



**STATE UNIVERSITY OF IOWA,
UNIVERSITY OF IOWA HOSPITALS AND CLINICS**

Financial Statements

June 30, 2010 and 2009

(With Independent Auditors' Report Thereon)



KPMG LLP
2500 Ruan Center
666 Grand Avenue
Des Moines, IA 50309

Independent Auditors' Report

The Board of Regents
State of Iowa:

We have audited the accompanying balance sheets of the State University of Iowa, University of Iowa Hospitals and Clinics (UIHC) as of June 30, 2010 and 2009, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of UIHC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of UIHC's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 1 to the financial statements, the financial statements of UIHC are intended to present the financial position and the changes in financial position and cash flows of only that portion of the business-type activities of the State University of Iowa that is attributable to the transactions of UIHC. UIHC is a department of the State University of Iowa for financial reporting purposes. The financial statements of UIHC do not purport to, and do not, present fairly the financial position of the State University of Iowa as of June 30, 2010 and 2009, and the changes in its financial position and its cash flows, for the years then ended, in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State University of Iowa, University of Iowa Hospitals and Clinics as of June 30, 2010 and 2009, and the changes in its net assets and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

The accompanying management's discussion and analysis on pages 3 through 7 is not a required part of the basic financial statements of UIHC, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

Des Moines, Iowa
December 6, 2010

**STATE UNIVERSITY OF IOWA,
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Management's Discussion and Analysis

June 30, 2010 and 2009

Introduction

This section of the State University of Iowa, University of Iowa Hospitals and Clinics' (UIHC) annual financial report presents management's discussion and analysis of UIHC's financial performance during the years ended June 30, 2010 and 2009. The purpose is to provide an objective analysis of the financial activities of UIHC based on currently known facts, decisions, and conditions. Please read it in conjunction with UIHC's financial statements and the accompanying notes to the financial statements.

Financial Highlights

The University of Iowa Hospitals and Clinics demonstrated financial success in 2010, with an increase in net assets of \$52.5 million or 5.4% as compared to a decrease in net assets in 2009 by \$11.2 million or 1.1%. Operating income in 2010 was \$26.1 million, an increase of \$34.9 million when compared to 2009. Nonoperating revenues and expenses increased \$32.3 million, primarily due to investment income of \$28.6 million versus \$3.3 million in 2009.

Overview of the Financial Statements

This annual report consists of two parts – management's discussion and analysis and the basic financial statements.

The financial statements consist of three statements – a balance sheet; a statement of revenues, expenses, and changes in net assets; and statement of cash flows. These financial statements and related notes provide information about the activities of UIHC and have been prepared on an accrual basis in accordance with Governmental Accounting Standards Board (GASB) accounting principles.

Balance Sheet and Statement of Revenues, Expenses, and Changes in Net Assets

In 2010, net assets increased by \$52.5 million or more than 5.4% to \$1,021 million. This is primarily due to net income from operations of \$26.1 million and investment income of \$28.6 million.

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Table 1 provides a summary of UIHC's assets, liabilities and net assets as of June 30, 2010, 2009, and 2008.

Table 1
UNIVERSITY OF IOWA HOSPITALS AND CLINICS
Condensed Balance Sheet Information

(In thousands)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Assets:			
Current assets	\$ 275,824	243,815	237,131
Noncurrent cash and investments	494,312	440,088	431,925
Capital assets, net	506,927	528,100	508,652
Other assets	2,736	2,915	2,122
Total assets	<u>\$ 1,279,799</u>	<u>1,214,918</u>	<u>1,179,830</u>
Liabilities:			
Current liabilities	\$ 109,289	114,326	102,304
Long-term debt	114,165	105,807	76,230
Other long-term liabilities	35,249	26,201	21,540
Total liabilities	<u>258,703</u>	<u>246,334</u>	<u>200,074</u>
Net assets:			
Invested in capital assets, net of related debt	398,505	427,073	436,169
Restricted	16,130	13,334	13,292
Unrestricted	606,461	528,177	530,295
Total net assets	<u>1,021,096</u>	<u>968,584</u>	<u>979,756</u>
Total liabilities and net assets	<u>\$ 1,279,799</u>	<u>1,214,918</u>	<u>1,179,830</u>

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Table 2 shows the changes in net assets for 2010 compared to 2009 and 2008.

Table 2

UNIVERSITY OF IOWA HOSPITALS AND CLINICS

Condensed Revenues, Expenses, and Changes in Net Assets Information

(In thousands)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Operating revenues:			
Net patient service revenue	\$ 899,706	883,417	826,362
Other revenue	43,752	44,777	44,810
Total operating revenues	<u>943,458</u>	<u>928,194</u>	<u>871,172</u>
Operating expenses:			
Salaries and benefits	465,583	494,519	451,927
Medical supplies and drugs	184,974	185,665	172,265
Other supplies and general expenses	191,999	183,795	160,032
Depreciation and amortization	74,812	72,975	68,140
Total operating expenses	<u>917,368</u>	<u>936,954</u>	<u>852,364</u>
Operating income (loss)	<u>26,090</u>	<u>(8,760)</u>	<u>18,808</u>
Nonoperating revenues (expenses):			
Loss on disposal of capital assets	(966)	(6,312)	(1,341)
Noncapital grants and contributions	5,670	3,189	1,942
Investment income	28,608	3,315	13,753
Interest expense	(4,207)	(3,392)	(1,440)
Total nonoperating revenues, (expenses) net	<u>29,105</u>	<u>(3,200)</u>	<u>12,914</u>
Excess of revenues over expenses before transfers	55,195	(11,960)	31,722
Net transfers (out) in	<u>(2,683)</u>	<u>788</u>	<u>(145)</u>
Increase (decrease) in net assets	52,512	(11,172)	31,577
Net assets, beginning of year	<u>968,584</u>	<u>979,756</u>	<u>948,179</u>
Net assets, end of year	<u>\$ 1,021,096</u>	<u>968,584</u>	<u>979,756</u>

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Net Patient Service Revenue

Net patient service revenue increased from 2009 to 2010 by \$16.3 million or 1.8% and \$57.1 million or 6.9% from 2008 to 2009. The increases in net patient service revenue were driven by both increases in patient volumes and pricing increases during the same periods. The increase in 2010 is primarily due to an increase in outpatient clinic visits from 2009 to 2010 by 11,511 or 1.6% and increase in outpatient surgeries of 1,129 or 8.6%. During 2009, acute admissions increased 193 or 0.7% from 29,349 to 29,542 admissions.

