

MINUTES OF THE FINANCE COMMITTEE
University of Kentucky Board of Trustees
December 7, 2010, 11:15 AM
18th Floor Patterson Office Tower, Board Room

Committee Members Present

Jim Stuckert, Chairperson, Jo Hern Curris, Keith Gannon, Bill Gatton, Terry Mobley, and Frank Shoop

Approval of Minutes

The minutes of the October 12, 2010 Finance Committee meeting were approved as presented.

FCR 1, (Consent)

Jim Stuckert, Chairperson, acknowledged a gift of \$451,500 from the Gary M. Browning estate, and a pledge of \$2,048,500 for a total of \$2.5 million to create and endow the Gary M. Browning M.D. Quasi-Endowed Scholarship and Student Support Fund in the College of Medicine. Mr. Stuckert acknowledged Mr. Browning's generous support.

FCR 2, Acceptance of Interim Financial Report for the University of Kentucky for the Three Months Ended September 30, 2010

Jim Stuckert presented the University's consolidated financial report for the three months ended September 30, 2010. As of September 30, the University had recognized \$662,962,701 of current funds revenue representing 27 percent of the 2010-11 approved budget of \$2,469,115,200. Operating expenditures totaled \$619,898,343 or 25 percent of the approved budget. Frank Shoop moved for approval. Terry Mobley seconded, and the motion for approval unanimously carried.

FCR 3, 2010-11 Budget Revisions

Angie Martin, Vice President for Financial Operations and Treasurer, presented the 2010-11 Budget Revisions and stated that there was an increase of the University's total budget by \$31.2 million, a 1.3 percent increase from \$2,469,115,200 to \$2,500,327,000. Jo Curris moved for approval. Bill Gatton seconded, and the motion for approval unanimously carried.

FCR 4, Approval of Investment in Coldstream Laboratories, Inc

Mr. Larry Kranking, CEO of Coldstream Laboratories, Inc. (CLI) requested approval for transfer of \$5.5 million from the University of Kentucky Research Foundation to be used for investment to Coldstream Laboratories, Inc. to fund operations, the development of new product lines, and working capital. Mr. Kranking presented a plan for making CLI more self-sustaining in the years ahead.

After the presentation Chairman Stuckert asked if anyone from the committee had any questions of Mr. Kranking.

Jo Curris welcomed Mr. Kranking and said it was her understanding the intent was always to take this company on-line and then sell it in the future. She asked if this was still the plan.

Mr. Kranking replied that he hoped to make this company so valuable that “if you have that conversation about whether to sell it that it would be a very, very tough decision for the University. I believe the value will be such that you could fund a lot of programs with CLI. I’m going to make it difficult for you to have that conversation.”

Mrs. Curris also asked if CLI anticipated coming back to the board for more than the \$5.5 million that is being requested today.

Mr. Kranking responded that he hoped they would not, but that he could not predict the economy or what was going to happen out in the world. “Everything being equal right now and looking forward the answer is no, looking at the controls we put in place we don’t buy anything unless it’s strategic, we don’t hire unless it’s strategic, it has to be driving our business, and with that whole philosophy I honestly believe we should have enough, but again I can’t predict the future. Right now the answer is no, I don’t have any intention of coming back (to the board).”

Committee member, Keith Gannon, stated that he was very impressed with Mr. Kranking’s energy and vision, and he wished he had had prior information to this notification as he didn’t know much about CLI. “I wish I could have had more background about your thoughts on the plan for the next six months. I would suspect you have some real intangible plans beyond that and I would like to see that plan.”

Mr. Kranking stated “it’s sensitive, the contracts that I have with the customers are such of a proprietary nature I can’t give out a lot of information. I’d be glad, if we can work out something, to share my vision and strategic objective, they are short term and long term and we’re putting in place some very tangible goals. I’m holding people accountable, that’s all on our strategic plan and I’d be glad to share but I’ll have to somehow figure out how to do that so we maintain confidentiality.”

Dr. Lee T. Todd, Jr. said that it would be helpful if Mr. Kranking mentioned that \$1.3 million is for future product development. “It may help Keith (Gannon) understand where some of this money is going. Also how does this break out the \$5.5 million into the three categories of your plan?”

Mr. Kranking responded that CLI had some previous debt that he had inherited that he wants to get rid of and move forward. He said, “We have some operating capital that is required and then we’ll look at new products.”

Dr. Todd noted that CLI was asking for some of the money for investment for future revenues. Mr. Kranking responded that “we’re looking for companies that we can compete with in the \$50-60 million in generic. There’s a very nice turn-around. It does take six to nine months to create the proof of concept and file with the FDA. This takes 24-25 months for approval. Then once you have FDA approval you can start the manufacturing of the product. That’s your revenue. Then the company will be self-sustaining.”

Dr. Todd noted that one thing that impressed him with Larry's background was that he's aware of drugs that are coming off of patent, and becoming available to be made generic. "If you're selective you can choose the ones with complexities to them so not everyone can manufacturing them or they're of such a volume not everyone is willing to do that. That's an addition to the business plan that wasn't there previously. We were just manufacturing for other people. This is a strategy and that's what \$1.4 million is for so we can take on some of these drugs that are coming off patent and do them ourselves. When the consultants were here that was one of their concerns. Fortunately, Larry was known by these consultants and came on board and brought that concept. When you are talking about selling, it's always nice to have a broad portfolio. The other \$2 million is for back-up."

