years.

The provisions of this statement are effective for financial statements for fiscal periods beginning after December 15, 2006. The impact of implementing this change in the method of recognizing the cost for post employment retiree health benefits will increase the annual expense associated with providing this benefit from $7.7 million to $14.2 million per year beginning in fiscal year 2008.

2. RESEARCH CHALLENGE TRUST FUND

The Research Challenge Trust Fund (RCTF) was created by the Kentucky General Assembly with the passage of the Postsecondary Education Improvement Act of 1997 (House Bill 1). The objectives of the Trust Fund, as stated in the Bill, include support of efforts by the University of Kentucky to attain status as a top-20 public research university. The RCTF Endowment Match Program provides state funds on a dollar-for-dollar match basis. This program, also known as "Bucks for Brains", supports endowed chairs, professorships and graduate fellowships, and the research and graduate mission of the University.

The status of the RCTF endowed funds as of June 30, 2006, is summarized as follows (in thousands):

	Kentucky General Assembly Funding	University of Kentucky Share of Funding	State Funds Received to Date	Matching Pledges Receivable
1998 Biennium	$ 100,000	$ 66,667	$ 66,667	
2000 Biennium	100,000	68,857	68,857	$ 733
2002 Biennium	100,000	66,667	25,409	6,477
Total	$ 300,000	$ 202,191	$ 160,933	$ 7,210

Interest income of approximately $2.2 million earned on the state matching funds is included in the University's share of the 2000 Biennium funding.

The University expects to fully realize all outstanding matching pledges, however, it may be obligated to return any state funds and accrued interest income related to pledges not received within five years of the initial pledge dates if unable to replace the unpaid pledges with other eligible gifts. A payment schedule of the outstanding pledges is shown below (in thousands):

	2000 Biennium	2002 Biennium
Pledges due in fiscal years 2006 or prior	$ 245	$ 498
Pledges due in fiscal year 2007	359	1,412
Pledges due in fiscal year 2008	99	1,853
Pledges due in fiscal year 2009	30	1,533
Pledges due in fiscal year 2010	-	1,039
Pledges due in fiscal year 2011	-	142
Total	$ 733	$ 6,477

3. DEPOSITS AND INVESTMENTS

The fair value and cost of deposits and investments, by type, at June 30, 2006 and 2005 are as follows (in thousands):

	2006	
	Fair Value	Cost
Deposits with banks and the Commonwealth of Kentucky	$ 45,631	$ 45,631
United States government fixed income securities	129,968	127,682
Common and preferred stocks	67,313	63,102
Pooled equity funds	478,759	401,134
Pooled real estate funds	53,602	47,937
Pooled fixed income funds	510,613	511,008
Corporate fixed income securities	26,156	25,442
Guaranteed investment contracts	38,254	38,225
Repurchase agreements	132,804	132,804
Certificates of deposit	19,264	19,250
Cash and cash equivalents	11,132	11,132
Other	148	148
Total	$ 1,513,644	$ 1,423,495

	2005	
	Fair Value	Cost
Deposits with banks and the Commonwealth of Kentucky	$ 43,199	$ 43,199
United States government fixed income securities	112,086	111,542
Common and preferred stocks	56,339	51,552
Pooled equity funds	334,238	284,841
Pooled real estate funds	42,504	40,378
Pooled fixed income funds	448,873	447,508
Corporate fixed income securities	28,573	27,820
Guaranteed investment contracts	41,712	41,670
Repurchase agreements	66,728	66,728
Equity in healthcare corporations	31,379	31,379
Certificates of deposit	27,810	27,794
Cash and cash equivalents	4,951	4,951
Other	148	148
Total	$ 1,238,540	$ 1,179,510

	2006	2005
Statement of Net Assets classification		
Cash and cash equivalents	$ 369,088	$ 364,987
Current investments	32,109	29,847
Restricted cash and cash equivalents	172,627	74,868
Endowment investments	767,693	555,365
Other long-term investments	172,127	213,473
Total	$ 1,513,644	$ 1,238,540

Included above in the caption "Equity in healthcare corporations" was the University's approximately 84 percent ownership of CHA Service Company (CHA) .(a Kentucky for-profit corporation established to provide an integrated health care delivery system throughout the Commonwealth of Kentucky), which was sold during fiscal 2006 at a gain of approximately $25.1 million. The University accounted for its investment in CHA by the equity method since, under the provision of CHA's by-laws, the University could not exercise control over the day-to-day operations of CHA. A summary of the University's investment in CHA is as follows (in thousands):

	June 30, 2004	Fiscal 2004-05	June 30, 2005	Fiscal 2005-06	June 30, 2006
Capital investment	$ 38,180		$ 38,180		$ 38,180
Equity in income (losses) through December 31, 2004 (CHA fiscal year end) and date of sale	(9,111)	$ 1,226	(7,885)	$ 11,731	3,846
Cash dividend				$ (25,148)	(25,148)
Sale proceeds				$ (41,964)	(41,964)
Gain on sale				$ 25,086	25,086
Net investment	$ 29,069	$ 1,226	$ 30,295	$ (30,295)	$ -

As part of the sale agreement, escrow funds were established totaling $9.5 million to cover any potential unrecorded liabilities or overstatement of asset value and for any additional transaction costs. Any monies remaining in these escrow accounts as of August 2007 will be returned to the University in proportion to its prior ownership interest in CHA. No assets related to this potential gain contingency are recorded in these financial statements.

Deposit and investment policies. The University's Board of Trustees is responsible for establishing deposit and investment policies. Once established, the Board has delegated day-to-day management to the Treasurer of the University, who is also the Treasurer of the Board. Deposit and investment policies are developed to insure compliance with state laws and regulations as well as to establish and maintain sound financial management practices.

The University follows Kentucky Revised Statutes (KRS 42.500) for the investment of public funds, which list allowable investment instruments to include: obligations of the United States or a United States government agency; obligations of any corporation of the United States Government; collateralized certificates of deposit; highly rated uncollateralized certificates of deposit, bankers acceptances and commercial paper; highly rated securities issued by a state or local government; and mutual funds comprised of any of the above allowable investments.

For purposes of investment management, the majority of the University's deposits and investments can be grouped into five significant categories, as follows:

- Overnight investments (deposits and repurchase agreements) with local banks and the Commonwealth of Kentucky;
- Bond revenue fund investments held by the Treasurer of the Commonwealth of Kentucky as required by the University's bond trust indentures, and invested in pooled fixed income funds managed by the Commonwealth of Kentucky;
- Short term investments managed by the University, including individual securities purchased and held by the University and short term investments in pooled fixed income funds managed by the Commonwealth of Kentucky;
- Debt service reserve fund investments required by the University's bond trust indentures and held by the bond trustee;
- Endowment investments administered by the University and managed using external investment managers.

The Treasurer manages the overnight and short term investment programs of the University based on the Statement of Investment Objectives and Policies for Short-Term Current Funds Investments established by the Investment Committee of the University's Board of Trustees.

The University's policy for the investment of bond revenue and debt service reserve funds is governed by each respective bond's trust indenture.

The Investment Committee of the University's Board of Trustees establishes and maintains the University's Endowment Investment Policy.

Deposit and investment risks. The University's deposits and investments are exposed to various risks, including credit, interest rate and foreign currency risk, as discussed in more detail below:

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligation, causing the University to experience a loss of principal.

As a means of limiting its exposure to losses arising from credit risk, the University's investment policies limit the exposure of its various investment types, as follows:

- Overnight investment (deposits and repurchase agreements) policies minimize credit risk in several ways. Deposits are governed by State law which requires full collateralization. Credit risk on repurchase agreements with local banks is mitigated by the issuing financial institution's pledge of specific U.S. treasury or agency securities, held in the name of the University by the Federal Reserve Bank. Credit risk on repurchase agreements with the Commonwealth of Kentucky is mitigated by the Commonwealth's requirement that providers of overnight repurchase agreements collateralize these investments at 102% of face value with U.S. treasury or agency securities, pledged in the name of the Commonwealth.
- Bond revenue fund investments held in the Commonwealth's investment pools can invest in U.S. treasuries and agencies; commercial paper or asset backed securities rated in the highest category by a nationally recognized rating agency; certificates of deposit, bankers acceptances, state or local government securities and corporate, Yankee and Eurodollar securities rated in one of the three highest categories by a nationally recognized rating agency; shares of mutual funds (up to 10%); and state and local property tax certificates of delinquency secured by interests in real estate.
- Short-term investments managed by the University are limited to direct obligations of the U.S. Treasury, other appropriate securities issued by federal agencies, repurchase agreements of U.S. government obligations, and certificates of deposit collateralized by U.S. government obligations or general obligations of the University of Kentucky. Short term investments held in the Commonwealth's investment pools are subject to the same credit quality requirements as denoted above for bond revenue fund investments.
- Investment securities held in bond debt service reserve funds may be invested and reinvested solely in bonds or interest bearing notes of the United States Government.
- Endowment investments held by fixed income managers are generally limited to holdings of high quality fixed income securities. These managers may invest a portion of the portfolio in other below-investment

grade bonds, non U.S. dollar denominated bonds, and emerging market bonds, provided the overall credit quality of the fixed income portfolios is not lower than A-.

The credit quality of the University's fixed income investments as of June 30, 2006, is as follows (in thousands):

	S&P/Moody's Credit Ratings			
	AAA/Aaa	A	BBB/Baa	Not rated
U.S. government fixed income	$ 86,130			
Corporate fixed income	12,378		$ 13,778	
Fixed income pools				$ 501,689
Repurchase agreements				132,804
Cash equivalents	438	$ 2,670		
Total fixed income securities	$ 98,946	$ 2,670	$ 13,778	$ 634,493

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investment or collateral securities that are in possession of an outside party.

As a means of limiting its exposure to losses arising from custodial credit risk, the University's investment policies limit the exposure of its various investment types, as follows:

- Overnight investments (deposits and repurchase agreements) are not exposed to custodial credit risk other than repurchase agreements with the Commonwealth of Kentucky which are held in the Commonwealth's name.
- Bond revenue fund investments and short term investments held in the Commonwealth's investment pools are held in the Commonwealth's name by the Commonwealth's custodian.
- Short term investments managed by the University are held in the University's name by the University's custodian.
- Investment securities held in bond debt service reserve funds are held by the respective bond trustee in a specific trust account for the benefit of the University and bondholders.
- Endowment investments are held in the University's name by the University's custodian.

At June 30, 2006, the following University deposit and investment balances held in the name of the Commonwealth of Kentucky were exposed to custodial credit risk as follows (in thousands):

	State Deposits	Overnight Investments	Bond Revenue Investments	Short-term Investments	Other State Investments	Total
Uninsured and collateralized with securities held by the pledging financial institution's trust department or agent but not in the University's name	$ 35,947	$ 93,000				$ 128,947
Uninsured, not registered in the name of the University and held by the counterparty but not in the University's name			$ 219,632	$ 59,366	$ 142,176	421,174
Total	$ 35,947	$ 93,000	$ 219,632	$ 59,366	$ 142,176	$ 550,121

Concentrations of Credit Risk. University investments can be exposed to a concentration of credit risk if significant amounts are invested in any one issuer.

As a means of limiting its exposure to concentrations of credit risk, the University's investment policies limit concentrations in various investment types, as follows:

- Overnight investments (deposits and repurchase agreements) are not limited as to the maximum amount that may be invested in one issuer. However, all such investments in excess of Federal Depository Insurance are required to be fully collateralized by U.S. treasury and/or U.S. agency securities or other similar investments as provided by KRS 41.240.
- Bond revenue fund investments and short-term investments held in the Commonwealth's investment pools are limited as follows: U.S. dollar denominated corporate and Yankee securities issued by foreign and domestic issuers shall not exceed twenty-five (25) per cent of an individual pool and $25,000,000 per issuer, inclusive of commercial paper, bankers' acceptances and certificates of deposit; and U. S. dollar denominated sovereign debt shall not exceed five (5) per cent of any individual portfolio and $25,000,000 per issuer.
- There is no specific limit on the maximum amount of short term investments managed by the University that may be invested in one issuer. However, such investments are limited to direct U.S. government obligations (U.S. Treasuries) and U.S. government agencies.
- There is no specific limit on the maximum amount of investment securities held in bond debt service reserve funds that may be invested in one issuer. However, such investments are limited to bonds or interest bearing notes of the U.S. government.
- Endowment investment managers are limited to a maximum investment in any one issuer of no more than 5% of total investments.

At June 30, 2006, the University has no investments in any one issuer, other than U.S. treasury and/or agency securities, that represent 5 percent or more of total investments.

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

As a means of limiting its exposure to fair value losses arising from increasing interest rates, the University's investment policies limit the maturity of its various investment types, as follows:

- Overnight investments (deposits and repurchase agreements) have limited exposure to interest rate risk due to the short term nature of the investment. The University requires that all deposits and repurchase agreements be available for use on the next business day.
- Bond revenue fund investments and short-term investments held in the Commonwealth's short term investment pool are limited to a duration that does not exceed 90 days. Such investments in the Commonwealth's intermediate-term investment pool must maintain a modified duration of less than 3 years.
- Short term investments managed by the University are limited to a maximum maturity of 24 months.
- Investment securities held in bond debt service reserve funds are required to have a maturity no later than two years from the date of the investment.
- Endowment investments held by fixed income managers are limited to a duration that is within +/-25% of the duration of the Lehman Aggregate Bond Index.

At June 30, 2006, the University had the following investments managed based on maturities (in thousands):

Investment Type	Fair Value	Maturities in Years Less than 1	1 - 3
U.S. government fixed income	$ 50,052	$ 37,250	$ 12,802
Guaranteed investment contracts	27,942	27,942	
Repurchase agreements	132,804	132,804	
Cash equivalents	5,799	5,799	
Total	$ 216,597	$ 203,795	$ 12,802

At June 30, 2006, the University had the following investments managed based on duration (in thousands):

Investment Type	Fair Value	Modified Duration (Years)
U.S. government fixed income		
Pooled endowment fund	$ 62,624	5.74
Corporate fixed income		
Pooled endowment fund	26,156	4.35
Fixed income pools		
Pooled endowment fund	80,516	5.21
Commonwealth of Kentucky intermediate pool	230,351	1.30
Commonwealth of Kentucky short term pool	190,822	0.11
Total	$ 590,469	

Foreign Currency Risk. Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit.

The University's exposure to foreign currency risk derives from certain limited endowment investments, including pooled fixed income funds, a pooled global equity fund, and a pooled non-U.S. equity fund. The University's endowment investment policy allows fixed-income managers to invest a portion of their funds in non-U.S. securities and equity fund managers of co-mingled portfolios to invest in accordance with the guidelines established in the individual fund's prospectus.

At June 30, 2006, the following endowment investments were subject to foreign currency risk (in thousands):

Endowment Investment	Fair Value
Pooled fixed income funds	$ 4,929
Pooled global equity fund	61,287
Pooled non-U.S. equity fund	83,588
	$ 149,804

4. NOTES, LOANS AND ACCOUNTS RECEIVABLE

Notes, loans and accounts receivable as of June 30, 2006 and 2005, respectively, are as follows (in thousands):

	2006		
	Gross Receivable	Allowance	Net Receivable
Hospital patient accounts	$ 68,087	$ (13,901)	$ 54,186
KMSF patient accounts	24,016	(6,151)	17,865
Student loans	25,939	(2,494)	23,445
Reimbursement receivable - grants and contracts	49,167	-	49,167
Pledges receivable	23,638	(8,359)	15,279
Accrued interest receivable	4,215	-	4,215
Student receivables	8,090	(2,854)	5,236
Other	18,298	(660)	17,638
Total	$ 221,450	$ (34,419)	$ 187,031
Current portion			$ 154,909
Non-current portion			32,122
Total			$ 187,031

	2005		
	Gross Receivable	Allowance	Net Receivable
Hospital patient accounts	$ 63,199	$ (12,611)	$ 50,588
KMSF patient accounts	30,003	(10,894)	19,109
Student loans	27,213	(2,760)	24,453
Reimbursement receivable - grants and contracts	29,066	-	29,066
Pledges receivable	15,768	(5,986)	9,782
Accrued interest receivable	3,214	-	3,214
Student receivables	8,426	(4,388)	4,038
Other	19,133	(1,555)	17,578
Total	$ 196,022	$ (38,194)	$ 157,828
Current portion			$ 126,763
Non-current portion			31,065
Total			$ 157,828

5. CAPITAL ASSETS, NET

Capital assets as of June 30, 2006, and capital asset activity for the year ended June 30, 2006, are summarized as follows (in thousands):

	June 30, 2005	Additions	Deletions	June 30, 2006
Land	$ 39,559	$ 5,122		$ 44,681
Land improvements - nonexhaustible	13,128	3,195	$ 32	16,291
Land improvements - exhaustible	45,787	5,306	23	51,070
Buildings	1,125,326	70,672	11,371	1,184,627
Fixed equipment - communications	40,253	4,247	27	44,473
Infrastructure	44,779	3,238	63	47,954
Equipment	351,879	49,686	28,211	373,354
Vehicles	17,699	1,840	1,011	18,528
Library materials	118,856	5,628	351	124,133
Nondepreciable library materials	5,947	366	-	6,313
Capitalized software	31,465	18,747	-	50,212
Art	6,969	85	-	7,054
Construction in progress	54,802	38,571	50,265	43,108
	1,896,449	206,703	91,354	2,011,798
Accumulated Depreciation				
Land improvements - exhaustible	39,841	2,094	-	41,935
Buildings	464,944	30,775	666	495,053
Fixed equipment - communications	21,036	3,088	-	24,124
Infrastructure	8,334	1,884	-	10,218
Equipment	227,735	35,181	19,971	242,945
Vehicles	13,003	1,505	867	13,641
Library materials	90,228	5,906	-	96,134
Capitalized software	3,264	3,328	-	6,592
	868,385	83,761	21,504	930,642
Capital assets, net	$ 1,028,064	$ 122,942	$ 69,850	$ 1,081,156

Capital assets as of June 30, 2005, and capital asset activity for the year ended June 30, 2005, are summarized as follows (in thousands):

	June 30, 2004	Additions	Deletions	June 30, 2005
Land	$ 39,258	$ 811	$ 510	$ 39,559
Land improvements - nonexhaustible	8,048	5,080	-	13,128
Land improvements - exhaustible	44,375	1,412	-	45,787
Buildings	1,048,919	76,407	-	1,125,326
Fixed equipment - communications	32,953	7,300	-	40,253
Infrastructure	34,799	9,980	-	44,779
Equipment	345,853	31,064	25,038	351,879
Vehicles	16,549	1,827	677	17,699
Library materials	115,698	4,605	1,447	118,856
Nondepreciable library materials	-	5,947	-	5,947
Capitalized software	14,254	17,211	-	31,465
Art	6,893	76	-	6,969
Construction in progress	89,562	42,281	77,041	54,802
	1,797,161	204,001	104,713	1,896,449
Accumulated Depreciation				
Land improvements - exhaustible	38,193	1,648	-	39,841
Buildings	436,829	28,115	-	464,944
Fixed equipment - communications	18,366	2,670	-	21,036
Infrastructure	6,742	1,592	-	8,334
Equipment	216,747	34,188	23,200	227,735
Vehicles	12,118	1,515	630	13,003
Library materials	85,568	5,459	799	90,228
Capitalized software	232	3,032	-	3,264
	814,795	78,219	24,629	868,385
Capital assets, net	$ 982,366	$ 125,782	$ 80,084	$ 1,028,064

At June 30, 2006, the University has construction projects in process totaling approximately $512 million in scope. The estimated cost to complete these projects is approximately $469 million. Such construction is principally financed by proceeds from the University's general receipts bonds and by capital appropriations from the Commonwealth of Kentucky.

The University has utilized capital leases to acquire various items of equipment costing approximately $14.9 million. Additionally, the University has entered into capital lease agreements with the State Property and Buildings Commission and lease financing agreements with the Kentucky Asset/Liability Commission to finance renovations to Commonwealth Stadium and for the construction of several educational buildings and the new hospital patient care facility. The University has also utilized a capital lease to fund the purchase and implementation of its new administrative computing systems.