The provision for bad debts (a deduction from gross patient charges) decreased \$4.5 million from \$27.5 million in 2009 to \$23.0 million in 2010 due to a decrease in self-pay patient volumes. Self-pay admissions decreased 17% from prior year and self-pay clinic visits decreased 11% from prior year. The provision for bad debts decreased \$1.9 million from \$29.4 million in 2008 to \$27.5 million in 2009.

Operating Expenses

Total operating expenses decreased 2.1% from \$937.0 million in 2009 to \$917.4 million in 2010. The largest decrease in expenses in 2010 is attributable to salaries and benefits, which decreased \$28.9 million and 5.9% when compared to 2009. Total paid full time equivalents (FTE's) decreased by 474 or 7.1% from 6,685 in 2009 to 6,211 in 2010. In addition, during 2010, UIHC recorded a reduction to benefit expense in the amount of \$8.0 million related to medical resident FICA refund claims for periods ending before April 1, 2005 due to notification from the IRS of its intent to honor these claims. Medical supplies and drugs expense decreased \$0.7 million when compared to 2009. This is primarily due to a cost saving initiative to reduce expenses. Total operating expenses increased 9.9% from \$852.4 million in 2008 to \$937.0 million in 2009. The largest increases in expenses during these years are attributed to salaries and benefits, medical supplies and drugs, and depreciation.

Nonoperating Revenues and Expenses

Nonoperating revenues consist primarily of loss on disposals of capital assets, investment income, interest expense and noncapital grants and contributions. Investment income increased from 2009 to 2010 by \$25.3 million or 762.9% and investment income decreased from 2008 to 2009 by \$10.4 million or 75.9%. During 2010, UIHC recorded overall earnings on the endowment and operating pools of \$4.7 million and a net unrealized gain on investments of \$20.0 million, which increased investment income accordingly. This compares to the overall earnings on the endowment and operating pools of \$6.9 million and a net unrealized loss of \$3.6 million in the previous year. In addition, during 2010, UIHC recorded an interest accrual in the amount of \$3.9 million related to medical resident FICA refund claims for periods ending before April 1, 2005 due to notification from the IRS of their intent to honor these claims.

Statement of Cash Flows

The statement of cash flows reports cash receipts, cash payments and net changes in cash resulting from operations, investing and financing activities. UIHC's overall liquidity increased during the year, with a net increase in cash and cash equivalents of \$236,589. In 2010, net cash from operating and non-capital financing activities provided cash inflows of \$94.9 million and \$3.0 million, respectively. UIHC was able to purchase capital assets, investments and pay down long term debt with the net cash inflows mentioned above.

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Capital Assets and Debt Administration

Capital Assets

At the end of 2010, UIHC had \$506.9 million invested in capital assets, net of accumulated depreciation. This is a \$21.2 million dollar decrease when compared to capital assets, net in 2009 of \$528.1 million. This is primarily due to assets depreciating faster than capital assets were purchased.

During 2010 and 2009, UIHC constructed or purchased \$55.5 million and \$98.8 million, respectively, of capital assets. The major capital asset additions in 2010 included:

- Institute for Clinical and Translational Science Facilities Development
- Sports Medicine Center
- Emergency Treatment Center Expansion and Renovation
- PIC Unit Expansion
- Medical Psych Inpatient Unit Relocation
- Additional major equipment additions in 2010 consisted of a Magnetom Avanto MRI for the Sports Medicine Center, a SOMATOM Definition Dual Source CT Scanner, a Single Axiom Artis DFC Single Plane Fluoroscopy, and a DataCaptor Software license to be used with EPIC

Debt

At June 30, 2010 and 2009, UIHC had \$118.6 and \$110.3 million, respectively, in revenue bonds and capital lease obligations outstanding. During 2010, reductions of long-term debt were \$4.6 million. In comparison, during 2009, reductions of long-term debt were \$6.7 million, which included refinancing the \$4.2 million balance of the Series S.U.I. 2000 Telecommunications Facilities Revenue Bonds. During 2010, UIHC issued \$12.8 million of Series S.U.I. 2009 Telecommunications Facilities Revenue Bonds, the proceeds of which will be used to defray costs of constructing, equipping and installing a new data center to support redundant operations of the Telecommunications System of the University.

In October 2010, UIHC issued \$30.0 million of Series S.U.I. 2010 Hospital Revenue Bonds. The proceeds of the Bonds will be used by the UIHC for the costs of constructing, improving, remodeling, repairing, furnishing, and equipping inpatient and outpatient care facilities, including construction of a new medical office building and related space, including finish materials, fixtures, furnishings, equipment, and appliances, funding a deposit to the Reserve Fund, and paying the costs of issuance of the Bonds.

Contacting UIHC's Financial Management

This financial report provides the citizens of Iowa, our patients, bondholders, and creditors with a general overview of UIHC's finances and operations. If you have questions about this report, please contact Mr. Kenneth L. Fisher, Associate Vice President for Finance, UI Healthcare and CFO, University of Iowa Hospitals and Clinics, 300 CMAB, Iowa City, Iowa 52242.