Bill Gatton asked if we could assume this doubling in sales and increase in profit margin is going to come without additional investments and is it going to make CLI in the black or at least close to it. "What are your sales projections beyond that and how much investment are you going to have to have in facilities and equipment to go beyond that?"

Mr. Kranking stated "that hopefully CLI would be self-sustaining and break-even in the October timeframe. As we build and have retained earnings, something that we've not had before, then we should be able to start to fund the expansion. As we get to beyond the \$10 million we'll need to have more staff and different technologies. There will be equipment we need to buy and once we break even there will be a whole different business structure. There will be things that we can do to keep us self-sustaining without coming back to the board. There are things I can do, as a business guy, to generate and keep us self-sustaining and build more business."

Mr. Bill Gatton asked "in current operations, are you having to pay interest on what's been lost by previous investments or is that not something you have to face?"

Mr. Kranking responded by saying "I don't know what your expectations were, but to build a pharmaceutical company from scratch is six to seven years, typically its \$45-50 million dollars. I think we're on track. We'll start to fund our own expansions."

Dr. Todd stated that he thought Mr. Gatton's question was "are you paying interest on the money that you're living off of and invested by the medical center."

Mr. Kranking stated "that he didn't think so as it was not a loan. The investment in CLI from the medical center has been treated as an investment. We are not paying interest on the investments. There is a fair amount of debt finance in the organization from third parties and CLI has paid interest on that debt."

Mr. Stuckert asked Mr. Kranking if he had the talent to take this entity forward, and Mr. Kranking said he did.

Mr. Gatton said, "if we were making money, we would be paying taxes. Does it have a tax loss carry forward, and how soon does that burn off, and can you carry it forward for five years or something?"

Several board members were uncomfortable with approving this FCR without seeing more details such as CLI's financial statement, and it was suggested that in the future that CLI have a prepared financial statement for the board members to review, and if necessary to work with legal counsel to receive proprietary information.

Frank Shoop noted that a lot has already been invested, and this is a very insignificant amount and if this has a chance to work he was all for it.

Frank Shoop moved for approval. Terry Mobley seconded, and the motion for approval unanimously carried

FCR 5 – Authorization to Lease Four Acres to the Kentucky Medical Services Foundation on Which to Construct a Child Care Facility

Frank Butler, Executive Vice President for Finance and Administration, requested that the Board authorize him to negotiate and execute a lease with the Kentucky Medical Services Foundation (KMSF) for approximately four acres south of Alumni Drive on the University's south campus to construct a Child Care Facility. The center will be a 22,000 gross square foot facility to house a Child Care Development Center (CDC) providing child care services for children from the community, as well as children of faculty and staff. The University and KMSF have agreed to a fifty year lease for the designated property for the sum of \$1 a year. Construction plans are subject to advance review by the University. All costs associated with construction are to be paid by KMSF, CDC of the Bluegrass, and other private funds. In addition, all maintenance responsibilities during the term of the lease will be the responsibility of KMSF and CDC of the Bluegrass, and should the center fail the land lease reverts back to the University. Terry Mobley moved for approval. Frank Shoop seconded, and the motion for approval unanimously carried.

FCR 6 – Approval of the 2009-10 Endowment Match Program Annual Report

Jim Stuckert requested that Board accept the 2009-10 Endowment Match Program Annual Report. The Research Challenge Trust Fund (RCTF) was established in 1997 with the passage of the Kentucky Postsecondary Education Improvement Act (House Bill 1). The RCTF is designed to encourage research activities at the University of Kentucky and the University of Louisville. The Endowment Match Program, also known as 'Bucks for Brains', is one of several programs created as part of the RCTF. Terry Mobley noted that he would like to approve the motion as "he knows how much effort has gone into this since 1997 It was wonderfully done." Terry Mobley moved for approval. Jo Curriss seconded, and the motion for approval unanimously carried.

FCR 7 – Capital Construction Report

Bob Wiseman, Vice President for Facilities Management, presented the capital construction report for the three months ending September 30, 2010. There was one new contract, one contract was completed, and 35 change orders. In reference to the change order for the replacement of the Wildcat Lodge, Jo Curriss asked that with the change in the name of Wildcat Lodge, what other facility have we chosen to carry forward the name of Joe B. Hall. Frank Butler responded by saying that we have a building naming committee that will take that up, and because of the lodge building timeframe being 2012 there will be time. Mrs. Curriss asked if there had been any decision on how the old lodge building would be used. Mrs. Curriss said she would like to see proposals on what the

use of the building would be “as there were many of us who absolutely agreed to take a stand in making and agreeing to the new building and the change of the name so I think we have a definite interest in knowing what the utilization is going to be prior to it being determined.” Jo Curris moved for approval. Terry Mobley seconded, and the motion for approval unanimously carried.

Other Business

Next Meeting

Tuesday, February 22, 2011, 11:15 AM, 18th Floor Patterson Office Tower Board Room

Respectfully submitted,

Barbara Royalty-Tatum

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