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2006 and 2005, respectively, are as follows (in thousands):

	2006	2005
Payable to vendors and contractors	$ 46,336	$ 53,083
Accrued expenses, including vacation and sick leave	42,685	44,974
Employee withholdings and deposits payable to third parties	37,299	20,019
Total	$ 126,320	$ 118,076

7. DEFERRED REVENUE

Deferred revenue as of June 30, 2006 and 2005, respectively, is as follows (in thousands):

	2006	2005
Unearned summer school revenue	$ 4,421	$ 4,692
Unearned hospital revenue	12,542	9,644
Unearned grants and contracts revenue	28,906	20,744
Prepaid athletic ticket sales	9,162	8,245
Unearned state deferred maintenance pool funds	-	475
Other	2,491	4,575
Total	$ 57,522	$ 48,375

8. LONG-TERM LIABILITIES

Long-term liabilities as of June 30, 2006, and long-term liability activity for the year ended June 30, 2006, are summarized as follows (in thousands):

	June 30, 2005	Additions	Reductions	June 30, 2006	Current Portion	Noncurrent Portion
Bonds, notes and capital leases						
General receipts Notes		$ 107,540		$ 107,540		$ 107,540
General receipts Bonds		7,160		7,160	$ 245	6,915
Educational buildings bonds	$ 141,565	11,495	$ 13,890	139,170	12,945	126,225
Housing and dining bonds	77,055	-	3,055	74,000	3,155	70,845
Hospital bonds	1,770	-	1,770	-	-	-
Library bonds	41,415	-	1,165	40,250	1,215	39,035
Capital leases	66,077	4,845	5,727	65,195	5,110	60,085
Notes payable	3,104	3,017	2,713	3,408	2,608	800
Total bonds, notes and capital leases	330,986	134,057	28,320	436,723	25,278	411,445
Other liabilities						
Medical malpractice	27,964	5,067	3,252	29,779	3,396	26,383
Long term disability	10,460	1,899	2,303	10,056	1,912	8,144
Annuities payable	5,691	419	173	5,937	559	5,378
Health insurance	8,614	27,176	27,332	8,458	8,458	-
Federal loan programs	21,840	1,081	1,032	21,889	-	21,889
Workers compensation	4,235	4,565	3,524	5,276	3,300	1,976
Mining and Minerals Trust	55	-	55	-	-	-
Compensated absences	3,000	250	-	3,250	473	2,777
Supplemental disability	342	284	195	431	254	177
Arbitrage rebate	365	190	190	365	-	365
Unamortized bond premium	-	2,267	85	2,182	113	2,069
Outstanding check liability	450	596	450	596	596	-
Unemployment compensation	419	505	469	455	455	-
Other	1,079	377	749	707	707	-
Total other liabilities	84,514	44,676	39,809	89,381	20,223	69,158
Total	$ 415,500	$ 178,733	$ 68,129	$ 526,104	$ 45,501	$ 480,603

Long-term liabilities as of June 30, 2005, and long-term liability activity for the year ended June 30, 2005, are summarized as follows (in thousands):

	June 30, 2004	Additions	Reductions	June 30, 2005	Current Portion	Noncurrent Portion
Bonds, notes and capital leases						
Educational buildings bonds	$ 154,325		$ 12,760	$ 141,565	$ 13,610	$ 127,955
Housing and dining bonds	79,275	$ 6,230	8,450	77,055	3,055	74,000
Hospital bonds	3,850	-	2,080	1,770	1,770	-
Library bonds	42,520	-	1,105	41,415	1,165	40,250
Capital leases	43,086	29,700	6,709	66,077	5,003	61,074
Notes payable	3,485	3,062	3,443	3,104	2,713	391
Total bonds, notes and capital leases	326,541	38,992	34,547	330,986	27,316	303,670
Other liabilities						
Medical malpractice	25,960	5,004	3,000	27,964	3,205	24,759
Long term disability	11,607	1,739	2,886	10,460	1,934	8,526
Annuities payable	5,646	231	186	5,691	494	5,197
Health insurance	5,455	25,224	22,065	8,614	8,614	-
Federal loan programs	21,414	1,346	920	21,840	-	21,840
Workers compensation	5,677	1,395	2,837	4,235	3,542	693
Mining and Minerals Trust	55	-	-	55	55	-
Compensated absences	2,750	250	-	3,000	454	2,546
Supplemental disability	608	57	323	342	195	147
Arbitrage rebate	278	191	104	365	64	301
Outstanding check liability	413	450	413	450	450	-
Unemployment compensation	303	612	496	419	419	-
Other	-	1,079	-	1,079	719	360
Total other liabilities	80,166	37,578	33,230	84,514	20,145	64,369
Total	$ 406,707	$ 76,570	$ 67,777	$ 415,500	$ 47,461	$ 368,039

Principal maturities and interest on bonds, notes and capital leases for the next five years and in subsequent five-year periods as of June 30, 2006, are as follows (in thousands):

	Principal	Interest	Total
2007	$ 25,278	$ 17,468	$ 42,746
2008	26,996	17,315	44,311
2009	27,024	16,421	43,445
2010	32,042	15,434	47,475
2011	23,234	14,323	37,558
2012-2016	104,960	58,542	163,502
2017-2021	115,108	34,221	149,329
2022-2026	82,081	9,170	91,251
Total	$ 436,723	$ 182,894	$ 619,617

At June 30, 2006, assets with a fair market value of approximately $50,349,000 have been placed on deposit with trustees to totally defease bonds with a par amount of $53,475,000. The liability for these fully defeased bonds is not included in the financial statements.

9. COMPONENTS OF RESTRICTED EXPENDABLE NET ASSETS

Restricted expendable net assets are subject to externally imposed stipulations or conditions that must be followed and cannot be used for support of general operations of the University. At June 30, 2006 and 2005, respectively, restricted expendable net assets were composed of the following (in thousands):

	2006	2005
Appreciation on permanent endowments	$ 102,827	$ 74,636
Term endowments	6,867	5,655
Quasi-endowments initially funded with restricted assets	43,177	43,525
Funds restricted for capital purposes	68,000	19,271
Funds restricted for non-capital purposes	77,352	65,830
Loan funds (primarily University funds required for Federal match)	8,972	8,726
Total	$ 307,195	$ 217,643

10. DESIGNATIONS OF UNRESTRICTED NET ASSETS

Unrestricted net assets are designated for specific purposes by action of the Board of Trustees or management or may otherwise be limited by contractual agreements. Commitments for the use of unrestricted net assets at June 30, 2006 and 2005, respectively, are as follows (in thousands):

	2006	2005
Working capital requirements	$ 246,063	$ 54,447
Budget appropriations for future year fiscal operations	32,462	27,057
Designated for capital projects	53,958	59,783
Designated for renewal and replacement of capital assets	73,396	169,265
Hospital	133,858	125,263
Affiliated corporations	64,190	65,989
Total	$ 603,927	$ 501,804

11. PLEDGED REVENUES

Under the University's General Receipts Trust Indenture, substantially all of the unrestricted operating and non-operating revenues of the University are pledged to secure the payment of debt. As of June 30, 2006 and 2005, respectively, pledged revenues are as follows (in thousands):

	2006	2005
Student tuition and fees	$ 147,267	$ 133,389
Nongovernmental grants and contracts	33,531	6,880
Recoveries of facilities and administrative costs	43,303	40,333
Sales and services	42,826	38,857
Hospital patient services	511,441	440,609
Auxiliary enterprises - housing and dining	36,385	32,142
Auxiliary enterprises - other	20,633	20,699
Other operating revenue	2,222	465
State appropriations	314,294	287,897
Gifts and grants	2,000	1,807
Investment income	5,000	3,987
	$ 1,158,902	$ 1,007,065

12. INVESTMENT INCOME

Components of investment income for the years ended June 30, 2006 and 2005 are as follows (in thousands):

	2006	2005
Interest and dividends earned on endowment investments	$ 13,706	$ 11,294
Realized and unrealized gains and losses on endowment investments	39,368	26,742
Interest and dividends on cash and non-endowment investments	25,157	16,101
Realized and unrealized gains and losses on non-endowment investments	36,272	1,503
Investment income from external trusts	992	877
Total	$ 115,495	$ 56,517

13. FUNDS HELD IN TRUST BY OTHERS

The University is the income beneficiary of various trusts that are held and controlled by independent trustees. For the years ended June 30, 2006 and 2005, the University received income from these trusts of approximately $992,000 and $877,000, respectively. The market value of the external trust assets as of June 30, 2006 and 2005 was approximately $42,401,000 and $40,950,000, respectively. However, as the University does not have ownership of the trust assets held by external trustees, the trusts are recorded at a nominal value of $1 each.

14. PLEDGES AND DEFERRED GIFTS

At June 30, 2006, pledges totaling approximately $39,753,000 are expected to be collected primarily over the next five years, as follows (in thousands):

Operating purposes	$ 6,162
Capital projects	22,118
Endowment principal	11,473
Total	$ 39,753

In accordance with GASB Statement No. 33, "Accounting and Financial Reporting for Nonexchange Transactions," the University is required to record operating and capital pledges as revenue when all eligibility requirements have been met. Endowment pledges are not recognized as revenue until the gifts are actually received. Accordingly, for the years ended June 30, 2006 and 2005, the University recorded the discounted value of operating and capital pledges, net of the allowance for uncollectible pledges, of approximately $15,279,000 and $9,782,000, respectively.

Deferred gifts through insurance, known bequests and irrevocable trusts in which the University has a remainder interest are estimated to be approximately $62,994,000 at June 30, 2006. The University records these amounts as revenue when the cash is received.

15. GRANTS AND CONTRACTS AWARDED

At June 30, 2006, grants and contracts of approximately $221 million had been awarded to the University and the University of Kentucky Research Foundation but not expended. These amounts will be recognized in future periods.

16. PENSION PLANS

Regular full-time employees, including faculty, are participants in the University of Kentucky Retirement Plan, a defined contribution plan. The University of Kentucky Retirement Plan consists of five groups as follows:

Group I	Established July 1, 1964, for faculty and certain administrative officials.
Group II	Established July 1, 1971, for staff members in the clerical, technical and service categories.
Group III	Established July 1, 1972, for staff members in the managerial, professional and scientific categories.
Group IV	Established January 1, 1973, for staff members having U.S. Civil Service retirement entitlement.
Group V	Established July 1, 1987, for staff members covered under the Federal Employees Retirement System that replaced Civil Service (those whose employment began during the period from January 1, 1984 to March 31, 1987). Staff members whose employment began after March 31, 1987 are under one of the above University of Kentucky Retirement Plans.

Participation in the University of Kentucky Retirement Plan is mandatory for all regular full-time employees in groups I, II and III who are age 30 or older. Participation is voluntary for regular full-time employees under the age of 30 and for those employees in groups IV and V. Participants in groups I, II, III and IV contribute 5 percent and the University contributes 10 percent of the participant's eligible compensation to the retirement plan. Participants in group V contribute 1 percent and the University contributes 2 percent of the participant's eligible compensation to the retirement plan.

The University has authorized three retirement plan carriers, as follows:

Teachers Insurance and Annuity Association/College
Retirement Equities Fund (TIAA/CREF)
Fidelity Institutional Services Company
American Century Investments

Under the fully funded University of Kentucky Retirement Plan, the University and plan participants make contributions to provide fully vested retirement benefits to employees in individually owned contracts. The University's contributions and costs for 2006 and 2005 were approximately $58,578,000 and $51,702,000, respectively. Employees contributed approximately $29,120,000 in 2006 and $25,626,000 in 2005. The University's total payroll costs were approximately $804,628,000 and $730,380,000, respectively, for the years ended June 30, 2006 and 2005. The payroll for employees covered by the retirement plan was approximately $585,778,000 and $517,025,000 for 2006 and 2005, respectively.

In addition to retirement benefits provided from the group retirement plan, the University provides supplemental retirement income benefits to certain eligible employees in each of the retirement groups (see Note 17).

17. MINIMUM ANNUAL RETIREMENT BENEFITS AND SUPPLEMENTAL RETIREMENT INCOME

Employees in retirement groups I, II and III, referred to in Note 16, who were age 40 or older prior to the date of establishment of each group plan, and who were employed by the University prior to that date, qualify for the minimum annual retirement benefit provisions of the retirement plan. Benefits for these eligible employees are based upon a percentage, determined through years of service, of the participant's annual salary in the last year of employment prior to retirement. Retirement benefits as determined are funded by each individual retiree's accumulation in the group retirement plan, with the balance, if necessary, provided by the University as supplemental retirement income.

The Legislature of the Commonwealth of Kentucky has appropriated funds to the University for the payment of supplemental retirement income benefits since adoption of the group retirement plans, and is expected to continue this practice. However, the Constitution of the Commonwealth of Kentucky prohibits the commitment of future revenues beyond the end of the current biennium. Accordingly, the University does not recognize the liability for supplemental retirement income benefits during the service life of covered employees, but recognizes its costs when funds are appropriated by the Legislature and payments are made. The University intends to continue paying supplemental retirement income benefits contingent upon the Legislature continuing to appropriate funds required to make these payments. Supplemental retirement benefit payments were approximately $3,255,000 and $3,460,000 for the years ended June 30, 2006 and 2005, respectively.

The latest actuarial valuation was prepared as of July 1, 2006, by TIAA. The actuarial present value of accumulated supplemental retirement income benefits as determined by this valuation, utilizing an assumed rate of return of 7 percent, was $18,356,000.

18. HEALTH INSURANCE BENEFITS FOR RETIREES

The University provides a health care credit towards health insurance coverage to retirees who have a minimum of fifteen years service. The University recognizes the cost of providing this credit by expensing the credit in the year provided. These health care credits totaled approximately $7,716,000 and $7,311,000 for the years ended June 30, 2006 and 2005, respectively. At June 30, 2006, there were approximately 2,200 retirees who met the service requirement and were receiving the health care credit.

19. RISK MANAGEMENT

The University is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by (1) the State Fire and Tornado Insurance Fund (the Fund), (2) Sovereign Immunity and the State Board of Claims, or (3) in the case of risks not covered by the Fund and Sovereign Immunity, commercial insurance, participation in insurance risk retention groups or self-insurance.

The Fund covers losses to property from fire, wind, earthquake, flood and most other causes of loss between $250,000 and $500,000 per occurrence. Losses in excess of $500,000 are insured by commercial carriers up to $500 million per occurrence, buildings at replacement cost and contents on an actual cash value basis. As a state agency, the University is vested with Sovereign Immunity and is subject to the provisions of the Board of Claims Act, under which the University's liability for certain negligence claims is limited to $200,000 for any one person or $350,000 for all persons damaged by a single act of negligence. Claims against educators' errors and omissions and wrongful acts are insured through a reciprocal risk retention group. There have been no significant reductions in insurance coverage from 2005 to 2006. Settlements have not exceeded insurance coverage during the past three years.

The University and its agents are insured against medical malpractice by a combination of Sovereign Immunity, self-insurance, commercial liability insurance, and an excess coverage fund established by the Commonwealth of Kentucky. The malpractice liability at June 30, 2006, is based on the requirements of GASB Statement No. 10, which requires that a liability for claims be recorded if it is probable that a liability has occurred and the amount of loss can be reasonably estimated. The liability includes an estimate for claims that have been incurred but not reported at June 30, 2006.

The University is self-insured for the long-term disability income program and has established a 501(c)(9) trust for purposes of paying claims and establishing necessary reserves. The estimated long-term disability payments for known claims at June 30, 2006 are reported at their present value assuming an investment yield of 6 percent.

The University also self-insures certain employee benefits, including health insurance, worker's compensation, unemployment claims, and a long-term disability supplemental reserve, to the extent not covered by insurance. The University has recorded an estimate for asserted claims at June 30, 2006.

Long-term liabilities related to self-insurance are detailed in Note 8, above.

20. CONTINGENCIES

The University is defendant in various lawsuits. However, University officials are of the opinion, based on advice of in-house legal counsel, that the effect of the ultimate outcome of all litigation will not be material to the future operations or financial position of the University.

21. NATURAL CLASSIFICATION

The University's operating expenses by natural classification were as follows for the years ended June 30, 2006 and 2005, respectively (in thousands):

	2006	2005
Salaries and wages	$ 793,519	$ 665,604
Employee benefits	191,789	164,016
Repairs and maintenance	23,653	65,461
Supplies	163,189	165,894
Depreciation	82,617	78,219
Student scholarships and financial aid	36,110	38,531
Utilities	102,409	50,255
Communications	6,595	17,912
Professional services	110,225	94,802
Travel	15,953	13,743
Resale	12,553	9,297
Other, various	94,109	104,471
Total	$ 1,632,721	$ 1,468,205

22. RECLASSIFICATIONS

Certain reclassifications to fiscal 2005 comparative amounts have been made to conform to the 2006 classifications.

23. SUBSEQUENT EVENTS

On July 19, 2006, the University sold $24,325,000 of University of Kentucky General Receipts Bonds (Student Health Facility Project), 2006 Series A, at a net interest cost of 4.50%. The proceeds of the bond issue will be used for constructing and equipping a new University student health facility on the main campus of the University.

University of Kentucky
Albert B. Chandler Medical Center
University Hospital
Consolidated Financial Statements

Management's Discussion and Analysis

The following Management's Discussion and Analysis, or MD&A, provides an overview of the financial position and activities of the University of Kentucky Albert B. Chandler Medical Center University Hospital (the Hospital) and it's wholly-owned for-profit subsidiary for the years ended June 30, 2006 and 2005. Management has prepared this discussion, and we encourage you to read it in conjunction with the consolidated financial statements and the notes appearing in this report.

About the University Hospital

The UK Chandler Medical Center, which opened in 1960, is considered one of the nation's finest academic medical centers. The faculty, students and staff take pride in achieving excellence in education, patient care, research, and community service. As one of two Level 1 Trauma Centers in the state and the first health-care facility in central and eastern Kentucky to obtain distinction as a Primary Stroke Center, UK Hospital cares for the most critically injured and ill patients in the region. The 473-bed UK Hospital and Kentucky Children's Hospital are supported by more than 500 faculty physicians and dentists, 400 resident physicians, and a staff of 3,300 health professionals committed to high-quality patient care.

The Hospital's mission is to help the people of the Commonwealth and beyond gain and retain good health through creative leadership and quality initiatives in patient care, education and research. The Hospital serves patients primarily from central and eastern Kentucky and offers a full spectrum of routine and specialty services appropriate for a major regional quaternary care center.

Financial Highlights

The Hospital's overall financial position remains strong with assets of $683.5 million and liabilities of $161.7 million. Net assets, which represent the Hospital's residual interest in assets after liabilities are deducted, were $521.8 million or 76.3 percent of total assets. For the fiscal year ended June 30, 2006, the Hospital reported net income before other changes in net assets of $76.4 million, generating a margin of 14.8 percent.

- Financial results for fiscal year 2006 significantly exceeded revenue expectations with net inpatient revenue increasing approximately $47.6 million or 15.9 percent over the prior fiscal year and net outpatient revenues increasing $22.8 million or 16.3 percent over the previous fiscal year. The additional revenues are primarily the result of increases in patient activity and rate increases in selected services.
- Total assets increased $174.2 million or 34.2 percent. This increase is primarily due to the proceeds from the hospital project notes issued during the current year in the amount of $107.5 million plus the increase in net assets from current year operating and non-operating net income of $65.2 million.
- Total liabilities increased $109.0 million or 207.0 percent, primarily due to the issuance of the $107.5 million of hospital project notes denoted above.
- Total net assets increased $65.2 million or 14.3 percent.
- Operating revenues increased $72.9 million or 16.5 percent.
- Operating expenses increased $79.5 million or 19.6 percent due primarily to increases in personnel costs and supplies due to increased patient activity, and increases in the provision for uncollectible accounts.
- Nonoperating revenues increased $37.3 million due primarily to the increase in equity in income of unconsolidated investees of $10.3 million and the gain of $25.1 million on the sale of the Hospital's equity investment in CHA.
- During the year, the Hospital invested $150.0 million of available cash in the University of Kentucky pooled endowment fund. It is intended that this cash will remain invested for the foreseeable future and that it will generate a superior return on investment in excess of overnight investment rates.