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Balance Sheets

June 30, 2010 and 2009

Assets	2010	2009
Current assets:		
Cash and cash equivalents	\$ 974,014	737,425
Short-term investments	103,393,534	81,841,579
Patient accounts receivable, net of estimated uncollectibles \$20,629,913 in 2010 and \$21,360,139 in 2009	129,962,178	130,912,741
Inventories	19,983,647	20,573,605
Current portion of debt service funds	1,212,829	1,030,729
Other current assets	20,297,833	8,719,327
Total current assets	<u>275,824,035</u>	<u>243,815,406</u>
Noncurrent cash and investments:		
Designated by the Board of Regents	469,203,243	418,475,325
Held by trustee for debt service	10,190,835	9,309,934
Restricted by contributors and grantors for capital acquisitions and research	14,917,379	12,302,640
	<u>494,311,457</u>	<u>440,087,899</u>
Capital assets, net	506,927,469	528,100,503
Other assets	2,735,983	2,914,408
Total assets	<u>\$ 1,279,798,944</u>	<u>1,214,918,216</u>
Liabilities and Net Assets		
Current liabilities:		
Current maturities of long-term debt and capital lease obligation	\$ 4,448,626	4,530,288
Accounts payable and accrued expenses	79,642,106	82,175,782
Estimated third-party payor settlements	9,394,009	17,992,560
Due to related parties	8,373,892	3,575,699
Other current liabilities	5,407,446	3,915,491
Accrued interest	2,022,472	2,136,585
Total current liabilities	<u>109,288,551</u>	<u>114,326,405</u>
Long-term debt and capital lease obligation, net of current maturities	114,165,082	105,807,174
Other long-term liabilities	35,249,333	26,201,132
Total liabilities	<u>258,702,966</u>	<u>246,334,711</u>
Net assets:		
Invested in capital assets, net of related debt	398,504,596	427,072,975
Restricted by donors for specific purposes	14,917,379	12,302,640
Restricted for debt service	1,212,829	1,030,729
Unrestricted	606,461,174	528,177,161
Total net assets	<u>1,021,095,978</u>	<u>968,583,505</u>
Total liabilities and net assets	<u>\$ 1,279,798,944</u>	<u>1,214,918,216</u>

See accompanying notes to financial statements.

**STATE UNIVERSITY OF IOWA,
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Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Operating revenues:		
Net patient service revenue, net of provision for bad debts of \$22,964,009 in 2010 and \$27,512,826 in 2009	\$ 899,705,992	883,416,576
Other revenue	43,751,997	44,776,895
Total operating revenues	<u>943,457,989</u>	<u>928,193,471</u>
Operating expenses:		
Salaries and benefits	465,583,057	494,401,447
Medical supplies and drugs	184,973,830	185,666,247
Other supplies and general expenses	191,999,323	183,911,252
Depreciation and amortization	74,811,680	72,974,749
Total operating expenses	<u>917,367,890</u>	<u>936,953,695</u>
Operating income (loss)	<u>26,090,099</u>	<u>(8,760,224)</u>
Nonoperating revenues (expenses):		
Loss on disposal of capital assets	(966,206)	(6,311,918)
Noncapital grants and contributions	5,670,492	3,189,117
Investment income	28,607,579	3,315,242
Interest expense	(4,206,657)	(3,392,141)
Total nonoperating revenues (expenses), net	<u>29,105,208</u>	<u>(3,199,700)</u>
Excess (deficiency) of revenues over expenses before transfers	55,195,307	(11,959,924)
Net transfers (out) in	<u>(2,682,834)</u>	<u>788,034</u>
Increase (decrease) in net assets	52,512,473	(11,171,890)
Net assets, beginning of year	<u>968,583,505</u>	<u>979,755,395</u>
Net assets, end of year	<u>\$ 1,021,095,978</u>	<u>968,583,505</u>

See accompanying notes to financial statements.

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Statements of Cash Flows

Years ended June 30, 2010 and 2009

	2010	2009
Cash flows from operating activities:		
Receipts from and on behalf of patients	\$ 892,058,004	875,938,623
Receipts from state grants	—	6,839,740
Other receipts and payments, net	48,550,189	45,039,308
Payments to employees	(456,172,383)	(465,626,937)
Payment to suppliers and contractors	(389,541,780)	(389,531,843)
	<u>94,894,030</u>	<u>72,658,891</u>
Net cash provided by operating activities		
Cash flows from noncapital financing activities:		
Net transfers	(2,682,834)	788,034
Noncapital grants and contributions	5,670,492	3,189,117
	<u>2,987,658</u>	<u>3,977,151</u>
Net cash provided by noncapital financing activities		
Cash flows from capital and related financing activities:		
Purchase of capital assets	(55,531,592)	(98,797,627)
Proceeds from the sale of capital assets	2,065,159	105,441
Proceeds from the issuance of long-term debt	12,825,000	37,235,145
Premium received on issuance of long-term debt	75,910	621,931
Principal paid on long-term debt	(4,529,993)	(6,674,877)
Interest paid on long-term debt	(4,415,441)	(2,546,459)
	<u>(49,510,957)</u>	<u>(70,056,446)</u>
Net cash used in capital and related financing activities		
Cash flows from investing activities:		
Proceeds from sale of investments	89,904,407	86,602,925
Purchase of investments	(147,163,343)	(101,023,405)
Interest and dividends received on investments	9,124,794	7,968,112
	<u>(48,134,142)</u>	<u>(6,452,368)</u>
Net cash used in investing activities		
Net increase in cash and cash equivalents	236,589	127,228
Cash and cash equivalents at beginning of year	737,425	610,197
Cash and cash equivalents at end of year	<u>\$ 974,014</u>	<u>737,425</u>
Reconciliation of operating income (loss) to net cash provided by operating activities:		
Operating income (loss)	\$ 26,090,099	(8,760,224)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation and amortization	74,811,680	72,974,749
Provision for bad debts	22,964,009	27,512,826
Change in assets and liabilities:		
Accounts receivable	(22,013,446)	(41,491,919)
Inventories	589,958	(130,165)
Other assets	(11,754,392)	2,923,856
Accounts payable and accrued expenses	(2,533,676)	3,347,895
Other liabilities	10,540,156	2,678,580
Due to related parties	4,798,193	5,714,859
Estimated third-party payor settlements	(8,598,551)	7,888,434
	<u>94,894,030</u>	<u>72,658,891</u>
Net cash provided by operating activities	<u>\$ 94,894,030</u>	<u>72,658,891</u>

Noncash investing activities:

UIHC held cash and investments at June 30, 2010 and 2009 with a fair value of \$598,679,004 and \$524,058,599, respectively. During 2010 and 2009, the net (decrease) increase in fair value of these investments was \$20,061,849 and (\$3,589,643), respectively.