Operating Statistics

The following table presents utilization statistics for the Hospital for fiscal years ended 2006, 2005 and 2004:

Statistics	2006	2005	2004
Discharges:			
Medicare	6,225	5,574	4,591
Medicaid	7,005	6,544	5,942
Commercial/Blue Cross	8,827	7,933	7,095
Patient/charity	2,703	2,218	2,036
Total discharges	24,760	22,269	19,664
Average daily census	369	336	308
Average length of stay	5.43	5.51	5.72
Patient Days:			
Medicare	37,998	32,871	27,971
Medicaid	41,012	41,084	40,507
Commercial/Blue Cross	41,710	36,099	32,170
Patient/charity	13,800	12,650	11,927
Total patient days	134,520	122,704	112,575
Outpatient visits:			
Hospital clinics	275,608	266,245	246,546
Emergency visits	44,646	42,909	40,320
Total visits	320,254	309,154	286,866

Total discharges increased by 2,491 or 11.2 percent compared to the prior fiscal year. The major factor in this increase was improved recruitment and retention of medical faculty and staff combined with an increase in available beds.

Total patient days increased by 11,816 or 9.6 percent. The case mix index increased to 1.7119 from 1.7064 and the average length of stay decreased to 5.43 from 5.51.

Total outpatient visits increased by 11,100 or 3.6 percent over the prior year.

Using the Consolidated Financial Statements

The Hospital presents its financial reports in a “business type activity” format, in accordance with Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments* and GASB Statement No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities – an amendment of GASB Statement No. 34*. In addition to this MD&A section, the financial report includes a Statement of Net Assets, a Statement of Revenues, Expenses and Changes in Net Assets, a Statement of Cash Flows, and Notes to the Financial Statements. GASB requires that statements be presented on a consolidated basis to focus on the Hospital as a whole.

Reporting Entity

The University of Kentucky Albert B. Chandler Medical Center University Hospital is a division of the University of Kentucky (the University). The consolidated financial statements include Kentucky Healthcare Enterprise, Inc. (KHE), a wholly-owned for-profit subsidiary (collectively, the Hospital).

The University Hospital provides inpatient, outpatient and emergency care services for residents of the Commonwealth of Kentucky.

Consolidated Statement of Net Assets

The Consolidated Statement of Net Assets is the Hospital's balance sheet. It reflects the total assets, liabilities and net assets (equity) of the Hospital as of June 30, 2006, with comparative information as of June 30, 2005. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as non-current. Net assets, the difference between total assets and total liabilities, are an important indicator of the Hospital's current financial condition, while the change in net assets is an indicator of whether the overall financial position has improved or worsened during the year. Generally, assets and liabilities are reported using current values. A major exception is capital assets, which are stated at historical cost, less accumulated depreciation. A summarized comparison of the Hospital's assets, liabilities and net assets at June 30, 2006, 2005 and 2004 is as follows:

Condensed Consolidated Statements of Net Assets (in thousands)

ASSETS	**2006**	**2005**	**2004**
Current assets	$ 260,494	$ 322,867	$ 283,907
Capital assets, net of depreciation	156,412	133,279	138,277
Other noncurrent assets	266,586	53,183	51,765
Total assets	683,492	509,329	473,949
LIABILITIES			
Current liabilities	39,136	42,165	33,743
Noncurrent liabilities	122,522	10,487	11,844
Total liabilities	161,658	52,652	45,587
NET ASSETS			
Invested in capital assets, net of related debt	131,137	130,986	133,078
Restricted expendable	2,855	687	569
Unrestricted	387,842	325,004	294,715
Total net assets	$ 521,834	$ 456,677	$ 428,362

Assets. As of June 30, 2006, the Hospital's total assets amounted to approximately $683.5 million. Cash and cash equivalents represented the Hospital's largest asset, totaling $282.7 million or 41.4 percent of total assets. Long-term investments totaling $156.9 million or 23.0 percent of total assets were the Hospital's next largest asset. Capital assets, net of depreciation, totaling $156.4 million or 22.9 percent of total assets represent another significant asset of the Hospital. The Hospital had accounts receivable totaling $52.1 million or 7.6 percent of total assets at year end.

Total assets increased by $174.2 million during the year ended June 30, 2006. This increase was driven by:

- The proceeds from the issuance of $107.5 million in hospital project notes and
- Current year operating and non-operating net income of $65.2 million.

Liabilities. At June 30, 2006, the Hospital's liabilities totaled approximately $161.7 million. Long-term debt which consists of hospital project notes issued during the current fiscal year represents the largest liability of $107.5 million or 66.5 percent of total liabilities. Accrued expenses, primarily payroll, vacation and other employee benefits, totaled $22.1 million or 13.7 percent of liabilities. Accounts payable represent approximately $15.9 million or 9.8 percent of liabilities.

Net Assets. Net assets at June 30, 2006 totaled approximately $521.8 million, or 76.3 percent of total assets. Net assets invested in capital assets, net of related debt, totaled $131.1 million or 25.1 percent of total net assets. Restricted net assets totaled approximately $2.9 million or less than one percent of total net assets. Unrestricted net assets accounted for $387.8 million or 74.3 percent of total net assets. Total net assets increased $65.2 million or 14.3 percent.

Restricted net assets are subject to externally imposed restrictions governing their use. Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the unrestricted net assets have been internally designated for capital projects and working capital requirements.

Consolidated Statement of Revenues, Expenses and Changes in Net Assets

The Consolidated Statement of Revenues, Expenses and Changes in Net Assets is the Hospital's income statement. It details how net assets have increased (or decreased) during the year ended June 30, 2006, with comparative information for the year ended June 30, 2005. This statement is prepared on the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. All items that increase or decrease net assets must appear on the Consolidated Statement of Revenues, Expenses and Changes in Net Assets as revenues, expenses, gains or losses.

Financial activities are reported as either operating or nonoperating. GASB Statement No. 35 requires state appropriations and gifts to be classified as nonoperating revenues. The utilization of long-lived capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life. A summarized comparison of the Hospital's revenues, expenses and changes in net assets for the years ended June 30, 2006, 2005 and 2004 is as follows:

Condensed Consolidated Statements of Revenues, Expenses and Changes in Net Assets (in thousands)

	2006	2005	2004
OPERATING REVENUES			
Net patient service revenues	$ 509,444	$ 439,027	$ 369,044
Sales and services	5,375	2,908	2,938
Total operating revenues	514,819	441,935	371,982
OPERATING EXPENSES			
Salaries and wages	150,247	126,685	112,151
Fringe benefits	39,236	32,898	28,180
Supplies	105,832	85,194	79,210
Purchased services	74,063	66,178	51,071
Other expenses	44,019	35,208	28,819
Provision for uncollectible accounts	51,638	39,380	26,753
Provision for depreciation and amortization	19,210	19,234	15,139
Total operating expenses	484,245	404,777	341,323
OPERATING INCOME - continuing operations	30,574	37,158	30,659
NONOPERATING REVENUES (EXPENSES)			
State appropriations	1,053	1,053	1,053
Gifts	1,149	1,012	1,405
Investment income	6,098	5,674	834
Interest expense	(117)	(85)	(290)
Gain (loss) on disposal of capital assets	344	(418)	(22)
Other	645	-	8
Gain on sale of investment	25,086	-	-
Equity in income (loss) of unconsolidated investees	11,524	1,266	(5,973)
Income before other revenues, expenses, gains or losses	76,356	45,660	27,674
Transfer to the University of Kentucky-noncapital	(10,833)	(13,347)	(9,684)
Transfer (to) from the University of Kentucky-Capital	(323)	(3,958)	206
DISCONTINUED OPERATIONS			
Net loss from discontinued operations	(43)	(40)	(78)
Loss on disposal of capital assets	-	-	(31)
Net loss from discontinued operations	(43)	(40)	(109)
Total increase in net assets	65,157	28,315	18,087
Net assets, beginning of year	456,677	428,362	410,275
Net assets, end of year	$ 521,834	$ 456,677	$ 428,362

Operating Revenues:

Total operating revenues were approximately $514.8 million for the year ended June 30, 2006, an increase of approximately $72.9 million or 16.5 percent over 2005. Net patient revenues increased $70.4 million or 16.0 percent in fiscal year 2006 over 2005.

The most significant source of operating revenue for the Hospital was net patient service revenue of $509.4 million. Of the $72.9 million increase in operating revenues, essentially all came from net patient revenues. Approximately 50% of net patient service revenue was the result of increased patient activity in almost all services due to improved recruitment and retention of medical faculty and staff combined with an increase in available beds. The balance of the net patient service revenue increase was due to rate increases for selected services, primarily outpatient services. Patient service revenues are net of estimated allowances from contractual arrangements with Medicare, Medicaid, and other third-party payors and have been estimated based on the terms of reimbursement and contracts currently in effect.

The following table shows net patient revenue by funding source for fiscal years ended June 30, 2006, 2005 and 2004 (in thousands):

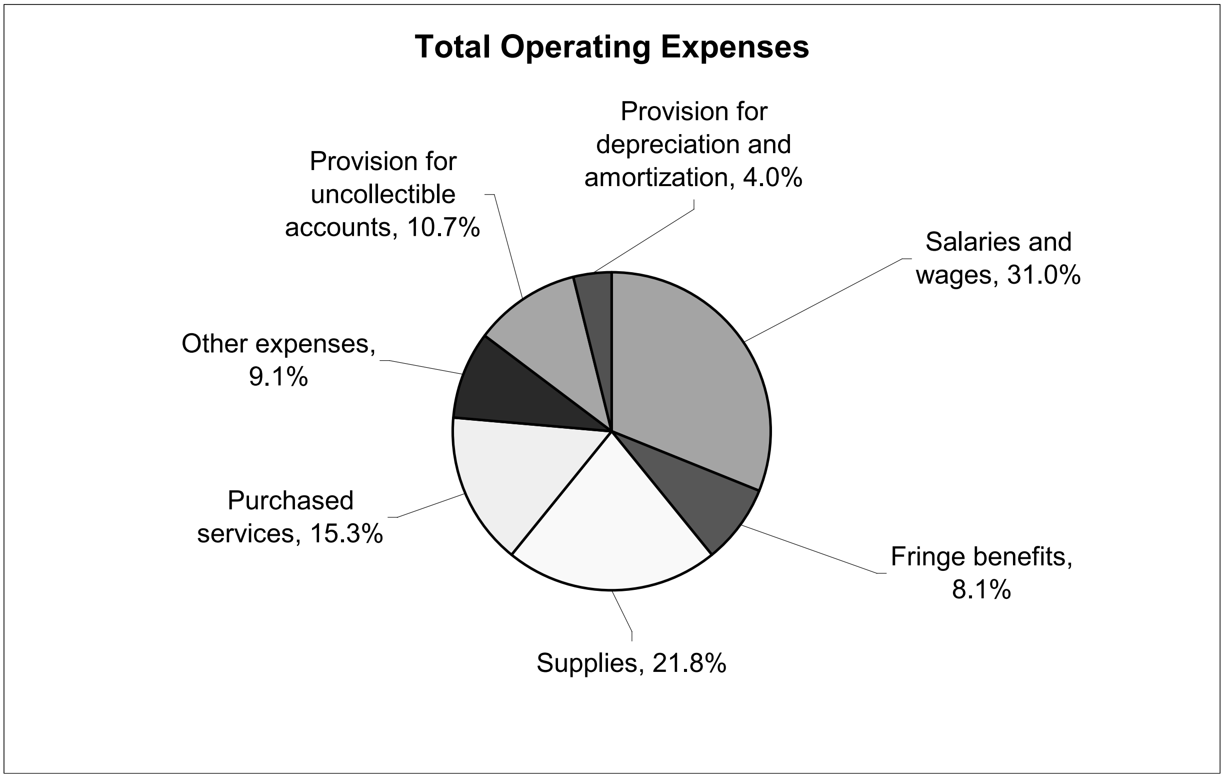
Payor	2006	2005	2004
Medicare	$ 133,772	$ 107,903	$ 90,288
Medicaid	112,925	102,020	91,739
Commercial/Blue Cross	219,505	186,618	152,223
Patient/charity	43,242	42,486	34,794
Total	$ 509,444	$ 439,027	$ 369,044

Net revenues for Medicare represent payments for services provided to patients under Title XVIII of the Social Security Act. Payments for inpatient services provided to Medicare beneficiaries are paid on a per-discharge basis at rates set at the national level with adjustments for prevailing area labor costs. The Hospital also receives additional payments for direct and indirect costs for graduate medical education, disproportionate share of indigent patients, capital reimbursement, and outlier payments on cases with unusually high costs of care. Hospital outpatient care is reimbursed under a prospective payment system. Medicare reimburses the Hospital for allowable costs at a tentative rate with final settlement of such items determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. Settlements with the Medicare program for prior years cost reports are recognized in the year the settlement is resolved.

Net revenues for Medicaid represent payments for services provided to Medicaid beneficiaries. Payments for inpatient services are paid on a per discharge basis and include Intensity Operating Allowance revenues, which are intergovernmental transfer payments available for public institutions to assure access to medical care for Medicaid participants. Outpatient services are reimbursed based upon a combination of fee schedule, per case and retrospective cost settlement basis.

Net revenues for patient/charity include reimbursement for uncompensated care by the Commonwealth of Kentucky from Disproportionate Share Hospital funds.

TOTAL OPERATING EXPENSES



Operating Expenses:

Total operating expenses, including $19.2 million of depreciation, were $484.2 million, an increase of $79.5 million or 19.6 percent over the prior year. Total operating expenses for 2005 increased by $63.5 million or 18.6 percent over 2004.

Salaries and employee benefit expenses increased by $29.9 million over the prior fiscal year due to increased staffing required for the increased patient activity and merit increases. The Hospital added 377.5 FTE's, which added an additional $17.1 million in wages and $4.8 million in benefits, due to the operation of additional beds. The Hospital is licensed to operate 473 beds. The number of available beds increased to 462 in 2006 from 436 in 2005. Salary and employee benefit expenses increased by $19.3 million in fiscal year 2005 over 2004.

Supplies expenses increased by $20.6 million or 24.2 percent mainly due to increases in overall patient activity. Supplies expenses increased in fiscal year 2005 by $6.0 million or 7.6 percent over 2004 due to inflation and volume increases.

Purchased services increased $7.9 million or 11.9 percent from fiscal year 2005. The Hospital purchased services from various departments in the College of Medicine, including resident costs, totaling $59.8 million or an increase of $7.9 million from the prior fiscal year.

Other expenses rose by $8.8 million or 25.0 percent in fiscal year 2006. Utilities accounted for the largest dollar increase of $3.3 million while equipment related expenses, such as maintenance and repair, constituted another $1 million of the increase. Other factors were increased building rental for relocated support units and increased advertising and collection costs.

The provision for uncollectible accounts increased by $12.3 million or 31.1 percent primarily due to the increase in patient service revenues coupled with increases in coinsurance payments and deductibles on commercial insurance, which caused increased provisions in this category of payer.

Nonoperating Revenues (Expenses):

Total nonoperating revenues (expenses) were $45.8 million for fiscal year 2006 compared to $8.5 million for the prior fiscal year. This increase is primarily due to the increase in equity in income of unconsolidated investees of $11.5 million and a gain on the sale of CHA ownership of $25.1 million.

Consolidated Statement of Cash Flows

The Consolidated Statement of Cash Flows details how cash has increased (or decreased) during the year ended June 30, 2006, with comparative financial information for the year ended June 30, 2005. It breaks out the sources and uses of cash into the following categories:

- Operating activities
- Non-capital financing activities
- Capital financing activities
- Investing activities

Cash flows associated with the Hospital's expendable net assets appear in the operating and non-capital financing categories. Capital financing activities include payments for capital assets, proceeds from long-term debt, and debt repayments. Purchases and sales of investments are reflected in investing activities.

The primary purpose of the Consolidated Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the Hospital during the year that will allow financial statement readers to assess the Hospital's:

- Ability to generate future net cash flows,
- Ability to meet obligations as they become due, and
- The possible need for external financing.

A comparative summary of the Hospital's Statement of Cash Flows for the years ended June 30, 2006, 2005 and 2004 is as follows:

<u>Condensed Consolidated Statements of Cash Flows (in thousands)</u>

Cash provided (used) by:	**2006**	**2005**	**2004**
Operating activities	$ 41,446	$ 60,104	$ 59,859
Noncapital financing activities	(16,885)	(10,909)	(5,992)
Capital and related financing activities	60,011	(20,312)	(34,844)
Investing activities	(72,423)	6,260	(4,092)
Net increase in cash and cash equivalents	12,149	35,143	14,931
Cash and cash equivalents, beginning of year	270,554	235,411	220,480
Cash and cash equivalents, end of year	$ 282,703	$ 270,554	$ 235,411

A major source of cash included in operating activities is patient service revenues of $453.1 million. The largest cash payments for operating activities were $225.9 million to suppliers and $193.4 million to employees for salaries, wages and fringe benefits.

Cash used by noncapital financing activities consists primarily of transfers to University of Kentucky for noncapital purposes.

The major source of cash from capital and related financing activities relates to proceeds from capital debt of $109.7 million. The largest use of cash is due to the purchase of capital assets of $37.4 million.

Investing activities include proceeds from sales and maturities of investments of $79.5 million and interest and dividends of $36.6 million. Cash of $189.1 million was used to purchase investments.

Key Ratios

The following table shows key liquidity and capital ratios for fiscal years 2006, 2005 and 2004:

	2006	2005	2004
Days cash on hand	153	251	258
Days of revenue in accounts receivable	37	42	44
Debt service coverage (times)	35.1	14.0	11.9

Days cash on hand decreased to 153 days in fiscal year 2006 from 251 days in fiscal year 2005 due to the transfer of cash to the University endowment pool reflected in the increase in long term investments. Days cash on hand measures the average number of days' expenses the Hospital maintains in cash.

The days of revenue in accounts receivable measures the average number of days it takes to collect patient accounts receivable. Fiscal year 2006 days in accounts receivable decreased by 5 days compared to 2005 days of 42. The main reason for this decrease was increased cash collections resulting from a formal revenue cycle team that focuses on various cash initiatives.

Debt service coverage ratio measures the amount of funds available to cover the principal and interest on long-term debt. The Hospital's ratio for fiscal year 2006 is 35.1 versus 14.0 in fiscal year 2005.

Capital Asset and Debt Administration

Capital Assets

Capital assets, net of accumulated depreciation, totaled approximately $156.4 million at June 30, 2006, a net increase of $23.1 million over the prior year end. Significant changes in capital assets during fiscal 2005-2006 included (in millions):

● Land, buildings and structures, net additions	$	5.4
● Equipment and vehicles, net additions	$	9.9
● Capitalized software additions	$	1.5
● Construction in process, net additions	$	16.8
● Increase in accumulated depreciation, net	$	(10.4)

Debt

At year-end, the Hospital had $108 million in hospital project notes outstanding. The Kentucky General Assembly granted the Hospital authority to issue an additional $150 million in debt for the remaining phases of the construction of the replacement patient care facility.

Economic Factors Impacting Future Periods

The following are known facts and circumstances that will affect future financial results:

- Net operating revenue for FY 2006-07 is budgeted to increase approximately 10.9 percent or $55.7 million due to a rate increase effective July 1, 2006 and a 6.0 percent projected increase in discharges. Growth includes the impact of strategic initiatives in Cardiology, Hematology/Oncology, Orthopedics, Neurosurgery, Digestive Health, and Pediatrics.
- State appropriations continue to remain constant at $1.1 million.
- Risks for the current year include capacity constraints which are being addressed through maximized utilization of existing licensed beds, approval of an increase of sixteen licensed specialty beds and the construction of the replacement hospital facility.
- The first phase of construction for the new hospital has begun, as ground has been broken on a new parking garage for patients and their families that will be completed in 2007. The new one million square foot UK Chandler Hospital will be the cornerstone for a new 20-year, $2.5 billion plan on the south side of campus to construct an academic medical campus of the future that will further accelerate growth in research and health education.
- The Hospital is largely supported by revenue from patient services. The local, state, and national economies, as well as national and state spending priorities affect moneys available for payment for healthcare services. Potential changes at the State and Federal level in Medicare and Medicaid spending could reduce revenues for the Hospital. Employers are shifting more of the cost of healthcare to employees, which may result in increased charity care and bad debt expense.
- Advances in care from new technology are putting upward pressure on the cost of care. To adjust to these changes, the Hospital must make constant improvements in the cost and efficiency of delivering care and programs must be developed and expanded to create new revenues.
- The University does not record a liability for post-employment retiree health benefits. Governmental Accounting Standards require that this liability be recognized in the financial statements beginning June 30, 2008. The impact of implementing this change from a cash basis to an accrual basis for recognizing the cost of post employment retiree health benefits will increase the University's annual expense associated with providing this benefit from $7.7 million to $14.2 million per year beginning in fiscal 2008. The Hospital will recognize its proportionate share of this increase.