See accompanying notes to financial statements.

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Notes to Financial Statements

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(1) Summary of Significant Accounting Policies and Related Matters

(a) Reporting Entity

For purposes of this report, the State University of Iowa, University of Iowa Hospitals and Clinics (UIHC) includes the healthcare units of the University of Iowa, which are generally referred to as the University Hospital, the Psychiatric Hospital, and the Center for Disabilities and Development. UIHC is part of the State University of Iowa (the University), which is owned and operated by the State of Iowa under the supervision of the Board of Regents, State of Iowa (the Board) and is a University department for financial reporting purposes.

UIHC includes substantially all of the healthcare provider activities for patient care associated with the University other than the physician and dentist services and research activities provided by the faculties of the University's Colleges of Medicine and Dentistry. Student Health Services, Specialized Child Health Services outreach programs, and the University of Iowa Health System, a UIHC affiliate, are not included in these financial statements.

UIHC is a comprehensive tertiary care referral center located in Iowa City, Iowa, offering a full range of clinical services in substantially all specialties and subspecialties of medicine and dentistry. UIHC serves as a resource for the state's primary and secondary healthcare providers. Patients are primarily from Iowa.

(b) Basis of Presentation

UIHC uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, UIHC has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, provided that such pronouncements do not conflict or contradict GASB pronouncements. UIHC has elected not to apply all FASB Statements and Interpretations issued after November 30, 1989.

(c) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(d) Cash and Investments

Cash and investments of UIHC include specific investments and other cash and investments that are pooled with the cash and investments of the University and held in the name of the University.

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UIHC's share of pooled investments and income thereon are determined on a pro rata basis reflecting UIHC's amounts available for investment as compared with the amounts for the overall University.

Undesignated cash equivalents totaling \$974,014 and \$737,425 at June 30, 2010 and 2009, respectively, represent money market funds and other short-term investments that mature in three months or less from date of purchase.

(e) Inventories

Inventories consist primarily of medical and surgical, pharmaceutical, dietary, and other supplies. Inventories are stated at the lower of cost or market, with cost determined on the first-in, first-out or weighted average basis.

(f) Capital Assets

UIHC's capital assets are reported at historical cost. Contributed capital assets are reported at their estimated fair value at the time of their donation. All capital assets other than land are depreciated or amortized (in the case of capital leases) using the straight-line method of depreciation using the following asset lives:

Buildings and leasehold improvements	10 to 40 years
Infrastructure and land improvements	5 to 20 years
Equipment and software	3 to 10 years

(g) Costs of Borrowing

Except for capital assets acquired through gifts, contributions, or capital grants, interest cost on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

(h) Grants and Contributions

From time to time, UIHC receives grants, as well as contributions from individuals and private organizations. Grants and contributions may be restricted for either specific operating purposes or for capital purposes.

(i) Restricted Resources

When UIHC has both restricted and unrestricted resources available to finance a particular program, it is UIHC's policy to use restricted resources before unrestricted resources.

(j) Net Assets

Net assets of UIHC are classified in four components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. Net assets for donors for specific purposes are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to UIHC. Net assets restricted for debt

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service are amounts deposited with trustees as required by bond indentures. Unrestricted net assets are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

(k) *Operating Revenues and Expenses*

UIHC's statements of revenues, expenses, and changes in net assets distinguish between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing healthcare services – UIHC's principal activity. Nonexchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide healthcare services, other than financing costs.

(l) *Net Patient Service Revenue*

UIHC has agreements with third-party payors that provide for payments to UIHC at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for service rendered, including estimated retroactive adjustments under reimbursement agreements 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.

(m) *Charity Care*

UIHC provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because UIHC does not pursue collection of amounts once determined to qualify as charity care, they are not reported as revenues in the accompanying statements of revenues, expenses, and changes in net assets.

(n) *Compensated Absences*

UIHC employees accumulate vacation and sick leave under the provisions of the Code of Iowa. Under the State's policy, accrued vacation benefits are paid at an employee's regular hourly rate when used or are paid upon retirement, death, or termination with certain exceptions. Sick leave is paid in a similar manner when used or to a maximum of \$2,000 upon retirement. These benefits are accrued in the financial statements as earned by UIHC employees.

Retirement benefits are provided to employees primarily through a defined contribution retirement plan sponsored by the University. UIHC funds its obligation to the retirement plan on a current basis, as earned by its employees.

(o) *Income Taxes*

UIHC, as part of the University, is exempt from federal income taxes, pursuant to Section 115 of the Internal Revenue Code. As such, UIHC is subject to income taxes only on unrelated business income under the provisions of Section 511 of the Internal Revenue Code.

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(p) Reclassification of Prior Year Amounts

Certain reclassifications were made to the prior year financial statements to conform to the presentation of 2010.

(2) Deposits and Investments

In accordance with the Code of Iowa, investments may consist of obligations of the following: U.S. government and its agencies, certificates of deposit, prime bankers' acceptances, commercial paper, repurchase agreements, investments authorized by the Iowa Public Employees' Retirement System (IPERS) in Section 97B.7 of the Code of Iowa, an open-end management investment company organized in trust form registered with the Securities and Exchange Commission under the Investment Company Act of 1940, and the Common Fund for Nonprofit Corporations.

UIHC's cash and investments include specific investments and amounts pooled with cash and investments of the University and held in the University's name. UIHC's cash deposits at June 30, 2010 and 2009 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. Chapter 12C provides for additional assessments against the depositories of the pool to ensure that there will be no loss of public funds.