UNIVERSITY OF KENTUCKY
ALBERT B. CHANDLER MEDICAL CENTER
UNIVERSITY HOSPITAL
CONSOLIDATED STATEMENTS OF NET ASSETS (in thousands)
JUNE 30, 2006 AND 2005

	2006	2005
ASSETS		
Current Assets		
Cash and cash equivalents	$ 195,078	$ 264,634
Accounts receivable (less allowance for doubtful accounts of $13,901 and $12,611)	52,065	50,229
Inventories and other	10,279	7,164
Accrued interest receivable	95	115
Estimated third-party payor settlements receivable	1,603	-
Notes receivable	1,374	725
Total current assets	260,494	322,867
Noncurrent Assets		
Restricted cash and cash equivalents	87,625	5,920
Equity in health care corporations	-	31,379
Long-term investments	156,901	9,492
Capital assets, net	156,412	133,279
Other assets	22,060	6,392
Total noncurrent assets	422,998	186,462
Total assets	683,492	509,329
LIABILITIES		
Current Liabilities		
Accounts payable	15,920	15,266
Accrued expenses	15,189	18,139
Estimated third-party payor settlements payable	-	2,399
Deferred revenue	7,143	4,446
Long-term debt-current portion	-	1,770
Capital lease obligations-current portion	884	145
Total current liabilities	39,136	42,165
Noncurrent Liabilities		
Accrued expenses	6,880	4,645
Deferred revenue and other	5,399	5,464
Long-term debt	107,540	-
Capital lease obligations	2,703	378
Total noncurrent liabilities	122,522	10,487
Total liabilities	161,658	52,652
NET ASSETS		
Invested in capital assets, net of related debt	131,137	130,986
Restricted		
Expendable		
Debt service	-	4
Capital projects	1,857	-
Other	998	683
Total restricted expendable	2,855	687
Total restricted	2,855	687
Unrestricted	387,842	325,004
Total net assets	$ 521,834	$ 456,677

See notes to consolidated financial statements.

UNIVERSITY OF KENTUCKY
ALBERT B. CHANDLER MEDICAL CENTER
UNIVERSITY HOSPITAL
CONSOLIDATED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (in thousands)
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
OPERATING REVENUES		
Net patient service revenues	$ 509,444	$ 439,027
Sales and services	5,375	2,908
Total operating revenues	514,819	441,935
OPERATING EXPENSES		
Salaries and wages	150,247	126,685
Fringe benefits	39,236	32,898
Supplies	105,832	85,194
Purchased services	74,063	66,178
Other expenses	44,019	35,208
Provision for uncollectible accounts	51,638	39,380
Provision for depreciation and amortization	19,210	19,234
Total operating expenses	484,245	404,777
Net income from continuing operations	30,574	37,158
NONOPERATING REVENUES (EXPENSES)		
State appropriations	1,053	1,053
Gifts	1,149	1,012
Investment income	6,098	5,674
Interest expense	(117)	(85)
Gain (loss) on disposal of capital assets	344	(418)
Other	645	-
Gain on sale of investment	25,086	-
Equity in income (loss) of unconsolidated investees	11,524	1,266
Net nonoperating revenues (expenses)	45,782	8,502
Net income before other revenues, expenses, gains or losses	76,356	45,660
Transfers (to) from the University of Kentucky for noncapital purposes	(10,833)	(13,347)
Transfers (to) from the University of Kentucky for capital purposes	(323)	(3,958)
Total other revenues (expenses)	(11,156)	(17,305)
Loss from discontinued operations (includes $0 and $71 revenue from discontinued operations for 2006 and 2005, respectively)	(43)	(40)
INCREASE IN NET ASSETS	65,157	28,315
NET ASSETS, beginning of year	456,677	428,362
NET ASSETS, end of year	$ 521,834	$ 456,677

See notes to consolidated financial statements.

UNIVERSITY OF KENTUCKY
ALBERT B. CHANDLER MEDICAL CENTER
UNIVERSITY HOSPITAL
CONSOLIDATED STATEMENTS OF CASH FLOWS (in thousands)
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Net patient service revenues	$ 453,113	$ 399,313
Sales and services	7,973	4,056
Payments to vendors and contractors	(225,903)	(186,368)
Salaries, wages and fringe benefits	(193,426)	(156,677)
Other receipts (payments)	(311)	(220)
Net cash provided (used) by operating activities	41,446	60,104
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	1,053	1,053
Gifts	1,149	1,012
Loans to University of Kentucky departmental units	(9,479)	(352)
Payments on loans to University of Kentucky departmental units	1,225	725
Transfers to (from) the University of Kentucky for noncapital purposes	(10,833)	(13,347)
Net cash provided (used) by noncapital financing activities	(16,885)	(10,909)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of capital assets	566	222
Purchases of capital assets	(37,363)	(12,894)
Principal payments-capital leases and long-term obligations	(2,292)	(3,311)
Interest payments-capital leases and long-term obligations	(1,871)	(97)
Proceeds from capital debt	109,722	-
Proceeds from sales and maturities of investments-funds on deposit with trustee	13,053	-
Purchase of investments- funds on deposit with trustee	(20,033)	-
Payments to bond agents- cost of issuance	(1,013)	-
Transfers (to) from the University of Kentucky for capital purposes	(758)	(4,232)
Net cash provided (used) by capital and related financing activities	60,011	(20,312)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	79,488	37
Other income	683	-
Purchase of investments	(189,147)	-
Interest and dividends on investments	36,553	6,223
Net cash provided (used) by investing activities	(72,423)	6,260
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	12,149	35,143
CASH AND CASH EQUIVALENTS, beginning of year	270,554	235,411
CASH AND CASH EQUIVALENTS, end of year	$ 282,703	$ 270,554
Reconciliation of net income from continuing operations to net cash provided (used) by operating activities:		
Operating income - continuing operations	$ 30,574	$ 37,158
Loss from discontinued operations	(43)	(40)
Adjustments to reconcile net income from continuing operations to net cash provided (used) by operating activities:		
Depreciation and amortization	19,210	19,276
Write off of principal - note receivable	152	44
Uncollectible accounts	51,638	39,380
Change in assets and liabilities:		
Accounts receivable	(53,474)	(44,928)
Supplies	(3,064)	(2,254)
Estimated third-party payor settlements receivable	(1,603)	3,052
Other assets	(298)	(221)
Accounts payable and accrued expenses	(2,145)	5,150
Estimated third-party payor settlements payable	(2,399)	2,399
Deferred revenue and other	2,898	1,088
Net cash provided (used) by operating activities	$ 41,446	$ 60,104

See notes to consolidated financial statements.

UNIVERSITY OF KENTUCKY
ALBERT B. CHANDLER MEDICAL CENTER
UNIVERSITY HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The University of Kentucky Albert B. Chandler Medical Center University Hospital is a division of the University of Kentucky (the University). The consolidated financial statements include Kentucky Healthcare Enterprise, Inc. (KHE), a wholly owned for-profit subsidiary (collectively, the Hospital). All significant balances and transactions between University Hospital and its subsidiary have been eliminated.

The University Hospital provides inpatient, outpatient and emergency care services for residents of the Commonwealth of Kentucky.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). GASB establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following net assets categories:

- Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted:

  Nonexpendable – Net assets subject to externally imposed stipulations that they be maintained permanently by the Hospital.

  Expendable – Net assets whose use by the Hospital is subject to externally imposed stipulations that can be fulfilled by actions of the Hospital pursuant to those stipulations or that expire by the passage of time.

- Unrestricted: Net assets whose use by the Hospital is not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.

The financial statement presentation is intended to provide a comprehensive, entity-wide perspective of the Hospital's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Summary of Significant Accounting Policies

Accrual Basis. The consolidated financial statements have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation has been incurred. The Hospital reports as a Business Type Activity (BTA) as defined by GASB Statement No. 35. BTA's are those activities that are financed in whole or part by fees charged to external parties for goods and services.

Cash and Cash Equivalents. The hospital considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Noncurrent cash and cash equivalents include the Hospital's plant funds allocated for capital projects, with the exception of unrestricted renewal and replacement cash, which is included in current cash and cash equivalents.

Pooled Endowment Funds. The Hospital's endowment investments are administered as part of the University's pooled endowment funds. The University employs the total return concept of investment management for setting investment objectives and determining investment performance. This concept recognizes dividends and interest, plus or minus realized and unrealized gains or losses, in determining the total return earned during any particular period. The market value method of accounting for pooled endowment funds is employed to ensure proper distribution of market price changes, realized gains (losses) on sales, accrued income earned, and distribution of investment earnings for expenditure by participating funds.

The Uniform Management of Institutional Funds Act (UMIFA), as adopted by the Commonwealth of Kentucky, permits the University to appropriate an amount of the realized and unrealized endowment appreciation to support current programs. Accordingly, spendable return from the endowment is determined using the total return philosophy. This philosophy recognizes a prudent amount of realized and unrealized gains as spendable return in addition to traditional yield. Distribution of investment earnings for expenditure by participating funds is supported first by traditional yield earned and, if necessary, a transfer from the endowment of any prior years' accumulated earnings (unexpended traditional yield) or net realized or unrealized gains. In fiscal years 2005-06 and 2004-05, the University's endowment spending rule provided for annual distributions of 4.75 percent and 5 percent, respectively, of the three-year moving average market value of fund units. For the year ended June 30, 2006, approximately $1,093,000 was transferred from endowment realized and unrealized gains to support current programs in accordance with the University's endowment spending rule.

The Investment Committee of the University's Board of Trustees has approved a spending rate distribution for fiscal year 2006-07 of 4.50 percent of the three-year moving average market value of fund units. Additionally, the University assesses eligible endowment accounts with a management fee to support fundraising and endowment administration. The management fee was .75 percent and 1 percent, respectively, of total asset value during the years ended June 30, 2006 and 2005. The Investment Committee has approved a management fee of .50 percent of total asset value for fiscal year 2006-07.

Inventories. Inventories are stated principally at the lower of cost or market.

Capital Assets. Capital assets are stated at cost at date of acquisition or, in the case of gifts, at fair market value at date of gift. Equipment with a unit cost of $2,000 or more ($1,000 for computers) and having an estimated useful life of greater than one year is capitalized. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred. Interest costs incurred during construction are capitalized.

Depreciation of capital assets is computed on a straight-line basis over the estimated useful lives of the respective assets, generally 40 years for buildings, 10 – 25 years for land and building improvements and infrastructure and 5 – 20 years for equipment.

Title to all capital assets of the Hospital belongs to the University. The financial information relating to capital assets represents assets that the Hospital occupies and uses. Transfer of capital assets to/from the University represents changes in control of individual assets within divisions of the University from one period to another.

Deferred Revenue. Deferred revenue consists of amounts received from the federal government through the Commonwealth of Kentucky for Disproportionate Share Hospital (DSH) funds and other unearned amounts. The DSH amounts are recognized as revenue over the term of the federal government fiscal year, October 1 – September 30.

Net Patient Service Revenues. Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including contractual allowances and estimated retroactive adjustments under reimbursement programs with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

The Hospital provides services for patients under third-party reimbursement programs, principally Medicare and Medicaid. These payors generally reimburse the Hospital at amounts different from the Hospital's established rates. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits by the fiscal intermediary.

Revenue from the Medicare and Medicaid programs accounted for approximately 26 percent and 22 percent, respectively, of the Hospital's net patient service revenues for the year ended June 30, 2006 and approximately 25 percent and 23 percent, respectively for the year ended June 30, 2005. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Charity Care. The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Since the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Income Taxes. The University, of which the Hospital is an organizational unit, is an agency and instrumentality of the Commonwealth of Kentucky, pursuant to Kentucky Revised Statutes sections 164.100 through 164.280. Accordingly, the University is excluded from Federal Income taxes as an organization described in Section 115 of the Internal Revenue Code of 1986.

Restricted Asset Spending Policy. The Hospital's policy is that restrictions on assets cannot be fulfilled by the expenditure of unrestricted funds for similar purposes. The determination on whether restricted or unrestricted funds are expended for a particular purpose is made on a case-by-case basis. Restricted funds remain restricted until spent for the intended purpose.

Operating Activities. The Hospital defines operating activities, as reported on the Consolidated Statement of Revenues, Expenses and Changes in Net Assets, as those that generally result from exchange transactions, such as payments received for providing goods and services and payments made for goods and services received. Nearly all of the Hospital's revenues and expenses are from exchange transactions. Certain revenues relied upon for operations, such as state appropriations, gifts and investment income, are recorded as non-operating revenues, in accordance with GASB Statement No. 35.

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 amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The accompanying financial statements include estimates for items such as contractual allowances, allowances for doubtful accounts, estimated third-party payor settlements and estimated medical claims payable.

Transactions with the University of Kentucky. Because of the nature of the relationship of the Hospital with the University, the Hospital has substantial transactions with the University, including purchases of various supplies and services. Additionally, the University and its affiliates provide certain administrative support functions to the Hospital. During 2006 and 2005, the Hospital paid approximately $5.8 million and $5.9 million, respectively, to the University as reimbursement for various educational and support functions.

Reclassifications. Certain reclassifications to fiscal 2005 comparative amounts have been made to conform to the fiscal 2006 classifications.

2. DEPOSITS AND INVESTMENTS

The fair value and cost of deposits and investments, by type, at June 30, 2006 and 2005 are as follows:

	2006	
	Fair Value	Cost
Cash on deposit with the Commonwealth of Kentucky	$ 282,703	$ 282,703
United States government securities	9,912	9,956
Investment in University of Kentucky pooled endowment funds	146,989	151,203
Total	$ 439,604	$ 443,862

	2005	
	Fair Value	Cost
Cash on deposit with the Commonwealth of Kentucky	$ 270,554	$ 270,554
United States government securities	9,492	9,677
Equity in health care corporations	31,379	38,180
Total	$ 311,425	$ 318,411

	2006	2005
Statement of Net Assets classification		
Cash and cash equivalents	$ 195,078	$ 264,634
Restricted cash and cash equivalents	87,625	5,920
Long-term investments	156,901	9,492
Equity in health care corporations	-	31,379
Total	$ 439,604	$ 311,425

Included above in the caption "Equity in health care corporations" was the Hospital's approximately 84 percent ownership of CHA Service Company (CHA), a Kentucky for-profit corporation established to provide an integrated health care delivery system throughout the Commonwealth of Kentucky, which was sold during fiscal year 2006 at a gain of approximately $25.1 million. The Hospital accounted for its investment in CHA by the equity method since, under the provision of CHA's by-laws, the Hospital could not exercise control over the day-to-day operations of CHA.

The Hospital also owned a 33 percent interest in Bluegrass Stone Therapy Center, Inc. (Bluegrass Stone), a tax-exempt organization, organized in 1987 as a non-stock corporation to provide outpatient lithotripsy services. During the year Bluegrass Stone was dissolved thus eliminating the Hospital's investment.

A summary of the Hospital's investment in CHA and Bluegrass Stone is as follows (in thousands):

	2006		
	CHA	Bluegrass Stone	Total
Balance, June 30, 2005	$ 30,295	$ 1,084	$ 31,379
Equity in net income	11,731	(207)	11,524
Distributed earnings	(25,148)	(877)	(26,025)
Sale proceeds of investment	(41,964)	-	(41,964)
Gain on sale of investment	25,086		25,086
Balance, June 30, 2006	$ -	$ -	$ -

	2005		
	CHA	Bluegrass Stone	Total
Balance, June 30, 2004	$ 29,069	$ 1,244	$ 30,313
Equity in net income	1,226	40	1,266
Distributed earnings	-	(200)	(200)
Balance, June 30, 2005	$ 30,295	$ 1,084	$ 31,379

As part of the CHA sales agreement, escrow funds were established totaling $9.5 million to cover any potential unrecorded liabilities or overstatement of asset value and for any additional transaction costs. Any monies remaining in these escrow accounts as of August 2007 will be returned to the Hospital in proportion to its prior ownership interest in CHA. No assets related to this potential gain contingency are recorded in these financial statements.

Deposit and investment policies. The University's Board of Trustees is responsible for establishing deposit and investment policies for the Hospital. Once established, the Board has delegated day-to-day management to the Treasurer of the University. Deposit and investment policies are developed to insure compliance with state laws and regulations as well as to establish and maintain sound financial management practices.

The Hospital follows Kentucky Revised Statutes (KRS 42.500) for the investment of public funds, which list allowable investment instruments to include: obligations of the United States or a United States government agency; obligations of any corporation of the United States Government; collateralized certificates of deposit; highly rated uncollateralized certificates of deposit, bankers acceptances and commercial paper; highly rated securities issued by a state or local government; and mutual funds comprised of any of the above allowable investments.

For purposes of investment management, the Hospital's deposits and investments can be grouped into four significant categories, as follows:

- Cash on deposit with the University of Kentucky, which the University invests in deposits and repurchase agreements with local banks and the Commonwealth of Kentucky;
- Bond revenue fund investments are held by the Treasurer of the Commonwealth of Kentucky as required by the University's general receipts trust indenture, and are invested in pooled fixed income funds managed by the Commonwealth of Kentucky;
- Short term investments managed by the University, including individual securities purchased and held by the University and short term investments in pooled fixed income funds managed by the Commonwealth of Kentucky and,
- Endowment investments in the University's pooled endowment fund.

Cash on deposit with the University and short term investments managed by the University follow the University's Statement of Investment Objectives and Policies for Short-Term Current Funds Investments established by the Investment Committee of the University's Board of Trustees.

The Hospital's policy for the investment of bond revenue funds is governed by the University's General Receipts bond trust indenture.

Endowment investments are managed by the University's Endowment Investment Policy as established by the Investment Committee of the University's Board of Trustees, which governs the University's pooled endowment fund.

Deposit and investment risks. The Hospital's deposits and investments are exposed to various risks, including credit, interest rate and foreign currency risk, as discussed in more detail below:

Credit Risk. Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligation, causing the Hospital to experience a loss of principal.

As a means of limiting its exposure to losses arising from credit risk, the University's investment policies limit the exposure of its various investment types, as follows:

- Cash on deposit with the Commonwealth of Kentucky is governed by policy that minimizes credit risk in several ways. Deposits are governed by State law which requires full collateralization. Credit risk on repurchase agreements with local banks is mitigated by the issuing financial institution's pledge of specific U.S. treasury or agency securities, held in the name of the University by the Federal Reserve Bank. Credit risk on repurchase agreements with the Commonwealth of Kentucky is mitigated by the Commonwealth's requirement that providers of overnight repurchase agreements collateralize these investments at 102% of face value with U.S. treasury or agency securities, pledged in the name of the Commonwealth.
- Bond revenue funds held in the Commonwealth's investment pools can be invested in U.S. treasuries and agencies; commercial paper or asset backed securities rated in the highest category by a nationally recognized rating agency; certificates of deposit, bankers acceptances, state or local government securities and corporate, Yankee and Eurodollar securities rated in one of the three highest categories by a nationally recognized rating agency; shares of mutual funds (up to 10%); and state and local property tax certificates of delinquency secured by interests in real estate.
- Short-term investments managed by the University are limited to direct obligations of the U.S. Treasury, other appropriate securities issued by federal agencies, repurchase agreements of U.S. government obligations, and certificates of deposit collateralized by U.S. government obligations or general obligations of the University of Kentucky. Short term investments held in the Commonwealth's investment pools are subject to the same credit quality requirements as denoted above for bond revenue fund investments.
- Endowment investments held by fixed income managers are generally limited to holdings of high quality fixed income securities. These managers may invest a portion of the portfolio in other below-investment grade bonds, non U.S. dollar denominated bonds, and emerging market bonds, provided the overall credit quality of the fixed income portfolios is not lower than A-.

Custodial Credit Risk. Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Hospital will not be able to recover the value of its investment or collateral securities that are in possession of an outside party.