Noncurrent cash and investments limited by bond resolutions or designated by the Board were held for the following purposes at June 30, 2010 and 2009:

	2010	2009
Limited by bond resolutions:		
Debt service reserve	\$ 10,190,835	9,309,934
Designated by the Board of Regents:		
Capital projects and equipment and other needs	5,538,230	4,521,869
Surplus	465,995	2,746,601
Improvement, extension, repair, operation, and maintenance funds	463,199,018	411,206,855
Restricted by donors	14,917,379	12,302,640
	\$ 494,311,457	440,087,899

Funds for improvement, extension, repair, operation, and maintenance shall be used to pay costs of operating and maintaining the hospital system whenever other funds are not sufficient and for improvements, extensions, and repairs. Noncurrent cash and investments include designated assets set aside by the Board for future facility infrastructure improvements, equipment, and technological needs, over which UIHC retains control and may, at its discretion, subsequently authorize its use for other purposes. The funds are invested in investment-grade, long-term fixed income and in certain high-quality equities through the University's pooled investment funds.

Cash and cash equivalents and short-term investments specifically identified or pooled with the cash and investments of the University totaled \$104,367,548 and \$82,579,004 at June 30, 2010 and 2009,

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respectively. Cash equivalents designated by the Board totaled \$166,199,632 and \$181,995,849 at June 30, 2010 and 2009, respectively.

UIHC's investments are recorded at fair value, as determined by quoted market price. As of June 30, 2010, UIHC had the following investments and quality credit ratings:

	<u>Fair market value</u>	<u>Effective duration</u>	<u>Quality rating</u>
University of Iowa Long-Term Endowment Pool:			
Cash and cash equivalents	\$ 1,164,937	NA	NA
U.S. obligations	2,741,626	4.31	NA
Agency securities	1,195,795	2.40	NR
Corporate issuance	2,574,664	4.60	A+
Mortgage-backed securities	177,246	2.47	NR
Mutual funds – fixed income	10,088,640	3.83	BBB+
Mutual funds – U.S. equity	13,797,284	NA	NA
Mutual funds – international equity	12,022,906	NA	NA
Mutual funds – real estate	1,457,051	NA	NA
Subtotal	<u>45,220,149</u>		
University of Iowa Intermediate (Quasi II) Endowment Pool:			
Cash and cash equivalents	4,833,553	NA	NA
U.S. obligations	14,726,303	4.50	NA
Agency securities	6,704,564	2.39	NR
Corporate issuance	15,695,301	4.50	A+
Mortgage-backed securities	1,133,510	2.43	NR
Mutual funds – fixed income	23,035,865	3.80	A
Subtotal	<u>66,129,096</u>		
University of Iowa Operating Investment Pool:			
Cash and cash equivalents	264,254,664	NA	NA
U.S. obligations	8,820,980	1.91	NA
Agency securities	2,615,846	1.06	NR
Corporate issuance	35,875,389	1.84	AA
Mortgage-backed securities	10,602,744	(0.23)	NR
Mutual funds – fixed income	128,890,051	NA	NA
Mutual funds – U.S. equity	19,378,434	NA	NA
Mutual funds – international equity	5,016,481	NA	NA
Mutual funds – real estate	13,088,000	NA	NA
Subtotal	<u>488,542,589</u>		
Total investments	<u>\$ 599,891,834</u>		

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As of June 30, 2009, UIHC had the following investments and quality credit ratings:

	<u>Fair market value</u>	<u>Effective duration</u>	<u>Quality rating</u>
University of Iowa Long-Term Endowment Pool:			
Cash and cash equivalents	\$ 1,234,405	NA	NA
U.S. obligations	901,725	2.80	NA
Agency securities	79,312	5.80	NR
Corporate issuance	3,027,291	5.20	A
Mortgage-backed securities	182,639	4.15	NR
Mutual funds – fixed income	6,778,991	3.65	BBB+
Mutual funds – U.S. equity	11,970,503	NA	NA
Mutual funds – international equity	11,106,970	NA	NA
Mutual funds – real estate	1,677,431	NA	NA
Subtotal	<u>36,959,267</u>		
University of Iowa Intermediate (Quasi II) Endowment Pool:			
Cash and cash equivalents	7,400,171	NA	NA
U.S. obligations	5,407,258	2.80	NA
Agency securities	461,449	5.86	NR
Corporate issuance	20,981,751	5.20	A
Mortgage-backed securities	1,088,725	4.16	NR
Mutual funds – fixed income	25,963,016	4.16	A+
Subtotal	<u>61,302,370</u>		
University of Iowa Operating Investment Pool:			
Cash and cash equivalents	255,045,179	NA	NA
U.S. obligations	12,870,551	3.25	NA
Agency securities	27,806,904	1.71	NR
Corporate issuance	56,085,003	1.95	A+
Mortgage-backed securities	12,085,969	0.32	NR
Mutual funds – fixed income	10,428,147	1.30	AA
Mutual funds – fixed income	37,556,468	NA	NA
Mutual funds – U.S. equity	7,135,850	NA	NA
Mutual funds – international equity	1,874,720	NA	NA
Mutual funds – real estate	4,547,204	NA	NA
Subtotal	<u>425,435,995</u>		
Total investments	<u>\$ 523,697,632</u>		

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. This risk is measured using effective duration. The maximum duration of the

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University's unrestricted operating portfolio may not exceed the duration of the Merrill 1-3 year Government/Corporate Index by more than 20%. At time of purchase, the effective maturity of securities in the operating portfolio cannot exceed sixty-three months. There is no explicit limit on the average maturity of fixed income securities in the endowment portfolios. Each fixed income portfolio is managed to an appropriate benchmark.

Credit Risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation to the University. The University manages exposure to credit risk by measuring portfolios against benchmarks as established by the Board of Regents. As of June 30, 2010, the short-term bond portfolio benchmark is AAA (Merrill Lynch 1-3 Year Government/Corporate Index) and the long-term bond portfolio benchmark is AA1 (Barclays Capital Aggregate Bond Index).

Concentration of Credit Risk – Concentration of credit risk is the risk of loss attributed to the magnitude of investments in a single issuer. Except for Treasury or Agency debentures, pass-throughs or REMICs, no more than 5% of the operating and fixed income endowment portfolios are invested in securities of a single issuer.

Foreign Currency Risk – Foreign currency risk is the risk of an investment's value changing due to changes in currency exchange rates. The University's investment policy does not allow direct investment in foreign currencies. Also, no more than 30% of the long-term endowment portfolio can be invested in non-U.S. securities.