As a means of limiting its exposure to losses arising from custodial credit risk, the University's investment policies limit the exposure of its various investment types, as follows:

- Cash on deposit with the Commonwealth of Kentucky is invested in deposits and repurchase agreements with local banks, which are held in the University's name, and deposits and repurchase agreements with the Commonwealth of Kentucky, which are held in the Commonwealth's name.
- Bond revenue fund investments and short term investments held in the Commonwealth's investment pools are held in the Commonwealth's name by the Commonwealth's custodian.
- Short term investments managed by the University are held in the University's name by the University's custodian.
- Endowment investments are held in the University's name by the University's custodian.

Concentrations of Credit Risk. Hospital investments can be exposed to a concentration of credit risk if significant amounts are invested in any one issuer.

As a means of limiting its exposure to concentrations of credit risk, the University's investment policies limit concentrations in various investment types, as follows:

- Cash on deposit with the University is not limited as to the maximum amount that may be invested in one issuer. However, all such investments in excess of Federal Depository Insurance are required to be fully collateralized by U.S. treasury and/or U.S. agency securities or other similar investments as provided by KRS 41.240.
- Bond revenue fund and short-term investments held in the Commonwealth's investment pools are limited as follows: U.S. dollar denominated corporate and Yankee securities issued by foreign and domestic issuers shall not exceed twenty-five (25) per cent of an individual pool and $25,000,000 per issuer, inclusive of commercial paper, bankers' acceptances and certificates of deposit; and U. S. dollar denominated sovereign debt shall not exceed five (5) per cent of any individual portfolio and $25,000,000 per issuer.
- There is no specific limit on the maximum amount of short term investments managed by the University that may be invested in one issuer. However, such investments are limited to direct U.S. government obligations (U.S. Treasuries) and U.S. government agencies.
- Endowment investment managers are limited to a maximum investment in any one issuer of no more than 5% of total investments.

At June 30, 2006, the Hospital has no investments in any one issuer that represent 5 percent or more of total investments.

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

As a means of limiting its exposure to fair value losses arising from increasing interest rates, the University's investment policies limit the maturity of its various investment types, as follows:

- Cash on deposit with the Commonwealth of Kentucky has limited exposure to interest rate risk due to the short term nature of the investment. The University requires that all deposits and repurchase agreements be available for use on the next business day.
- Bond revenue fund and short-term investments held in the Commonwealth's short term investment pool are limited to a duration that does not exceed 90 days. Such investments in the Commonwealth's intermediate-term investment pool must maintain a modified duration of less than 3 years.
- Short term investments managed by the University are limited to a maximum maturity of 24 months.
- Endowment investments held by fixed income managers are limited to a duration that is within +/-25% of the duration of the Lehman Aggregate Bond Index.

Foreign Currency Risk. Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit.

The Hospital's exposure to foreign currency risk derives from certain limited endowment investments, including pooled fixed income funds, a pooled global equity fund, and a pooled non-U.S. equity fund. The University's endowment investment policy allows fixed-income managers to invest a portion of their funds in non-U.S. securities and equity fund managers of co-mingled portfolios to invest in accordance with the guidelines established in the individual fund's prospectus.

3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net as of June 30, 2006 and 2005 are as follows (in thousands):

	2006	2005
Medicare, Medicaid, and other	$ 50,246	$ 49,532
Private pay and other receivables	1,819	697
Total accounts receivable, net	$ 52,065	$ 50,229

4. CAPITAL ASSETS, NET

Capital assets as of June 30, 2006 and capital asset activity for the year ended June 30, 2006 are summarized as follows (in thousands):

	Beginning Balance	Additions	Deletions	Ending Balance
Land	$ 3,973	$ 4,001		$ 7,974
Non-depreciable land improvements	7	33		40
Depreciable land improvements	3,149	22		3,171
Buildings	152,228	1,272	$ 613	152,887
Fixed equipment	4,891	1,167	-	6,058
Infrastructure	24	40	-	64
Leasehold improvements	536	-	536	-
Equipment	115,319	18,178	8,327	125,170
Vehicles	174	36	-	210
Capitalized software	12,365	1,533	-	13,898
Construction in process	1,541	16,772	8	18,305
	294,207	43,054	9,484	327,777
Accumulated Depreciation:				
Depreciable land improvements	2,651	112	-	2,763
Buildings	83,407	5,128	288	88,247
Fixed equipment	2,233	282	-	2,515
Infrastructure	2	4	-	5
Leasehold improvements	258	-	258	-
Equipment	70,193	11,634	8,620	73,207
Vehicles	74	46	-	121
Capitalized software	2,110	2,397	-	4,507
	160,928	19,603	9,166	171,365
Capital assets, net	$ 133,279	$ 23,451	$ 318	$ 156,412

Capital assets as of June 30, 2005 and capital asset activity for the year ended June 30, 2005 are summarized as follows (in thousands):

	Beginning Balance	Additions	Deletions	Ending Balance
Land	$ 3,162	$ 811		$ 3,973
Non-depreciable land improvements	7	-		7
Depreciable land improvements	3,149	-		3,149
Buildings	150,024	2,215	$ 11	152,228
Fixed equipment	4,322	569	-	4,891
Infrastructure	24	-	-	24
Leasehold improvements	536	-	-	536
Equipment	118,613	8,552	11,846	115,319
Vehicles	174	-	-	174
Capitalized software	10,551	1,814	-	12,365
Construction in process	872	2,354	1,685	1,541
	291,434	16,315	13,542	294,207
Accumulated Depreciation:				
Depreciable land improvements	2,871	(220)	-	2,651
Buildings	78,335	5,083	11	83,407
Fixed equipment	1,918	315	-	2,233
Infrastructure	2	-	-	2
Leasehold improvements	216	42	-	258
Equipment	69,785	12,115	11,707	70,193
Vehicles	30	44	-	74
Capitalized software	-	2,110	-	2,110
	153,157	19,489	11,718	160,928
Capital assets, net	$ 138,277	($3,174)	$ 1,824	$ 133,279

At June 30, 2006 the Hospital has construction projects in process totaling approximately $146.1 million in scope. The estimated cost to complete these projects is approximately $130.6 million.

5. OTHER ASSETS

Other assets at June 30, 2006 and 2005, respectively, are as follows (in thousands):

	2006	2005
Noncurrent portion of non-interesting bearing, unsecured receivable from UK Parking and Transportation, payable $250 annually through 2013	$ 2,000	$ 2,250
Noncurrent portion of non-interesting bearing, unsecured receivable from UK Office of Associate Vice President-Research, payable $500 annually through 2010	1,500	2,000
Noncurrent portion of non-interesting bearing, unsecured receivable from UK Office of Associate Vice President-Research payable $475 annually through 2009	950	1,425
Noncurrent portion of unsecured receivable, bearing interest at 4.34%, from UK Office of Executive Vice President for Research, payable $28 monthly through 2012	1,455	-
Noncurrent portion of non-interest bearing, unsecured receivable from the College of Pharmacy		353
payable at the completion of project	8,000	-
Notes receivable	247	360
Unamortized bond cost of issuance	924	-
Amounts on deposit with trustee, primarily invested in US government agencies, cost $6,980	6,984	4
	$ 22,060	$ 6,392

6. LONG-TERM LIABILITIES

Long-term liabilities as of June 30, 2006 and 2005 are summarized as follows (in thousands):

	2006					
	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion	Noncurrent Portion
Hospital Revenue Bonds	$ 1,770	-	$ 1,770	-	-	-
General Receipts Project Notes	-	$ 107,540	-	$ 107,540	-	$ 107,540
Total	$ 1,770	$ 107,540	$ 1,770	$ 107,540	-	$ 107,540

	2005					
	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion	Noncurrent Portion
Hospital Revenue Bonds	$ 3,850	-	$ 2,080	$ 1,770	$ 1,770	-

Principal maturities and interest on notes for the next five years and in subsequent five-year periods as of June 30, 2006 are as follows (in thousands):

Years ending June 30	Principal	Interest	Total
2007		$ 4,808	$ 4,808
2008		4,808	4,808
2009		4,808	4,808
2010	$ 4,395	4,735	9,130
2011	4,545	4,585	9,130
2012-2016	25,735	19,922	45,657
2017-2021	32,320	13,343	45,663
2022-2026	40,545	5,116	45,661
	$ 107,540	$ 62,124	$ 169,664

Interest costs incurred during the construction, net of related investment income, are capitalized. Total interest capitalized was $2,826 for 2006.

7. CAPITAL LEASE OBLIGATIONS

Capital lease obligations as of June 30, 2006 and 2005 are summarized as follows (in thousands):

	2006	2005
Capital lease obligations, at varying rates of imputed interest of 3.75% to 18.84% collateralized by leased equipment with an amortized cost of $3,790 and $3,970 at June 30, 2006 and 2005	$ 3,587	$ 523
Less current portion	(884)	(145)
Capital lease obligations - long term portion	$ 2,703	$ 378

Scheduled payments of capital lease obligations are as follows:

Years ending June 30	
2007	$ 1,013
2008	951
2009	927
2010	833
2011	168
Total	3,892
Less amount representing interest	(305)
Present value of net minimum lease payments	$ 3,587

8. DESIGNATIONS OF UNRESTRICTED NET ASSETS

Unrestricted net assets are designated for specific purposes by action of the University's Board of Trustees or management or may otherwise be limited by contractual obligations. Commitments for the use of unrestricted net assets at June 30, 2006 and 2005 are as follows (in thousands):

	2006	2005
Working capital requirements	$ 133,858	$ 125,541
Future capital expenditures	253,984	199,463
Total	$ 387,842	$ 325,004

9. INVESTMENT INCOME

Components of investment income for the years ended June 30, 2006 and 2005 are as follows:

	2006	2005
Interest and dividends earned on endowment investments	$ 754	
Realized and unrealized gains and losses on endowment investments	(2,497)	
Interest on cash and non-endowment investments	7,841	$ 5,674
Total	$ 6,098	$ 5,674

10. PROGRAM FOR INDIGENT CARE AND CHARITY CARE

The Hospital is reimbursed for uncompensated care, including indigent care, by the Commonwealth of Kentucky based upon available Disproportionate Share Hospital funds. The amounts are included in net patient service revenues and summarized below (in thousands):

	2006	2005
Revenue from the Commonwealth	$ 26,810	$ 20,269
2.5% tax paid by Hospital on patient cash receipts	(10,449)	(9,003)
Matching contribution paid by Hospital	(8,213)	(6,141)
Net amount received, included in net patient service revenues	$ 8,148	$ 5,125

The amount of charges forgone for services and supplies furnished under the Hospital's charity care policy aggregated to approximately $55,236 and $38,528 in 2006 and 2005, respectively.

11. PLEDGED REVENUES

Substantially all operating and nonoperating revenues are pledged as collateral for the General Receipt Project Notes as of June 30, 2006 and the Hospital's Revenue Bonds as of June 30, 2005.

12. PENSION PLANS

Regular full-time employees of the Hospital are participants in the University of Kentucky Retirement Plan, a defined contribution plan. Hospital employees participate in one of the following three groups of the University of Kentucky Retirement Plan:

Group I	Established July 1, 1964, for faculty and certain administrative officials.
Group II	Established July 1, 1971, for staff members in the clerical, technical and service categories.
Group III	Established July 1, 1972, for staff members in the managerial, professional and scientific categories.

Participation in these groups of the University of Kentucky Retirement Plan is mandatory for all regular full-time employees age 30 and older. Participation is voluntary until age 30. The Hospital contributes 10% and each employee contributes 5% of eligible compensation.
The University has authorized three retirement plan carriers, as follows:

Teachers Insurance and Annuity Association/College
Retirement Equities Fund (TIAA/CREF)
Fidelity Institutional Services Company
American Century Investments

In addition to retirement benefits provided from the group retirement plan, the Hospital provides supplemental retirement income benefits to certain eligible employees of the Hospital.

The total contributions charged to operations for the various retirement plans were approximately $10,557,000 and $8,991,000 for the years ended June 30, 2006 and 2005, respectively. Employees contributed $5,278,500 and $4,495,500 during 2006 and 2005, respectively. The payroll for employees covered by the retirement plans was $105,570,000 and $89,910,000 for 2006 and 2005, respectively.

13. HEALTH INSURANCE BENEFITS FOR RETIREES

The University of Kentucky provides a health care credit towards health insurance to retirees of the Hospital who have a minimum of fifteen years service. The University recognizes the cost of providing this credit by expensing the credit in the year paid.

14. RISK MANAGEMENT

The University, of which the Hospital is an organizational unit, is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by (1) the State Fire and Tornado Insurance Fund (the Fund), (2) Sovereign Immunity and the State Board of Claims, or (3) in the case of risks not covered by the Fund and Sovereign Immunity, commercial insurance, participation in insurance risk retention groups or self-insurance.

The Fund covers losses to property from fire, wind, earthquake, flood and most other causes of loss between $250,000 and $500,000 per occurrence. Losses in excess of $500,000 are insured by commercial carriers up to $500 million per occurrence, buildings at replacement cost and contents on an actual cash value basis. As a state agency, the University is vested with Sovereign Immunity and is subject to the provisions of the Board of Claims Act, under which the University's liability for certain negligence claims is limited to $200,000 for any one person or $350,000 for all persons damaged by a single act of negligence. Claims against educators' errors and omissions and wrongful acts are insured through a reciprocal risk retention group. There have been no significant reductions in insurance coverage from 2005 to 2006. Settlements have not exceeded insurance coverage during the past three years.

The University and its agents are insured against medical malpractice by a combination of Sovereign Immunity, self-insurance, commercial liability insurance, and an excess coverage fund established by the Commonwealth of Kentucky. The malpractice liability at June 30, 2006, is based on the requirements of GASB Statement No. 10, which requires that a liability for claims be recorded if it is probable that a liability has occurred and the amount of loss can be reasonably estimated. The liability includes an estimate for claims that have been incurred but not reported at June 30, 2006. All assets and liabilities related to medical malpractice are recorded in the financial records of the University. However, the Hospital does fund its required share of the actuarially determined medical malpractice expense, and accordingly, no assets or liabilities related to medical malpractice are recorded on the Hospital's financial statements.

The University is self-insured for the long-term disability income program and has established a 501(c)(9) trust for purposes of paying claims and establishing necessary reserves. The estimated long-term disability payments for known claims at June 30, 2006 are reported at their present value assuming an investment yield of 6 percent.

The University also self-insures certain employee benefits, including health insurance, worker's compensation, unemployment claims, and a long-term disability supplemental reserve, to the extent not covered by insurance. The University has recorded an estimate for asserted claims at June 30, 2006.

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15. FUNCTIONAL INCOME/EXPENSES

Below is a summary of functional income/expenses for the year ended June 30, 2006 (in thousands):

	Hospital Operations	Nonhospital Operations	Total
Operating revenue:			
Health care services	$ 509,444		$ 509,444
Other revenues	5,375		5,375
Total operating revenues	514,819		514,819
Operating expenses:			
Health care services	441,894		441,894
General and administrative	42,351		42,351
Total operating expenses	484,245		484,245
	-		
Income from continuing operations	30,574		30,574
Nonoperating revenues (expenses):			
State appropriations	1,053		1,053
Gifts	1,149		1,149
Investment income	6,098		6,098
Interest expense	(117)		(117)
Gain (loss) on disposal of capital assets	344		344
Other	(38)	683	645
Gain on sale of investment		25,086	25,086
Equity in income (loss) unconsolidated investees		11,524	11,524
Net nonoperating revenues	8,489	37,293	45,782
Income before other revenues, expenses, gains or losses	39,063	37,293	76,356
Transfers to UK-noncapital	(10,833)		(10,833)
Transfers to UK-capital	(323)		(323)
General and administrative expenses - discontinued operations		(43)	(43)
Net loss from discontinued operations		(43)	(43)
Increase in net assets	$ 27,907	$ 37,250	$ 65,157

Nonhospital operations include the accounts of KHE and the Hospital’s interests in CHA and Bluegrass Stone.

Below is a summary of functional income/expenses for the year ended June 30, 2005 (in thousands):

	Hospital Operations	Nonhospital Operations	Total
Operating revenues:			
Health care services	$ 439,027		$ 439,027
Other revenues	2,908		2,908
Total operating revenues	441,935		441,935
Operating expenses:			
Health care services	373,748		373,748
General and administrative	31,029		31,029
Total operating expenses	404,777		404,777
Income from continuing Operations	37,158		37,158
Nonoperating revenues (expenses):			
State appropriations	1,053		1,053
Gifts	1,012		1,012
Investment income	5,674		5,674
Interest expense	(85)		(85)
Loss on disposal of capital assets	(418)		(418)
Equity in income (loss) of unconsolidated investees		$ 1,266	1,266
Net nonoperating revenues	7,236	1,266	8,502
Income before other revenues, expenses, gains or losses	44,394	1,266	45,660
Transfer to UK-noncapital	(13,347)		(13,347)
Transfer to UK-capital	(3,958)		(3,958)
Health care services revenue-discontinued operations		71	71
General and administrative expenses-discontinued operations		(111)	(111)
Net loss from discontinued operations		(40)	(40)
Increase in net assets	$ 27,089	$ 1,226	$ 28,315

Nonhospital operations include the accounts of KHE and the Hospital’s interests in CHA and Bluegrass Stone.

APPENDIX D

INFORMATION PERTAINING TO THE COMMONWEALTH OF KENTUCKY

Financial Information Regarding the Commonwealth

The Commonwealth annually publishes *The Kentucky Comprehensive Annual Financial Report* with respect to the Fiscal Year of the Commonwealth most recently ended. The *Kentucky Comprehensive Annual Financial Report* includes certain financial statements of the Commonwealth as well as general financial information pertaining to the Accounting System and Budgetary Controls, Debt Administration, Cash Management, Risk Management, General Fund Budgetary Basis and Governmental Funds GAAP Basis. In addition, the Notes to Financial Statements as set forth in *The Kentucky Comprehensive Annual Financial Report* contain information regarding the basis of preparation of the Commonwealth's financial statements, Funds and Pension Plans. The "Statistical Section" of *The Kentucky Comprehensive Annual Financial Report* includes information on Commonwealth revenue sources, Commonwealth expenditures by function, taxes and tax sources, taxable property, assessed and estimated values, property tax, levies and collections, demographic statistics (population, per capita income and unemployment rate), construction and bank deposits, sources of personal income and largest Commonwealth manufacturers.

Certain Financial Information Incorporated by Reference; Availability from NRMSIRs and the Commonwealth

The Kentucky Comprehensive Annual Financial Report for Fiscal Year 2005 is incorporated herein by reference. The Commonwealth has filed *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2005 with the following Nationally Recognized Municipal Securities Information Repositories ("NRMSIRs") in accordance with SEC Rule 15c2-12:

(i) Bloomberg Municipal Repositories
100 Business Park Drive
Skillman, New Jersey 08558
Email: munis@bloomberg.com
Tel: (609) 279-3225
Fax: (609) 279-5962
Website: http://www.bloomberg.com/markets/rates/municontacts.html

(ii) DPC Data Inc.
One Executive Drive
Fort Lee, New Jersey 07024
Email: nrmsir@dpcdata.com
Tel: (201) 346-0701
Fax: (201) 947-0107
Website: http:/www.dpcdata.com

(iii) Standard & Poor's Securities Evaluations, Inc.
55 Water Street, 45th Floor
New York, New York 10041
Email: nrmsir_repository@sandp.com
Tel: (212) 770-4595
Fax: (212) 770-7994
Website: www.jjkenny.com/jjkenny/pser_descrip_data_rep.html

(iv) FT Interactive Data
Attn: NRMSIR
100 William Street, 15^{th} Floor
New York, New York 10038
Internet: nrmsir@ftid.com
Tel: (212) 771-6999; (800) 689-8466
Fax: (212) 771-7390 (Secondary Market Information)
(212) 771-7391 (Primary Market Information)
Website: http://www.InteractiveData.com

A copy of *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2005 may be obtained from the NRMSIRs or from the Office of Financial Management, 702 Capitol Avenue, Suite 76, Frankfort, Kentucky 40601, (502) 564-2924. Additionally, *The Kentucky Comprehensive Annual Financial Report* for Fiscal Year 2005 and certain other fiscal years may be found on the Internet at:

http://finance.ky.gov/ourcabinet/caboff/ooc/ofm/debt/cafr.htm

Only information contained on the Internet web page identified above is incorporated herein and no additional information that may be reached from such page by linking to any other page should be considered to be incorporated herein.