(3) Capital Assets

Capital assets at June 30, 2010 and 2009 are summarized as follows:

	<u>2010</u>	<u>2009</u>
Land improvements	\$ 782,080	782,080
Infrastructure	41,211,418	40,538,941
Buildings and leasehold improvements	724,424,339	693,912,097
Equipment	310,584,995	310,205,207
Software	71,169,942	69,649,103
Construction in progress (nondepreciable)	25,674,418	29,746,213
	<u>1,173,847,192</u>	<u>1,144,833,641</u>
Less accumulated depreciation	666,919,723	616,733,138
	<u>\$ 506,927,469</u>	<u>528,100,503</u>

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Capital asset additions, retirements, and balances for the years ended June 30, 2010 and 2009 were as follows:

<u>Cost basis summary</u>	<u>June 30, 2009 balances</u>	<u>Acquisitions</u>	<u>Sales retirements and transfers</u>	<u>June 30, 2010 balances</u>
Land improvements	\$ 782,080	—	—	782,080
Infrastructure	40,538,941	672,477	—	41,211,418
Buildings and leasehold improvements	693,912,097	30,512,242	—	724,424,339
Equipment and software	379,854,310	28,418,668	(26,518,041)	381,754,937
Construction in progress (nondepreciable)	29,746,213	(4,071,795)	—	25,674,418
Total at historical cost	<u>1,144,833,641</u>	<u>55,531,592</u>	<u>(26,518,041)</u>	<u>1,173,847,192</u>
	<u>June 30, 2009 balances</u>	<u>Depreciation expense</u>	<u>Sales retirements and transfers</u>	<u>June 30, 2010 balances</u>
Less accumulated depreciation for:				
Land improvements	736,740	2,814	—	739,554
Infrastructure	33,564,749	1,978,497	—	35,543,246
Buildings and leasehold improvements	381,956,077	29,896,978	—	411,853,055
Equipment and software	200,475,572	42,761,178	(24,452,882)	218,783,868
Total accumulated depreciation	<u>616,733,138</u>	<u>74,639,467</u>	<u>(24,452,882)</u>	<u>666,919,723</u>
Total capital assets, net	<u>\$ 528,100,503</u>	<u>(19,107,875)</u>	<u>(2,065,159)</u>	<u>506,927,469</u>

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Cost basis summary	June 30, 2008 balances	Acquisitions	Sales retirements and transfers	June 30, 2009 balances
Land improvements	\$ 741,775	40,305	—	782,080
Infrastructure	40,487,990	50,951	—	40,538,941
Buildings and leasehold improvements	638,562,709	55,349,388	—	693,912,097
Equipment and software	322,535,077	72,070,813	(14,751,580)	379,854,310
Construction in progress (nondepreciable)	63,211,532	(28,713,830)	(4,751,489)	29,746,213
Total at historical cost	<u>1,065,539,083</u>	<u>98,797,627</u>	<u>(19,503,069)</u>	<u>1,144,833,641</u>
	June 30, 2008 balances	Depreciation expense	Sales retirements and transfers	June 30, 2009 balances
Less accumulated depreciation for:				
Land improvements	733,927	2,813	—	736,740
Infrastructure	31,323,376	2,241,373	—	33,564,749
Buildings and leasehold improvements	352,720,468	29,235,609	—	381,956,077
Equipment and software	172,109,324	41,494,954	(13,128,706)	200,475,572
Total accumulated depreciation	<u>556,887,095</u>	<u>72,974,749</u>	<u>(13,128,706)</u>	<u>616,733,138</u>
Total capital assets, net	<u>\$ 508,651,988</u>	<u>25,822,878</u>	<u>(6,374,363)</u>	<u>528,100,503</u>

At June 30, 2010, construction in progress is related to various projects throughout the UIHC. The estimated cost to complete the current phase of equipment and projects under construction at June 30, 2010 is \$19.0 million. Other projects at June 30, 2010, with an estimated cost of \$305.0 million, have been committed to by the Board and/or UIHC; however, construction contracts had not been signed as of such date. These projects are anticipated to be funded through existing designated funds, cash provided by future operations, and/or the issuance of additional long-term debt.

Cost of capital assets includes interest during the construction period for qualifying projects. Interest costs capitalized for the years ended June 30, 2010 and 2009 were \$1,399,173 and \$977,141, respectively.

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(4) Long-Term Debt

Long-term debt outstanding at June 30, 2010 and 2009 was as follows:

	<u>2010</u>	<u>2009</u>
Hospital Revenue Bonds:		
Series 2002 – 4.125% to 5.000%; maturing serially on September 1 through 2028	\$ 21,260,000	21,950,000
Series S.U.I. 2007 – 4.375% to 5.500%; maturing serially on September 1 through 2027	23,550,000	24,375,000
Series S.U.I. 2007A – 4.000% to 5.500%; maturing serially on September 1 through 2027	23,425,000	24,225,000
Series S.U.I. 2009 – 5.500% to 6.125%; maturing serially on September 1 through 2028	32,450,000	33,750,000
Net unamortized premium on Hospital Revenue Bonds	983,323	1,002,084
Telecommunications Facilities Revenue Bonds:		
Series S.U.I. 2003 – 3.150% to 3.800%; maturing serially on July 1 through 2013	957,600	1,309,350
Series S.U.I. 2008 – 2.375% to 3.375%; maturing serially on July 1 through 2015	2,996,970	3,485,145
Series S.U.I. 2009 – 3.000% to 4.250%; maturing serially on July 1 through 2036	<u>12,825,000</u>	<u>—</u>
Total long-term debt	118,447,893	110,096,579
Capital lease obligations (net book value of \$146,297)	<u>165,815</u>	<u>240,883</u>
	118,613,708	110,337,462
Long-term debt, current portion	<u>4,448,626</u>	<u>4,530,288</u>
	<u>\$ 114,165,082</u>	<u>105,807,174</u>

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Activity in long-term debt for the years ended June 30, 2010 and 2009 was as follows:

	June 30, 2009 balance	Additions	Reductions	June 30, 2010 balance	Amounts due within one year
Hospital Revenue Bonds, Series 2002	\$ 21,950,000	—	(690,000)	21,260,000	725,000
Hospital Revenue Bonds, Series 2007	24,375,000	—	(825,000)	23,550,000	875,000
Hospital Revenue Bonds, Series 2007A	24,225,000	—	(800,000)	23,425,000	825,000
Hospital Revenue Bonds, Series 2009	33,750,000	—	(1,300,000)	32,450,000	1,075,000
Net unamortized bond premium	1,002,084	75,910	(94,671)	983,323	—
Telecommunications Facilities					
Revenue Bonds:					
Series, 2003	1,309,350	—	(351,750)	957,600	362,250
Series, 2008	3,485,145	—	(488,175)	2,996,970	509,400
Series, 2009	—	12,825,000	—	12,825,000	—
Total long-term debt	110,096,579	12,900,910	(4,549,596)	118,447,893	4,371,650
Capital lease obligations	240,883	—	(75,068)	165,815	76,976
	<u>\$ 110,337,462</u>	<u>12,900,910</u>	<u>(4,624,664)</u>	<u>118,613,708</u>	<u>4,448,626</u>

	June 30, 2008 balance	Additions	Reductions	June 30, 2009 balance	Amounts due within one year
Hospital Revenue Bonds, Series 2002	\$ 22,615,000	—	(665,000)	21,950,000	690,000
Hospital Revenue Bonds, Series 2007	25,000,000	—	(625,000)	24,375,000	825,000
Hospital Revenue Bonds, Series 2007A	25,000,000	—	(775,000)	24,225,000	800,000
Hospital Revenue Bonds, Series 2009	—	33,750,000	—	33,750,000	1,300,000
Net unamortized bond premium	415,962	621,931	(35,809)	1,002,084	—
Telecommunications Facilities					
Revenue Bonds:					
Series, 2000	4,194,060	—	(4,194,060)	—	—
Series, 2003	1,651,650	—	(342,300)	1,309,350	351,750
Series, 2008	—	3,485,145	—	3,485,145	488,175
Total long-term debt	78,876,672	37,857,076	(6,637,169)	110,096,579	4,454,925
Capital lease obligations	259,656	54,744	(73,517)	240,883	75,363
	<u>\$ 79,136,328</u>	<u>37,911,820</u>	<u>(6,710,686)</u>	<u>110,337,462</u>	<u>4,530,288</u>

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The Hospital Revenue Bonds are special obligations of the Board of Regents payable solely out of Hospital Income, the general purpose of which is to expand and improve UIHC facilities. "Hospital Income" is defined as the gross income and funds received by the Hospital System, including the proceeds of rates, fees, charges, and payments for healthcare provider activities for patient care services rendered by the University's hospitals, clinics, laboratories, and ancillary facilities after deduction of current expenses. Hospital Income does not include State appropriations to the University or Hospital System. So long as the bonds or parity bonds remain outstanding, the entire Hospital System income and revenues shall be deposited to the revenue fund and shall be disbursed to the following funds in the following order: (1) the operation and maintenance fund, (2) the sinking fund, (3) the reserve fund, and (4) the system fund. The reserve fund requirement is at least equal to the maximum annual amount of the principal and interest coming due on the bonds and any parity bonds, or \$8,652,219. The maximum amount of Hospital Income pledged representing the undiscounted principal and interest on the bonds is \$180,413,480.

The Telecommunications Facilities Revenue Bonds (Telecommunications Bonds) represent UIHC's share of the remaining outstanding bonds that were issued by the University to pay costs of constructing and installing communications facilities and equipment on the University's campus. No specific revenue stream of UIHC has been pledged to service the Telecommunications Bonds. Monthly payments are required to be made to various sinking funds for payment of principal and interest. A portion of the monthly payments is supported by UIHC. The Series 2000 Bonds were refinanced during 2009, with the resulting gain being insignificant to the financial statements.

Scheduled principal and interest payments on the bonds for the next five years and five-year increments thereafter are as follows:

	<u>Principal</u>	<u>Interest</u>
Year ending June 30:		
2011	\$ 4,371,650	5,589,565
2012	4,576,985	5,352,240
2013	4,848,280	5,146,258
2014	5,052,025	4,930,559
2015	5,154,350	4,701,383
2016 through 2020	26,451,515	19,779,907
2021 through 2025	32,820,510	12,717,489
2026 through 2030	29,138,770	3,942,465
2031 through 2035	3,429,405	719,276
2036 through 2037	1,621,080	69,768
	<u>\$ 117,464,570</u>	<u>62,948,910</u>

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Capital Lease Obligations

The following is a schedule by year of future minimum payments required:

Year ending June 30:			
2011	\$	89,998	
2012		58,130	
2013		29,561	
2014		11,205	
Total minimum payments required		188,894	
Less amounts representing interest		23,079	
	\$	165,815	

(5) Retirement Benefit Plans

Substantially all UIHC employees meeting eligibility requirements participate in the University of Iowa Retirement Plan (the Plan). The Plan is a defined contribution retirement plan providing benefits through the Teachers Insurance and Annuity Association and the College Retirement Equity Fund (TIAA-CREF). UIHC contributions to the Plan are 10% of employee compensation after the first five years of employment. During the first five years of employment, UIHC's contribution is 6.67% of the first \$4,800 of compensation and 10% of the balance of employee compensation. Employees are required to contribute an amount equal to 50% of UIHC's contribution. All contributions to the Plan are immediately 100% vested.

Eligible employees not electing to participate in the Plan are required to participate in the Iowa Public Employees' Retirement System (IPERS), a multiple employer, cost-sharing public employees' retirement system.

The University internally accounts for employee benefits using a benefits pool. Each department, including UIHC, is assessed a total amount to be paid into the pool covering all employee benefits, which approximated \$28.6 million and \$30.2 million for contributions to TIAA-CREF and IPERS in 2010 and 2009, respectively.