The Commission will enter into a Continuing Disclosure Agreement in order to enable the purchaser of the Bonds to comply with the provisions of Rule 15c2-12. See "CONTINUING DISCLOSURE" herein. In addition, ongoing financial disclosure regarding the Commonwealth will be available through the filing by the Commonwealth of two documents entitled *The Kentucky Comprehensive Annual Financial Report* and *Supplementary Information to the Kentucky Comprehensive Annual Financial Report* (or successor reports) with the NRMSIRs as required under Rule 15c2-12.

Fiscal Year 2004

The Commonwealth's Government-Wide Financial Statements provide a broad view of the state's operations in a manner similar to a private-sector business. The Commonwealth's combined net assets (governmental and business-type activities) totaled $16.6 billion at the end of 2004, as compared to $16.2 billion at the end of the previous year.

At $17.4 billion, the largest portion of the Commonwealth's net assets is invested in capital assets (e.g. land, infrastructures, buildings and improvements and machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The Commonwealth uses these capital assets to provide services to its citizens; therefore, these assets are not available for future spending.

The second largest portion of the Commonwealth's net assets, totaling $1.38 billion is restricted and represents resources that are subject to either external restrictions or legislative restrictions on how they may be used. The remaining balance is unrestricted net assets. The unrestricted net assets, which if positive could be used at the Commonwealth's discretion, showed a negative balance of $2.2 billion. Therefore, no funds were available for discretionary purposes. A contributing factor to the negative balance is that liabilities are recognized on the government-wide statement of net assets when the obligation is incurred. Accordingly, the Commonwealth recognizes long-term liabilities (such as general bonded debt, compensated absences, unfunded employer pension cost, and contingent liabilities) on the statement of net assets.

The Commonwealth received program revenues of $7.3 billion and general revenues of $8.5 billion for total revenues of $15.8 billion during Fiscal Year 2004. Expenses for the Commonwealth during Fiscal Year 2004 were $15.5 billion, which resulted in a total increase of the Commonwealth's net assets in the amount of $311 million, net of contributions, transfers and special items.

During the fiscal year, the net assets of governmental activities increased by $344 million or 2.10 percent. Approximately 54 percent of the governmental activities' total revenue came from taxes, while 35 percent resulted from grants and contributions (including federal aid). Overall, program revenues were insufficient to cover program expenses for governmental activities. Therefore, the net program expenses of these governmental activities were supported by general revenues, mainly taxes.

The focus of the Commonwealth's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Commonwealth's financing requirements. In particular, unreserved fund balances may serve as a useful measure of a government's net resources available for spending at the end of a Fiscal Year.

At the end of the fiscal year, the Commonwealth's governmental funds reported combined ending fund balances of $2.03 billion, a decrease of $74 million in comparison with the prior year. Approximately half ($999 million or 49 percent) of this total amount constitutes unreserved fund balance, which is available for spending in the coming year. The remainder of fund balance is reserved to indicate that it is not available for new spending.

The General Fund is the chief operating fund of the Commonwealth. At the end of the fiscal year, total fund balance reached $389 million, with an unreserved balance of $304 million. This compares to a General Fund unreserved balance of $184 million as of June 30, 2003. An unreserved fund balance represents the excess of the assets of the General Fund over its liabilities and reserved fund balance accounts. Reservations of fund balances of governmental funds represent amounts that are not available for appropriation. Examples of fund balance reservations reported include reserves for encumbrances, inventories and capital outlay.

The fund balance of the Commonwealth's General Fund increased by $94 million during the fiscal year. This is a 31.4 percent increase in net assets from the prior year. The increase is the result of spending reduction efforts, lapses of appropriations, and an increased number of interfund transfers-in.

The Transportation Fund balance at June 30, 2004 totaled $228 million, a decrease of $207 million during the fiscal year. The decrease primarily relates to an accelerated program for the construction of road projects.

The Commonwealth of Kentucky's bonded debt increased by $60 million to $3,225,431,000, a 1.90 percent increase during the fiscal year. No general obligation bonds were authorized or outstanding at June 30, 2004. The key factor in this increase was the issuance of new debt during Fiscal Year 2004.

Fiscal Year 2005

The Government-Wide Financial Statements provide a broad view of the Commonwealth's operations in a manner similar to a private-sector business. The Commonwealth's combined net assets (governmental and business-type activities) totaled $17.4 billion at the end of 2005, as compared to $16.6 billion at the end of the previous year.

At $17.4 billion, the largest portion of the Commonwealth's net assets is invested in capital assets (e.g. land, infrastructures, buildings and improvements and machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The Commonwealth uses these capital assets to provide services to its citizens; therefore, these assets are not available for future spending.

The second largest portion of the Commonwealth's net assets, totaling $1.46 billion, is restricted and represents resources that are subject to either external restrictions or legislative restrictions on how they may be used. The remaining balance is unrestricted net assets. The unrestricted net assets, which if positive could be used at the Commonwealth's discretion, showed a negative balance of $1.45 billion. Therefore, no funds were available for discretionary purposes. A contributing factor to the negative balance is that liabilities are recognized on the government-wide statement of net assets when the obligation is incurred. Accordingly, the Commonwealth recognizes long-term liabilities (such as general bonded debt, compensated absences, unfunded employer pension cost, and contingent liabilities) on the statement of net assets.

The Commonwealth received program revenues of $7.8 billion and general revenues (including transfers) of $9.3 billion for total revenues of $17.0 billion during Fiscal Year 2005. Expenses for the Commonwealth during Fiscal Year 2005 were $16.1 billion, which resulted in a total increase of the Commonwealth's net assets in the amount of $927 million, net of contributions, transfers and special items.

As a result of the improving economy during the fiscal year, the net assets of governmental activities increased by $850 million or 5.10 percent. Approximately 56 percent of the governmental activities' total revenue came from taxes, while 35 percent resulted from grants and contributions (including federal aid). Overall, program revenues were insufficient to cover program expenses for governmental activities. Therefore, the net program expenses of these governmental activities were supported by general revenues, mainly taxes.

As of the end of the fiscal year, the Commonwealth's governmental funds reported combined ending fund balances of $2.62 billion, an increase of $682 million in comparison with the prior year. The unreserved portion of fund balance ($1.88 billion), which is the portion of fund balance available for spending in the coming year, has increased to 72 percent of the total fund balance. The remainder of fund balance is reserved to indicate that it is not available for new spending.

The General Fund is the chief operating fund of the Commonwealth. At the end of the fiscal year, total fund balance reached $670 million, with an unreserved balance of $593 million. This compares to a General Fund unreserved fund balance of $304 million as of June 30, 2004. An unreserved fund balance represents the excess of the assets of the General Fund over its liabilities and reserved fund balance accounts. Reservations of fund balances of governmental funds represent amounts that are not available for appropriation. Examples of fund balance reservations reported include reserves for encumbrances, inventories and capital outlay.

The fund balance of the Commonwealth's General Fund increased by $284 million during the fiscal year. This is a 72.8 percent increase in net assets from the prior year. The contributing factors to this increase were continuing spending reduction efforts, an improving economy and tax reform.

The Transportation Fund balance at June 30, 2005 totaled $317 million, an increase of $83 million during the fiscal year. The increase primarily relates to completion of an accelerated program which funded the construction of road projects with current available resources.

The Commonwealth of Kentucky's bonded debt increased by $11 million to $3,236,766,000, a .35 percent increase during the fiscal year. No general obligation bonds were authorized or outstanding at June 30, 2005. The key factor in this increase was the issuance of new debt during Fiscal Year 2005.

Fiscal Year 2006 (Unaudited)

Fiscal Year 2006 General Fund revenues totaled $8,376.0 million versus $7,645.0 million for the prior fiscal year, which represents an increase of 9.6 percent. Actual revenues for Fiscal Year 2006 were

$159.9 million above the official revenue estimate on which the Budget Bill was based. Most major taxes exhibited across-the-board growth. Sales and use tax grew 6.0 percent ($154.8 million). Individual income taxes decreased 3.9 percent ($117.6 million), while corporate income taxes increased by a sharp 109.3 percent ($523.1 million) due primarily to lower refund payments. Coal severance taxes rose 21.7 percent ($40.1 million) due to strong energy markets. Property tax receipts grew 6.3 percent ($29.9 million), and the lottery receipts grew 17.8 percent ($28.7 million). Cigarette Tax receipts rose 446.9 percent ($150.5 million) due to an increase in the rate of the tobacco tax and the imposition of a one-time floor stock tax as of May 31, 2005. Per pack taxes increased from 3 cents to 30 cents per pack. The ending General Fund undesignated balance was $681.3 million, which was $136.5 million above the budgeted undesignated balance. $112.5 million of the undesignated balance was deposited in the Budget Reserve Trust Fund, bringing the balance in the fund to 2.7 percent of the estimated General Fund revenues in the Budget Bill for Fiscal Year 2007.

Fiscal Year 2007 (Unaudited)

On December 20, 2005, the Consensus Forecasting Group (the “Group”) released the official General Fund revenue estimates for Fiscal Years 2007 and 2008. The official General Fund revenue estimate for Fiscal Year 2007 was set at $8,341.2 million, an increase of $78.6 million over the preliminary estimate made in October 2005 of $8,262.6 million. The official General Fund revenue estimate for Fiscal Year 2008 was set at $8,675.7 million, an increase of $83.9 million over the preliminary estimate made in October 2005 of $8,581.8 million.

These official General Fund revenue estimates exclude Phase I Tobacco Settlement Agreement (“MSA”) payments, expected to be $88.8 million and $94.0 million in Fiscal Years 2007 and 2008, respectively.

General Fund revenues for July 2006 total $604.4 million, an increase of 1.2 percent compared to July 2005. General Fund revenues for August 2006 total $575.7 million, an increase of 0.6 percent compared to August 2005. Fiscal Year 2007 General Fund revenues total $1,180.1 million through August of 2006, an increase of 0.9 percent over the same two-month time period in Fiscal Year 2006.

During July and August of 2006, sales and use tax grew 5.3 percent over the same two-month period in 2005. Individual income tax receipts slipped 6.7 percent since last July and August due to higher refund payments as well as lower withholding. The Corporation income tax was 101.0 percent higher than last July and August due to both an increase in declaration payments and a more favorable balance on returns. Coal severance taxes rose 2.1 percent, property taxes slipped 3.3 percent, while Lottery revenues rose 10.4 percent over last July and August.

Investment Policy

The Commonwealth's investments are governed by KRS 42.500 et seq. and KAR Title 200 Chapter 14. The State Investment Commission, comprised of the Governor, the Treasurer, Secretary of the Finance and Administration Cabinet and gubernatorial appointees of the Kentucky Banker's Association, is charged with the oversight of the Commonwealth's investment activities. The Commission is required to meet at least quarterly, and delegates day-to-day investment management to the Office of Financial Management.

At June 30, 2006, the Commonwealth's operating portfolio was approximately $4.2 billion in cash and securities. The composition of investments was as follows: U.S. treasury securities (8%); securities issued by agencies, corporations and instrumentalities of the United States Government, including mortgage backed securities and collateralized mortgage obligations (40%); repurchase agreements collateralized by the aforementioned (18%); municipal securities (64%); and corporate and asset backed securities, including money market securities (28%). The portfolio had a current yield of 5.39% and an effective duration of 0.70 years.

The Commonwealth's investments are currently categorized into three investment pool types: Short-term, Intermediate-term and Bond Proceeds Pools. The purpose of these pools is to provide economies of scale that enhance yield, ease administration and increase accountability and control. The Short-term Pool consists primarily of General Fund and related accounts and provides liquidity to the remaining pools. The Intermediate-term Pool represents Agency Fund investments, state held component unit funds and fiduciary fund accounts held for the benefit of others by the Commonwealth. The Bond Proceeds Pool is where bond proceeds for capital construction projects are deposited until expended for their intended purpose.

The Commonwealth engages in selective derivative transactions. These transactions are entered into only with an abundance of caution and for specific hedge applications to minimize yield volatility in the portfolio. The State Investment Commission expressly prohibits the use of margin or other leveraging techniques. The Commonwealth executes a variety of transactions which may be considered derivative transactions, which include: the securities lending program, over-the-counter treasury options, interest rate swaps, mortgage backed securities, collateralized mortgage obligations and asset backed securities.

The Commonwealth has used over-the-counter treasury options since the mid-1980s to hedge and add value to the portfolio of treasury securities. These transactions involve the purchase and sale of put and call options on a covered basis, holding either cash or securities sufficient to meet the obligation should it be exercised. The State Investment Commission limits the total option commitment to no more than twenty percent of the total portfolio of treasury and agency securities. Historically, actual commitments have been less than ten percent of the portfolio.

The Commonwealth has had a securities lending program since the mid-1980s. The Commonwealth is able to enter into either a principal relationship or an agent relationship. In a principal relationship the Commonwealth reverses its treasury, agency and corporate securities in exchange for 102% of eligible collateral, marked to market daily. Eligible Collateral is defined as securities authorized for purchase pursuant to KRS 42.500. In an agent program the agent lends the Commonwealth's treasury, agency and corporate securities, takes the cash received from the loan and invests it in securities authorized for purchase pursuant to KRS 42.500. The income generated by these transactions is split between the agent and the Commonwealth. At the present time the Commonwealth has entered into an agent agreement that has a guarantee of 10 basis points of the average market value of securities in the program.

On June 20, 2003, the State Investment Commission adopted Resolution 03-03, which amended the Commonwealth's investment policy concerning asset-based interest rate swaps. The change modifies the exposure limits from a $200,000,000 notional amount to a net market value approach, the absolute value of which cannot exceed $50,000,000 for all counterparties. The Commonwealth engages in asset-based interest rate swaps to better manage its duration and to stabilize the volatility of interest income.

As of June 30, 2006, the Commonwealth had two asset-based interest rate swaps outstanding. The first swap has a notional amount of $23,000,000 and matures June 15, 2008. The second swap has a notional amount of $10,000,000 and matures June 15, 2011. The net of these positions partially hedges the Commonwealth from widening spreads in a yield curve steepening environment.

Financings of the Commission

General. The Commission has had outstanding obligations in several different forms, including tax and revenue anticipation notes and project notes. Project notes have been issued as General Fund Series, Agency Fund Series, Road Fund Series and Federal Highway Trust Fund Series depending upon the appropriation fund source that is being used to fund the payments under the related financing/lease agreement. Each type of obligation, described below, is secured by the trust indenture to which such types of obligations relate, and holders of notes issued under a particular trust indenture do not have any claim on the pledged receipts of the Commission arising under any other trust indenture.

The holders of the Notes do not have a claim against the moneys pledged under the trust indenture related to any other project notes issued as General Fund Series, Agency Fund Series, Road Fund Series or Federal Highway Trust Fund Series. The indentures for each particular type of notes issued by the Commission generally allow the issuance of additional notes on parity with the outstanding notes of the same type. The Commission's outstanding obligations as of June 30, 2006 are described below.

General Fund Tax and Revenue Anticipation Notes. Since 1997, with the exception of 2003, the Commission has issued General Fund Tax and Revenue Anticipation Notes ("TRANs") on an annual basis corresponding with its fiscal year. The TRANs are payable from taxes and certain revenues collected by the Commonwealth in the Fiscal Year in which they are issued. The 2006 TRAN Series was issued on July 3, 2006 in the amount of $150,000,000 and will mature on June 28, 2007.

Project Notes, General Fund Series. The Commission from time to time issues separate series of project notes, the proceeds of which are used to fund capital projects (the "General Fund Project Notes") authorized by the General Assembly. All General Fund Project Notes are payable from payments to be received by the Commission under separate financing/lease agreements and, as to bond anticipation notes, the issuance of bonds by the State Property and Buildings Commission. The Commission on August 15, 2005, authorized the issuance of an aggregate principal amount not to exceed $750,000,000 of Project Notes, 2005 General Fund Second Series. These payments are ultimately dependent upon General Fund appropriations by the General Assembly of the Commonwealth. The Commission has the following General Fund Project Notes outstanding:

General Fund Project Notes	Amount Issued	Amount Outstanding
2001 General Fund First Series	$37,450,000	$11,925,000
2003 General Fund Series A	171,260,000	84,485,000
2005 General Fund First Series	81,850,000	78,860,000
2005 General Fund Second Series	100,000,000	100,000,000
Total	$390,560,000	$275,270,000

Project Notes, Agency Fund Series. The Commission from time to time also issues separate series of project notes (the "Agency Fund Project Notes"), which are payable from payments to be received by the Commission under financing/lease agreements with various state agencies and from proceeds of bonds to be issued by the State Property and Buildings Commission or a state agency. The payments used to pay Agency Fund Project Notes are ultimately dependent upon Agency Fund appropriations by the General Assembly of the Commonwealth. The Commission on August 15, 2005, authorized the issuance of an aggregate principal amount not to exceed $250,000,000 of Project Notes, 2005 Agency Fund Second Series. These notes may be issued incrementally as needed by various state agencies.

Agency Fund Project Notes	Amount Issued	Amount Outstanding
2005 Agency Fund Taxable First Series	$11,275,000	$11,275,000
2005 Agency Fund Second Series	24,280,000	24,280,000
2005 UK General Receipts Series A	107,540,000	107,540,000
Total	$143,095,000	$143,095,000

Project Notes, Road Fund Series. There are currently no Road Fund Project Notes outstanding.

Project Notes, Federal Highway Trust Fund Series. The Commission is authorized to issue project notes (the "Federal Highway Trust Fund Project Notes") which are payable from payments to be received by the Commonwealth of Kentucky Transportation Cabinet from the Federal Highway Administration. Amounts used to pay those notes are ultimately dependent upon receipt of federal highway funds.

Federal Highway Trust Fund Project Notes	Amount Issued	Amount Outstanding
2005 First Series	$ 139,635,000	$ 136,425,000

Future Financings. The 2005 General Assembly enacted a State Budget for the biennium ending June 30, 2006, which authorized $2.056 billion of bond funded capital projects. The General Fund authorization was $1,204 million; the Road Fund authorization was $450 million; Agency Funds were authorized at $251.7 million; and $150 million was authorized to be supported by the Federal Highway Trust Funds. The Road Fund and Federal Highway Trust Fund authorizations have been issued. A portion of the Agency Fund and General Fund projects have been permanently funded.

The 2006 General Assembly adopted a State Budget for the biennium ending June 30, 2008 which authorized an additional $2.3 billion of capital projects to be funded with debt. The General Fund authorization is $1,392.9 million; the Agency Fund authorizations total $267.5 million; while the Road Fund and Federal Highway Trust Fund authorizations are $350 million and $290 million, respectively. The timing of the issuance of obligations is uncertain.

In 2006, ALCo entered into interest rate swap transactions to hedge the future issuance of approximately $300 million of State Property and Buildings Commission Revenue Bonds that are expected to fund a portion of the remaining authorized, but un-issued bonds for General Fund projects. The interest rate swaps were executed in anticipation of approximately $150 million of State Property and Buildings Commission bonds being sold in each of February 2007 and February 2008.

ALCo may enter into additional interest rate swaps or other agreements to manage the state's interest rate risk profile and/or hedge the future issuance of bonds authorized by the 2005, 2006 and future sessions of the Kentucky General Assembly.

Commonwealth Debt Management

Management

The Office of Financial Management ("OFM"), Finance and Administration Cabinet has central responsibility for the issuance, management, review and approval of all debt issued by the Commonwealth and its agencies. Table I lists state agencies which are active issuing entities. OFM is also responsible for the coordination and monitoring of cash needs relative to debt activity, debt service payments and the development of a comprehensive long-term debt plan. OFM serves as primary staff to the State Property and Buildings Commission, the Kentucky Asset/Liability Commission, and the Kentucky Local Correctional Facilities Construction Authority.

Structure

The Commonwealth's indebtedness is classified as either appropriation supported debt or non-appropriation supported debt.

Appropriation supported debt carries the name of the Commonwealth and is either (i) a general obligation of the State, or (ii) a project revenue obligation of one of its debt issuing agencies created by the Kentucky General Assembly to finance various projects which is subject to state appropriation for all or a portion of the debt service on the bonds.

General obligation bonds pledge the full faith, credit and taxing power of the Commonwealth for the repayment of the debt. The Kentucky Constitution requires voter approval by general referendum prior to the issuance of general obligation bonds in amounts exceeding $500,000. Kentucky has not issued general obligation bonds since 1966. The Commonwealth has no general obligation bonds outstanding.

Project revenue notes and bonds are issued by various debt issuing authorities of the Commonwealth. The revenues produced by the projects funded by the debt are pledged as security for repayment of the debt. Project revenues are not a direct obligation of the Commonwealth. Project revenues are, in some cases, derived partially or solely from biennial appropriations of the General Assembly. In other cases, the direct revenues generated from the project funded constitute the entire source of payment.

Moral obligation debt carries the name of the Commonwealth for the benefit and convenience of agencies or municipal corporations within the State. This type of indebtedness is a special obligation of the issuer, secured and payable solely from the sources pledged for the payment thereof and does not constitute a debt, liability, obligation or a pledge of the faith and credit of the Commonwealth. The General Assembly does not intend to appropriate General Funds to fulfill the financial obligations represented by these types of indebtedness. In most circumstances, in the event of a shortfall the issuer covenants to request from the Governor and the General Assembly sufficient amounts to pay debt service. The Kentucky Infrastructure Authority Governmental Agencies Program and certain Kentucky Higher Education Student Loan Corporation bond issues no longer represent moral obligation debt of the Commonwealth.

Default Record

The Commonwealth has never defaulted in the payment of principal or interest on its general obligation indebtedness or its project revenue obligations.

TABLE I
ACTIVE DEBT ISSUING ENTITIES

ENTITY	STATUTORY AUTHORITY/ PURPOSE	DEBT LIMITATIONS	RATING*
State Property and Buildings Commission	**KRS 56.450** Provide financing for capital construction projects and financing programs approved by the General Assembly.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly.	Aa3/A+/AA-
Kentucky Asset/Liability Commission	**KRS 56.860** Provide interim financing of capital projects and cash flow borrowings to meet working capital needs of the state.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly, exclusive of cash flow borrowings within a fiscal year.	Varies
Turnpike Authority of Kentucky	**KRS 175.410-175.990** Construct, maintain, repair, and operate Turnpike projects, resource recovery roads and economic development roads	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly.	Aa3/AA+/AA-
The State Universities (consisting of nine)	**KRS 56.495** Construct educational buildings and housing and dining facilities.	Cannot incur debt without prior approval of projects and appropriation of debt service by General Assembly.	Varies
Kentucky Housing Corporation	**KRS 198A** Make low interest mortgage loans and construction loans to increase the supply of housing for low and moderate income residents in the State.	Limited to $2.5 billion of debt outstanding	Aaa/AAA/NR
Kentucky Infrastructure Authority	**KRS 224A** Provide financial assistance to local governments for the construction or refinancing of infrastructure facilities and to provide loans to industries for construction of pollution control facilities.	Revolving Fund programs cannot incur debt without appropriation of debt service by the General Assembly. Without legislative approval, other programs are limited to debt outstanding of $500 million.	Aa3/A+/AA-
Kentucky Higher Education Student Loan Corporation	**KRS 164A** Make guaranteed student loans to residents of the state to attend postsecondary institutions and to make loans to students attending postsecondary schools within the state.	Limited to $5.0 billion of debt outstanding.	NR/AAA/AAA (Sr. Series) NR/A/A (Subord. Series)
School Facilities Construction Commission	**KRS 157.611-157.665** Assist local school districts with the financing and construction of school buildings. Finance the construction of vocational education facilities.	Cannot incur debt without appropriation of debt service by General Assembly.	Aa3
Kentucky Economic Development Finance Authority	**KRS 154** Issue industrial revenue bonds on behalf of industries, hospitals, and commercial enterprises in the state. Provide low interest loans to developing businesses. Provide financing and tax credits to manufacturing entities expanding or locating facilities in the state.	None.	Varies
Kentucky Local Correctional Facilities Construction Authority	**KRS 441.605-441.695** Provide an alternative method of constructing, improving, repairing and financing local jails.	Limited to the level of debt service supported by court fees pledged as repayment for the bonds.	Aaa/AAA/NR (Insured)

*Ratings, where applicable, include Moody's, Standard & Poor's and Fitch. S&P rates the Kentucky Infrastructure Authority's bonds which are paid from revenues (not appropriated funds), AA. Certain State Property and Buildings Commission Agency Fund Revenue Bonds may have ratings different than those identified above.

APPENDIX E

BOOK-ENTRY-ONLY SYSTEM

The Notes initially will be issued solely in book-entry-only form to be held in the book-entry-only system maintained by The Depository Trust Company ("DTC"), New York, New York. So long as such book-entry-only system is used, only DTC will receive or have the right to receive physical delivery of Notes and, except as otherwise provided herein with respect to tenders by Beneficial Owners (as hereinafter defined) of beneficial ownership interests, Beneficial Owners will not be or be considered to be, and will not have any rights as, owners or holders of the Notes under the Resolution.

The following information about the book-entry-only system applicable to the Notes has been supplied by DTC. Neither the Commission nor the Trustee makes any representations, warranties or guarantees with respect to its accuracy or completeness.

DTC will act as securities depository for the Notes. The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Note certificate will be issued for each maturity of each Series of the Notes, in the aggregate principal amount of the Notes and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2.2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 100 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, FICC and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Notes under the DTC system must be made by or through Direct Participants, which will receive a credit for the Notes on DTC's records. The ownership interest of each actual purchaser of each Note ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Notes are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Notes, except in the event that use of the book-entry system for the Notes is discontinued.

To facilitate subsequent transfers, all Notes deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Notes with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Notes; DTC's records reflect only the identity of the Direct Participants to whose accounts such Notes are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Notes may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Notes, such as redemptions, tenders, defaults, and proposed amendments to the Note documents. For example, Beneficial Owners of Notes may wish to ascertain that the nominee holding the Notes for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the Trustee and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Notes are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Notes unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Commission as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Notes are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Redemption proceeds, distributions, and interest payments on the Notes will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Commission or the Trustee, on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with bonds held for the accounts of customers in bearer form or registered in "street name" and will be the responsibility of such Participant and not of DTC or its nominee, the Trustee or the Commission, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Commission or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as depository with respect to the Notes at any time by giving reasonable notice to the Commission or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, Note certificates are required to be printed and delivered.

The Commission may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Note certificates will be printed and delivered.

NEITHER THE COMMISSION NOR THE TRUSTEE WILL HAVE ANY RESPONSIBILITY OR OBLIGATION TO ANY DIRECT PARTICIPANT, INDIRECT PARTICIPANT OR ANY BENEFICIAL OWNER OR ANY OTHER PERSON NOT SHOWN ON THE REGISTRATION

BOOKS OF THE TRUSTEE AS BEING A HOLDER WITH RESPECT TO: (1) THE NOTES; (2) THE ACCURACY OF ANY RECORDS MAINTAINED BY DTC OR ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT; (3) THE PAYMENT BY DTC OR ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT OF ANY AMOUNT DUE TO ANY BENEFICIAL OWNER IN RESPECT OF THE PRINCIPAL OR REDEMPTION PRICE OF OR INTEREST ON THE NOTES; (4) THE DELIVERY BY ANY DIRECT PARTICIPANT OR INDIRECT PARTICIPANT OF ANY NOTICE TO ANY BENEFICIAL OWNER WHICH IS REQUIRED OR PERMITTED UNDER THE TERMS OF THE INDENTURE TO BE GIVEN TO HOLDERS; (5) THE SELECTION OF THE BENEFICIAL OWNERS TO RECEIVE PAYMENT IN THE EVENT OF ANY PARTIAL REDEMPTION OF THE NOTES; OR (6) ANY CONSENT GIVEN OR OTHER ACTION TAKEN BY DTC AS HOLDER.

Each Beneficial Owner for whom a Direct Participant or Indirect Participant acquires an interest in the Notes, as nominee, may desire to make arrangements with such Direct Participant or Indirect Participant to receive a credit balance in the records of such Direct Participant or Indirect Participant, to have all notices of redemption or other communications to or by DTC which may affect such Beneficial Owner forwarded in writing by such Direct Participant or Indirect Participant, and to have notification made of all debt service payments.

Beneficial Owners may be charged a sum sufficient to cover any tax, fee, or other governmental charge that may be imposed in relation to any transfer or exchange of their interests in the Notes.

The Commission cannot and does not give any assurances that DTC, Direct Participants, Indirect Participants or others will distribute payments of debt service on the Notes made to DTC or its nominee as the registered owner, or any redemption or other notices, to the Beneficial Owners, or that they will do so on a timely basis, or that DTC, Direct Participants or Indirect Participants will serve and act in the manner described in this Official Statement.

The information in this "APPENDIX E" concerning DTC and DTC's book-entry system has been obtained from sources that the Commission believes to be reliable, but the Commission takes no responsibility for the accuracy thereof.

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APPENDIX F-1

FORM OF BOND COUNSEL'S OPINION FOR 2006A AND 2006B NOTES

October ___, 2006

Commonwealth of Kentucky
Kentucky Asset/Liability Commission
Frankfort, KY

$68,525,000
Commonwealth of Kentucky
Kentucky Asset/Liability Commission
University of Kentucky
General Receipts Refunding Project Notes, 2006 Series A
General Receipts Taxable Refunding Project Notes, 2006 Series B

Ladies and Gentlemen:

We have acted as Bond Counsel in connection with the issuance and sale by the Kentucky Asset/Liability Commission (the "Commission") of $66,305,000 aggregate principal amount of General Receipts Refunding Project Notes, 2006 Series A (the "Series 2006A Notes") and $2,220,000 aggregate principal amount of General Receipts Taxable Refunding Project Notes, 2006 Series B (the "Series 2006B Notes," and together with the Series 2006A Notes, the "Notes"). The Notes are issuable as fully registered Notes without coupons dated as of their date of delivery in the denomination of $5,000 or any integral multiple thereof, bearing interest payable semiannually on April 1 and October 1 of each year commencing on April 1, 2007, at the rates per annum set forth in the schedule below and maturing on October 1, in each of the years and in the principal amounts as follows:

Series A Notes

Maturity Date	Principal Amount	Interest Rate	Maturity Date	Principal Amount	Interest Rate

Series B Notes

Maturity Date	Principal Amount	Interest Rate

The Notes are subject to redemption upon the terms and at the prices set forth therein and as set forth in the Indenture described below.

The Notes are being issued by the Commission, pursuant to the Constitution and laws of the Commonwealth of Kentucky (the "Commonwealth"), including particularly Sections 56.860 et seq. of the Kentucky Revised Statutes, as supplemented and amended (the "Act"), a resolution adopted by the Commission on September 18, 2006 (the "Resolution"), and a Trust Indenture, dated as of October 1, 2006 (the "Indenture"), between the Commission and U.S. Bank National Association having offices in Atlanta, Georgia, as trustee (the "Trustee"). The proceeds of the Notes will be used to provide funds (a) to refund certain outstanding bonds issued by the University and by the State Property and Buildings Commission of the Commonwealth of Kentucky for the benefit of the University as more specifically described in the Indenture, (b) to pay a portion of the costs related to the Patient Care Facility Phase II – Hospital, and (c) to pay the costs of issuance of the Notes, all for the benefit of the University of Kentucky (the "University"). The projects to be financed and refinanced with the proceeds of the Notes (collectively, the "Project") have been leased to the University, pursuant to the Financing/Lease Agreement (the "Lease"), dated as of October 1, 2006, among the Commission, the University and the Finance and Administration Cabinet of the Commonwealth of Kentucky (the "Cabinet").

The Commission has covenanted in the Indenture to at all times do and perform all acts and things permitted by law and necessary or desirable to assure that the interest on the Series 2006A Notes shall, for purposes of federal income taxation, be excludable from the gross income of the recipient.

We have examined the laws of the Commonwealth of Kentucky, the Act, a certified copy of the Indenture, an executed counterpart of the Lease, an executed counterpart of the Escrow Agreement dated as of October 1, 2006, by and between the Commission and U.S. Bank, National Association, as Escrow Agent (the "Escrow Agreement"), an executed counterpart of the Memorandum of Instructions Regarding Use of Proceeds and Arbitrage Compliance dated the date hereof of the Commission, certified copies of proceedings of the Commission authorizing the issuance of the Notes, a copy of an executed note of each of said issue, House Bill 380 of the General Assembly of the Commonwealth of Kentucky, 2006 Regular Session, as enacted and vetoed in part, and such other documents, records, certificates and opinions as we have deemed relevant and necessary in rendering this opinion.

From such examination, we are of the opinion that:

1. The Indenture and the Resolution have been duly authorized, executed and delivered by the Commission, and constitute valid and binding obligations of the Commission enforceable in accordance with their respective terms.

2. The Lease has been duly authorized, executed and delivered by the Commission, the University and the Cabinet, and constitutes the valid and binding obligation of the Commission, the University and the Cabinet, as applicable, enforceable in accordance with its terms.

3. The Escrow Agreement has been duly authorized, executed and delivered by the Commission, and represents a valid and binding agreement of the Commission, enforceable against the Commission in accordance with its terms.

4. Assuming compliance by the Commission with certain covenants, including the covenant referred to in the fourth paragraph of this letter, under existing laws, regulations, rulings and judicial decisions, interest on the Series 2006A Notes (including any original issue discount properly allocable to the owners thereof) is excluded from gross income for federal income tax purposes and is not a special preference item for purposes of the federal alternative minimum tax imposed on individuals and corporations. Interest on the Series 2006A Notes,

however, must be included in the "adjusted current earnings" of certain corporations (i.e., alternative minimum taxable income as adjusted for certain items, including those items that would be included in the calculation of a corporation's earnings and profits under Subchapter C of the Code) and such corporations are required to include in the calculation of alternative minimum taxable income 75% of the excess of each such corporation's adjusted current earnings (which includes tax-exempt interest) over its alternative minimum taxable income (determined without regard to this adjustment and prior to reduction for certain net operating losses).

The accrual or receipt of interest on the Series 2006A Notes may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences will depend upon the recipient's particular tax status or other items of income or deduction. We express no opinion regarding any such consequences. Purchasers of the Series 2006A Notes, particularly purchasers that are corporations (including S corporations and foreign corporations operating branches in the United States), property or casualty insurance companies, banks, thrifts or other financial institutions or certain recipients of Social Security or Railroad Retirement benefits, taxpayers otherwise entitled to claim the earned income credit or taxpayers who may be deemed to have incurred (or continued) indebtedness to purchase or carry tax-exempt obligations are advised to consult their tax advisors as to the tax consequences of purchasing or holding the Series 2006A Notes.

The Notes are payable as to principal, premium, if any, and interest from and are secured by a pledge of and a first lien on the Pledged Receipts, as defined in the Indenture. The Notes do not pledge the general credit or taxing power, if any, of the Commonwealth, the Commission, the University, the Cabinet or any other agency or political subdivision of the Commonwealth.

5. The Notes are not secured by a pledge of or lien on the properties constituting the Project but are payable as to principal and interest solely and only from and are secured by the Pledged Receipts. The ability of the University to make payments under the Lease is dependent upon legislative appropriations to the University, which has leased the Project for an initial term ending on the final maturity date of the Notes.

6. Under the existing laws of the Commonwealth of Kentucky, interest on the Notes is excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Notes are exempt from ad valorem taxation by the Commonwealth of Kentucky and all political subdivisions and taxing authorities thereof.

We express no opinion as to the federal income tax treatment of the interest on the Series 2006B Notes, or as to any tax consequences of purchasing or holding the Series 2006B Notes.

The obligations of the Commission, the University and the Cabinet, and the enforceability thereof, with respect to the Notes and the other documents described above are subject, in part, to the provisions of the bankruptcy laws of the United States of America and to other applicable bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or affecting creditors' rights generally, now or hereafter in effect. Certain of such obligations, and enforcement thereof, are also subject to general equity principles, which may limit the specific enforcement of certain remedies but which do not affect the validity of such documents.

We express no opinion as to the title to, or the sufficiency in the Indenture or otherwise of the description of, the Project, or the priority of any liens, charges or encumbrances on the Project.

Very truly yours,

APPENDIX F-2

FORM OF BOND COUNSEL'S PRELIMINARY OPINION FOR 2007A NOTES

October ___, 2006

Commonwealth of Kentucky
Kentucky Asset/Liability Commission
Frankfort, KY

$77,905,000
Commonwealth of Kentucky
Kentucky Asset/Liability Commission
University of Kentucky
General Receipts Project Notes, 2007 Series A

Ladies and Gentlemen:

We have acted as Bond Counsel in connection with the sale by the Kentucky Asset/Liability Commission (the "Commission") of $77,905,000 aggregate principal amount of General Receipts Project Notes, 2007 Series A (the "Notes"). The Notes are issuable as fully registered Notes without coupons, will be dated as of their date of delivery in the denomination of $5,000 or any integral multiple thereof, and will bear interest payable semiannually on April 1 and October 1 of each year commencing on April 1, 2008, at the rates per annum set forth in the schedule below and maturing on October 1, in each of the years and in the principal amounts as follows:

Maturity Date	Principal Amount	Interest Rate	Maturity Date	Principal Amount	Interest Rate

The Notes are subject to redemption upon the terms and at the prices set forth therein and as set forth in the Indenture described below.

The Notes will be issued by the Commission, pursuant to the Constitution and laws of the Commonwealth of Kentucky (the "Commonwealth"), including particularly Sections 56.860 et seq. of the Kentucky Revised Statutes, as supplemented and amended (the "Act"), a resolution adopted by the Commission on September 18, 2006 (the "Resolution"), and a Trust Indenture, dated as of October 1, 2006 (the "Indenture"), between the Commission and U.S. Bank National Association having offices in Atlanta, Georgia, as trustee (the "Trustee"). The proceeds of the Notes will be used to provide funds (a) to pay a portion of the costs related to the Patient Care Facility Phase II – Hospital, and (b) to pay the costs of issuance of the Notes, all for the benefit of the University of Kentucky (the "University"). The project to be financed with the proceeds of the Notes (the "Project") will be leased to the University, pursuant to the Financing/Lease Agreement (the "Lease"), dated as of October 1, 2006, among the

Commission, the University and the Finance and Administration Cabinet of the Commonwealth of Kentucky (the "Cabinet").

The Commission has covenanted in the Indenture to at all times do and perform all acts and things permitted by law and necessary or desirable to assure that the interest on the Notes shall, for purposes of federal income taxation, be excludable from the gross income of the recipient.

We have examined the laws of the Commonwealth of Kentucky, the Act, a certified copy of the Indenture, an executed counterpart of the Lease, an executed counterpart of the Memorandum of Instructions Regarding Use of Proceeds and Arbitrage Compliance dated the date hereof of the Commission, certified copies of proceedings of the Commission authorizing the issuance of the Notes, a form of note of said issue, House Bill 380 of the General Assembly of the Commonwealth of Kentucky, 2006 Regular Session, as enacted and vetoed in part, and such other documents, records, certificates and opinions as we have deemed relevant and necessary in rendering this opinion.

From such examination, we are of the opinion that:

1. The Indenture and the Resolution have been duly authorized, executed and delivered by the Commission, and constitute valid and binding obligations of the Commission enforceable in accordance with their respective terms.

2. The Lease has been duly authorized, executed and delivered by the Commission, the University and the Cabinet, and constitutes the valid and binding obligation of the Commission, the University and the Cabinet, as applicable, enforceable in accordance with its terms.

3. Assuming compliance by the Commission with certain covenants, including the covenant referred to in the fourth paragraph of this letter, under existing laws, regulations, rulings and judicial decisions, we are of the preliminary opinion that interest on the Notes (including any original issue discount properly allocable to the owners thereof), if issued on the date of this opinion, would be excluded from gross income for federal income tax purposes and would not be a special preference item for purposes of the federal alternative minimum tax imposed on individuals and corporations. Interest on the Notes, however, would be required to be included in the "adjusted current earnings" of certain corporations (i.e., alternative minimum taxable income as adjusted for certain items, including those items that would be included in the calculation of a corporation's earnings and profits under Subchapter C of the Code) and such corporations are required to include in the calculation of alternative minimum taxable income 75% of the excess of each such corporation's adjusted current earnings (which includes tax-exempt interest) over its alternative minimum taxable income (determined without regard to this adjustment and prior to reduction for certain net operating losses).

The accrual or receipt of interest on the Notes may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences will depend upon the recipient's particular tax status or other items of income or deduction. We express no opinion regarding any such consequences. Purchasers of the Notes, particularly purchasers that are corporations (including S corporations and foreign corporations operating branches in the United States), property or casualty insurance companies, banks, thrifts or other financial institutions or certain recipients of Social Security or Railroad Retirement benefits, taxpayers otherwise entitled to claim the earned income credit or taxpayers who may be deemed to have incurred (or continued) indebtedness to purchase or carry tax-exempt obligations are advised to consult their tax advisors as to the tax consequences of purchasing or holding the Notes.

4. The Notes will be payable as to principal, premium, if any, and interest from and will secured by a pledge of and a first lien on the Pledged Receipts, as defined in the Indenture. The Notes will not pledge the general credit or taxing power, if any, of the Commonwealth, the Commission, the University, the Cabinet or any other agency or political subdivision of the Commonwealth.

5. The Notes will not be secured by a pledge of or lien on the properties constituting the Project but will be payable as to principal and interest solely and only from and will be secured by the Pledged Receipts. The ability of the University to make payments under the Lease is dependent upon legislative appropriations to the University, which has leased the Project for an initial term ending on the final maturity date of the Notes.

6. Under the existing laws of the Commonwealth of Kentucky, interest on the Notes will be excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Notes will be exempt from ad valorem taxation by the Commonwealth of Kentucky and all political subdivisions and taxing authorities thereof.

The obligations of the Commission, the University and the Cabinet, and the enforceability thereof, with respect to the Notes and the other documents described above will be subject, in part, to the provisions of the bankruptcy laws of the United States of America and to other applicable bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or affecting creditors' rights generally, now or hereafter in effect. Certain of such obligations, and enforcement thereof, will also subject to general equity principles, which may limit the specific enforcement of certain remedies but which do not affect the validity of such documents.

The Notes have been sold pursuant to the terms of the Forward Delivery Note Purchase Contract (the "Forward Purchase Contract"). Under the Forward Purchase Contract, the Commission has agreed to execute and deliver to Morgan Stanley & Co. Incorporated, as the underwriter of the Notes (the "Underwriter"), and the Underwriter has agreed to accept and purchase from the Commission, the Notes on the delivery date specified in the Forward Purchase Contract (the "Forward Delivery Date"), subject to the satisfaction of certain conditions provided in the Forward Purchase Contract. The issuance and delivery of the Notes on the Forward Delivery Date will be subject to, among other things, receipt of an opinion of Bond Counsel (as defined in the Indenture) confirming the opinions set forth in this opinion letter (the "Confirming Opinion"). During the period between the date of this letter and the Forward Delivery Date new legislation, new court decisions, new regulations, or new rulings may be enacted, promulgated or interpreted that prevent Bond Counsel from delivering the Confirming Opinion or may otherwise affect the substance of the Confirming Opinion, and no assurance can be given that Bond Counsel will be able to deliver the Confirming Opinion on the Forward Delivery Date.

We express no opinion as to the title to, or the sufficiency in the Indenture or otherwise of the description of, the Project, or the priority of any liens, charges or encumbrances on the Project.

Very truly yours,

APPENDIX F-3

FORM OF BOND COUNSEL'S CONFIRMING OPINION FOR 2007A NOTES

[To be dated the date of delivery]

Commonwealth of Kentucky
Kentucky Asset/Liability Commission
Frankfort, KY

$77,905,000
Commonwealth of Kentucky
Kentucky Asset/Liability Commission
University of Kentucky
General Receipts Project Notes, 2007 Series A

Ladies and Gentlemen:

We have acted as Bond Counsel in connection with the issuance and sale by the Kentucky Asset/Liability Commission (the "Commission") of $77,905,000 aggregate principal amount of General Receipts Project Notes, 2007 Series A (the "Notes"). The Notes are issuable as fully registered Notes without coupons, dated as of their date of delivery in the denomination of $5,000 or any integral multiple thereof, bearing interest payable semiannually on April 1 and October 1 of each year commencing on April 1, 2008, at the rates per annum set forth in the schedule below and maturing on October 1, in each of the years and in the principal amounts as follows:

Maturity Date	Principal Amount	Interest Rate	Maturity Date	Principal Amount	Interest Rate

The Notes are subject to redemption upon the terms and at the prices set forth therein and as set forth in the Indenture described below.

The Notes are being issued by the Commission, pursuant to the Constitution and laws of the Commonwealth of Kentucky (the "Commonwealth"), including particularly Sections 56.860 et seq. of the Kentucky Revised Statutes, as supplemented and amended (the "Act"), a resolution adopted by the Commission on September 18, 2006 (the "Resolution"), and a Trust Indenture, dated as of October 1, 2006 (the "Indenture"), between the Commission and U.S. Bank National Association having offices in Atlanta, Georgia, as trustee (the "Trustee"). The proceeds of the Notes will be used to provide funds (a) to pay a portion of the costs related to the Patient Care Facility Phase II – Hospital, and (b) to pay the costs of issuance of the Notes, all for the benefit of the University of Kentucky (the "University"). The project to be financed with the proceeds of the Notes (the "Project") have been leased to the University, pursuant to the Financing/Lease Agreement (the "Lease"), dated as of October 1, 2006, among the

Commission, the University and the Finance and Administration Cabinet of the Commonwealth of Kentucky (the "Cabinet").

The Commission has covenanted in the Indenture to at all times do and perform all acts and things permitted by law and necessary or desirable to assure that the interest on the Notes shall, for purposes of federal income taxation, be excludable from the gross income of the recipient.

We have examined the laws of the Commonwealth of Kentucky, the Act, a certified copy of the Indenture, an executed counterpart of the Lease, an executed counterpart of the Memorandum of Instructions Regarding Use of Proceeds and Arbitrage Compliance dated the date hereof of the Commission, certified copies of proceedings of the Commission authorizing the issuance of the Notes, a copy of an executed Note of said issue, House Bill 380 of the General Assembly of the Commonwealth of Kentucky, 2006 Regular Session, as enacted and vetoed in part, and such other documents, records, certificates and opinions as we have deemed relevant and necessary in rendering this opinion.

From such examination, we are of the opinion that:

1. The Indenture and the Resolution have been duly authorized, executed and delivered by the Commission, and constitute valid and binding obligations of the Commission enforceable in accordance with their respective terms.

2. The Lease has been duly authorized, executed and delivered by the Commission, the University and the Cabinet, and constitutes the valid and binding obligation of the Commission, the University and the Cabinet, as applicable, enforceable in accordance with its terms.

3. Assuming compliance by the Commission with certain covenants, including the covenant referred to in the fourth paragraph of this letter, under existing laws, regulations, rulings and judicial decisions, interest on the Notes (including any original issue discount properly allocable to the owners thereof) is excluded from gross income for federal income tax purposes and is not a special preference item for purposes of the federal alternative minimum tax imposed on individuals and corporations. Interest on the Notes, however, must be included in the "adjusted current earnings" of certain corporations (i.e., alternative minimum taxable income as adjusted for certain items, including those items that would be included in the calculation of a corporation's earnings and profits under Subchapter C of the Code) and such corporations are required to include in the calculation of alternative minimum taxable income 75% of the excess of each such corporation's adjusted current earnings (which includes tax-exempt interest) over its alternative minimum taxable income (determined without regard to this adjustment and prior to reduction for certain net operating losses).

The accrual or receipt of interest on the Notes may otherwise affect the federal income tax liability of the recipient. The extent of these other tax consequences will depend upon the recipient's particular tax status or other items of income or deduction. We express no opinion regarding any such consequences. Purchasers of the Notes, particularly purchasers that are corporations (including S corporations and foreign corporations operating branches in the United States), property or casualty insurance companies, banks, thrifts or other financial institutions or certain recipients of Social Security or Railroad Retirement benefits, taxpayers otherwise entitled to claim the earned income credit or taxpayers who may be deemed to have incurred (or continued) indebtedness to purchase or carry tax-exempt obligations are advised to consult their tax advisors as to the tax consequences of purchasing or holding the Notes.

4. The Notes are payable as to principal, premium, if any, and interest from and will secured by a pledge of and a first lien on the Pledged Receipts, as defined in the Indenture. The Notes do not pledge the general credit or taxing power, if any, of the Commonwealth, the Commission, the University, the Cabinet or any other agency or political subdivision of the Commonwealth.

5. The Notes are not secured by a pledge of or lien on the properties constituting the Project but are payable as to principal and interest solely and only from and are secured by the Pledged Receipts.

The ability of the University to make payments under the Lease is dependent upon legislative appropriations to the University, which has leased the Project for an initial term ending on the final maturity date of the Notes.

6. Under the existing laws of the Commonwealth of Kentucky, interest on the Notes is excluded from the gross income of the recipients thereof for Kentucky income tax purposes and the Notes are exempt from ad valorem taxation by the Commonwealth of Kentucky and all political subdivisions and taxing authorities thereof.

The obligations of the Commission, the University and the Cabinet, and the enforceability thereof, with respect to the Notes and the other documents described above are subject, in part, to the provisions of the bankruptcy laws of the United States of America and to other applicable bankruptcy, insolvency, reorganization, moratorium or similar laws relating to or affecting creditors' rights generally, now or hereafter in effect. Certain of such obligations, and enforcement thereof, are also subject to general equity principles, which may limit the specific enforcement of certain remedies but which do not affect the validity of such documents.

We express no opinion as to the title to, or the sufficiency in the Indenture or otherwise of the description of, the Project, or the priority of any liens, charges or encumbrances on the Project.

This letter is the "Confirming Opinion" as defined in our opinion dated October ___, 2006 (the "Preliminary Opinion") relating to the initial sale of the Notes, and is delivered in accordance with the Forward Delivery Note Purchase Contract described in the Preliminary Opinion.

Very truly yours,

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APPENDIX G

FORM OF BOND INSURANCE POLICIES

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Ambac

Financial Guaranty Insurance Policy

Ambac Assurance Corporation
One State Street Plaza, 15th Floor
New York, New York 10004
Telephone: (212) 668-0340

Obligor: Policy Number:

Obligations: Premium:

Ambac Assurance Corporation (Ambac), a Wisconsin stock insurance corporation, in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to The Bank of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of the Holders, that portion of the principal of and interest on the above-described obligations (the "Obligations") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor.

Ambac will make such payments to the Insurance Trustee within one (1) business day following written notification to Ambac of Nonpayment. Upon a Holder's presentation and surrender to the Insurance Trustee of such unpaid Obligations or related coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Holder the amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Obligations and/or coupons and shall be fully subrogated to all of the Holder's rights to payment thereon.

In cases where the Obligations are issued in registered form, the Insurance Trustee shall disburse principal to a Holder only upon presentation and surrender to the Insurance Trustee of the unpaid Obligation, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee duly executed by the Holder or such Holder's duly authorized representative, so as to permit ownership of such Obligation to be registered in the name of Ambac or its nominee. The Insurance Trustee shall disburse interest to a Holder of a registered Obligation only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Obligation and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee, duly executed by the Holder or such Holder's duly authorized representative, transferring to Ambac all rights under such Obligation to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all of the Holders' rights to payment on registered Obligations to the extent of any insurance disbursements so made.

In the event that a trustee or paying agent for the Obligations has notice that any payment of principal of or interest on an Obligation which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from the Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Holder will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Holder" means any person other than (i) the Obligor or (ii) any person whose obligations constitute the underlying security or source of payment for the Obligations who, at the time of Nonpayment, is the owner of an Obligation or of a coupon relating to an Obligation. As used herein, "Due for Payment", when referring to the principal of Obligations, is when the scheduled maturity date or mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity; and, when referring to interest on the Obligations, is when the scheduled date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Obligor to have provided sufficient funds to the trustee or paying agent for payment in full of all principal of and interest on the Obligations which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Obligations prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.

Robert J. Genader

President

AMBAC ASSURANCE CORPORATION CORPORATE SEAL WISCONSIN

Anne G. Gill

Secretary

Effective Date:

Authorized Representative

THE BANK OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.

Noraida Lauro

Authorized Officer of Insurance Trustee

Form No.: 2B-0012 (1/01)

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APPENDIX H

FORM OF DELIVERY CONTRACT

October __, 2006

Re: Commonwealth of Kentucky, Kentucky Asset/Liability Commission University of Kentucky General Receipts Project Notes, 2007 Series A (the "2007 A Notes")

Dear Ladies and Gentlemen:

The Purchaser designated below and executing this instrument (the "Purchaser") hereby agrees to purchase from the Underwriter for the initial offering of the 2007 A Notes, namely: Morgan Stanley & Co. Incorporated (the "Underwriter"), and the Underwriter agrees to sell to the Purchaser, $__________ in aggregate principal amount of the 2007 A Notes (the "Purchased 2007 A Notes") offered by the Kentucky Asset/Liability Commission's Preliminary Official Statement dated September 29, 2006 (the "Preliminary Official Statement") and the Official Statement dated October [10], 2006 (the "Official Statement"), receipt of copies of which is hereby acknowledged, at a purchase price of $__________ (plus accrued interest, if any, from the date of initial delivery of the 2007 A Notes) bearing the interest rates, amounts and maturity dates shown in the following table, and on the further terms and conditions set forth in this Delivery Contract:

Maturity Date	Par Amount	Coupon	CUSIP Number

Capitalized terms used and note otherwise defined in this Delivery Contract have the meanings set forth in the Official Statement.

The Purchaser hereby confirms that it has reviewed the Preliminary Official Statement and the Official Statement (including without limitation, the section entitled "CERTAIN FORWARD DELIVERY CONSIDERATIONS" therein), has considered the risks associated with purchasing the Purchased 2007 A Notes and is duly authorized to purchase the Purchased 2007 A Notes. The Purchaser further acknowledges and agrees that the Purchased 2007 A Notes are being sold on a "forward" basis, and the Purchaser hereby purchases and agrees to accept delivery of such Purchased 2007 A Notes from the Underwriter on or about November 1, 2007 (the "Settlement Date"), as and if they may be issued pursuant to the Forward Delivery Note Purchase Contract between the Kentucky Asset/Liability Commission (the "Commission") and the Underwriter (the "Forward Purchase Contract").

Payment for the Purchased 2007 A Notes which the Purchaser has agreed to purchase on the Settlement Date shall be made to the Underwriter or its order by wire transfer to a bank account specified by the Underwriter on the Settlement Date upon delivery to the Purchaser of the Purchased 2007 A Notes then to be purchased by the Purchaser through the book-entry system of The Depository Trust Company.

Upon issuance by the Commission of the 2007 A Notes and the purchase thereof by the Underwriter, the obligation of the Purchaser to take delivery of the Purchased 2007 A Notes hereunder shall be unconditional. The Underwriter may terminate the Forward Purchase Contract and its obligation to purchase the 2007 A Notes on the Settlement Date for re-sale to the Purchaser because of a Change in Law. A "Change in Law" is defined to mean:

(i) any change in or addition to applicable federal or state law, whether statutory or as interpreted by the courts, including any changes in or new rules, regulations, or other pronouncements or interpretations by federal or state agencies;

(ii) any legislation enacted by the Congress of the United States or introduced therein or recommended for passage by the President of the United States (if such enacted, introduced or recommended legislation has a proposed effective date which is on or before the Settlement Date);

(iii) any rule or regulation proposed or enacted by any governmental body, department, or agency (if such proposed or enacted rule or regulation has a proposed effective date which is on or before the Settlement Date); or

(iv) any judgment, ruling or order issued by any court or administrative body;

which in any such case, would:

(A) as to the Underwriter, legally prohibit (or have the retroactive effect of prohibiting, if enacted, adopted, passed or finalized) the Underwriter from

(1) accepting delivery of and paying for the 2007 A Notes in accordance with the provisions of the Forward Purchase Contract or

(2) selling the 2007 A Notes or beneficial ownership interests therein to bona fide purchasers; or

(B) as to the Commission,

(1) make the issuance, sale, or delivery of the 2007 A Notes illegal (or have the retroactive effect of making such issuance, sale, or delivery illegal, if enacted, adopted, passed, or finalized);

(2) eliminate the exclusion from gross income for federal or Kentucky income tax purposes of interest on the 2007 A Notes or otherwise adversely affect the tax treatment of ownership of the 2007 A Notes (or have any such effect retroactively if enacted, adopted, passed, or finalized); or

(3) require the 2007 A Notes to be registered under the Securities Act of 1933, as amended, or the Indenture or Resolution to be qualified under the Trust Indenture Act of 1939; or

(C) as to the University, diminish in any way the obligations of the University under the Financing Agreement as the Financing Agreement relates to the Notes;

provided, however, that such change in or addition to law, legislation, rule or regulation, or judgment, ruling, or order shall have become effective, been enacted, introduced, or recommended, or been proposed or been issued, as the case may be, subsequent to the date of the Forward Purchase Contract. IF A CHANGE OR ADDITION TO LAW, LEGISLATION, RULE OR REGULATION, OR JUDGMENT, RULING, OR ORDER INVOLVES THE ENACTMENT OF LEGISLATION WHICH ONLY DIMINISHES THE VALUE OF, AS OPPOSED TO ELIMINATING THE EXCLUSION FROM GROSS INCOME FOR FEDERAL INCOME TAX PURPOSES, INTEREST PAYABLE ON “STATE OR LOCAL BONDS,” THE COMMISSION MAY, NONETHELESS, BE ABLE TO SATISFY THE REQUIREMENTS FOR THE DELIVERY OF THE PURCHASED 2007 A NOTES. IN SUCH EVENT, THE PURCHASER WOULD BE REQUIRED TO ACCEPT DELIVERY OF THE PURCHASED 2007 A NOTES.

The Purchaser acknowledges and agrees that it will not be able to withdraw its order as described herein, and will not otherwise be excused from performance of its obligations to take up and pay for the Purchased 2007 A Notes on the Settlement Date because of market or credit changes, including specifically, but not limited to (a) changes in the ratings anticipated to be assigned to the 2007 A Notes or in the credit associated with the 2007 A Notes generally, or (b) changes in the financial condition, operations, performance, properties, or prospects of the Commission or the University from the date hereof to the Settlement Date of the 2007 A Notes (unless such changes give rise to an event of default under the financing documents). The Purchaser further acknowledges that the Underwriter could be liable under the Forward Purchase Contract for damages to the Commission in the event of a wrongful failure to accept delivery of the 2007 A Notes, and that the Underwriter has executed such Forward Purchase Contract in reliance on the Purchaser's commitment set forth herein. Finally, the Purchaser acknowledges and agrees that it will remain obligated to purchase the Purchased 2007 A Notes in accordance with the terms hereof even if the Purchaser decides to sell such Purchased 2007 A Notes following the date hereof.

The Purchaser represents and warrants that, as of the date of this Delivery Contract, the Purchaser is not prohibited from purchasing the Purchased 2007 A Notes hereby agreed to be purchased by it under the laws of the jurisdiction to which the Purchaser is subject.

This Delivery Contract will inure to the benefit of and be binding upon the parties hereto and their respective successors but will not be assignable by either party hereto without the written consent of the other.

This Delivery Contract may be executed by either of the parties hereto in any number of counterparts, each of which shall be deemed to be an original, but all such counterparts shall constitute one and the same instrument.

It is understood that the acceptance by the Underwriter of any Delivery Contract (including this one) is in the Underwriter's sole discretion and that, without limiting the foregoing, acceptances of such contracts need not be on a first-come, first-served basis. If this Delivery Contract is acceptable to the Underwriter, the Underwriter is asked to execute the form of acceptance below and mail or deliver one of the counterparts hereof to the Purchaser at its address set forth below. This will become a binding contract between the Underwriter and the Purchaser when such executed counterpart is so mailed or delivered by the Underwriter. This Delivery Contract does not constitute a customer confirmation pursuant to Rule G-15 of the Municipal Securities Rulemaking Board.

This Delivery Contract shall be construed and administered under the laws of the State of New York. The Commission is not a party to this Delivery Contract.

____
as Purchaser

By: _____________________________________
(Signature)

Name:___________________________________
Title: ____________________________________
Address: ____________________________
____
____

Accepted: October __, 2006

MORGAN STANLEY & CO. INCORPORATED

By: _____________________________________
Name: __________________________________
Title: ___________________________________
As Underwriter

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COMMONWEALTH OF KENTUCKY • KENTUCKY ASSET/LIABILITY COMMISSION • UNIVERSITY OF KENTUCKY GENERAL RECEIPTS PROJECT NOTES

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