(6) Health Insurance Benefits for Retirees

Other postemployment benefits (OPEB) are recorded in the financial statements as noncurrent accrued payroll on the balance sheets and are included as an operating expense in salaries, wages, and employee benefits on the statements of revenues, expenses, and changes in net assets.

All UIHC employees meeting eligibility requirements participate in the University of Iowa Health Insurance Benefits for Retirees. The University of Iowa's defined benefit postemployment healthcare plan provides medical and dental benefits to eligible retired employees, which include employees who retire from the University after attaining age 55 and before reaching age 62, or who retire after attaining age 62 with ten or more years of service.

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The contribution requirements of plan members and the University are established and may be amended by the Board of Regents. The terms and conditions governing the postemployment benefits to which employees are entitled are in the sole authority and discretion of the University's Board of Regents. For fiscal year 2010 and 2009, UIHC's allocated annual OPEB cost was \$8.5 million and \$4.7 million, respectively, of which \$3.7 million was contributed to the plan in 2010 and \$2.2 million in 2009. The net allocated OPEB obligation at June 30, 2010 and 2009 was \$12.3 million and \$4.4 million, respectively. Although there is no requirement to fund the OPEB liability, the University has chosen to fund it on a "pay as you go" basis. University Policy dictates the payment of retiree claims as they become due. Plan members receiving benefits contributed 55% of the premium costs. In fiscal year 2010 and 2009, total member contributions were \$4.8 million and \$2.6 million, respectively.

The University's defined benefit postemployment healthcare plan does not issue a separate financial report, but is included in the University's annual report, which can be obtained at the University of Iowa, 4 Jessup Hall, Iowa City, IA 52242.

(7) Risk Management

The University, or the State of Iowa on behalf of UIHC, self-insures workers' compensation, unemployment, medical, and dental benefits for eligible employees, automobile, professional, and general liability. UIHC pays the employer portion of the costs related to workers' compensation, unemployment, and medical and dental benefits. UIHC purchases commercial property insurance for its facilities, including business interruption insurance. UIHC also purchases commercial life and disability insurance for eligible employees as part of the University's benefit program.

UIHC's portion of the health insurance liability, which is included in accounts payable and accrued expenses, is \$4,678,317 and \$3,631,515 as of June 30, 2010 and 2009, respectively, as follows:

	2010	2009
Liability for unpaid healthcare claims at beginning of year	\$ 3,631,515	3,761,143
Healthcare expenses incurred during the year	53,759,504	40,862,825
Healthcare payments to the University during the year	(52,712,702)	(40,992,453)
Liability for unpaid healthcare claims at end of year	\$ 4,678,317	3,631,515

Board institutions cooperatively self-insure for automobile liability up to \$250,000. Losses in excess of \$250,000 are self-insured by the State of Iowa.

The State Appeals Board, subject to the advice and approval of the Attorney General, is authorized to settle tort claims against the State of Iowa as set forth in Chapter 669 of the Code of Iowa. Tort liability claims settled in excess of \$5,000 must have the unanimous approval of all the members of the State Appeals Board, the State Attorney General, and the District Court of the State of Iowa for Polk County. By interagency agreement, tort liability claims (including professional liability) under \$5,000 may be administered by the University, subject to a maximum expenditure of \$100,000 per year. All other tort claims are paid from the State of Iowa's general fund and are not an obligation of UIHC.

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The State maintains an employee fidelity bond where the first \$100,000 in losses is the responsibility of UIHC. Losses in excess of the \$100,000 deductible are insured up to \$10,000,000. Coverage extends to all UIHC employees.

(8) Transactions with Related Parties

UIHC receives certain administrative services, utilities, and other general services from the University. The services and support costs include amounts due to the University's Carver College of Medicine for support of graduate medical education, specific clinical services, and other services. These services are charged to UIHC at the approximate cost incurred by the servicing unit. For the years ended June 30, 2010 and 2009, UIHC expensed approximately \$127.4 million and \$122.5 million, respectively, for these administrative services, utilities, and other services and support requirements. At June 30, 2010 and 2009, approximately \$5.7 million and \$1.1 million, respectively, was due to the Carver College of Medicine and \$2.7 million and \$2.5 million, respectively, was due to the University of Iowa for services and support.

UIHC also provides certain administrative services to units of the University. These services include billing, collection, and other physician practice-related clinic overhead expenses. These services are charged to units of the University at the approximate cost incurred by the servicing unit. For the years ended June 30, 2010 and 2009, UIHC received revenue from these units of approximately \$30.0 million and \$29.0 million, respectively, for these services.

UIHC and the College of Medicine have formed a nonprofit corporation, University of Iowa Health System (UIHS), to enhance and support the educational missions of the UIHC and the College of Medicine, particularly as these missions apply to clinical activities and statewide and multi-state network development activities. UIHC paid UIHS for certain administrative and other general services in the amount of \$2.5 million and \$0.9 million for the years ended June 30, 2010 and 2009, respectively.

(9) Net Patient Service Revenue

UIHC has agreements with third-party payors that provide for payments to UIHC at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare

Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors.

Iowa Medicaid

Inpatient and outpatient services rendered to Medicaid program beneficiaries are primarily paid at prospectively determined rates per discharge. Physician clinical services are paid based on fee schedule amounts.

Revenue from Medicare and Medicaid programs accounted for approximately 25% and 13%, respectively, of UIHC's net patient revenue for the year ended 2010, and 24% and 13%, respectively, of UIHC's net patient revenue for the year ended 2009. Laws and regulations governing the Medicare and Medicaid

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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. The 2010 and 2009 net patient service revenue increased approximately \$1.6 million and \$2.2 million, respectively, due to prior year retroactive adjustments in excess of amounts previously estimated.

UIHC has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to UIHC under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Net patient service revenue, as reflected in the accompanying statements of revenues, expenses, and changes in net assets, consists of the following:

	2010	2009
Gross patient charges:		
Inpatient charges	\$ 1,124,983,324	1,115,977,290
Outpatient charges	978,344,507	872,887,178
Total gross patient charges	2,103,327,831	1,988,864,468
Less:		
Deductions from gross patient charges:		
Contractual adjustments – Medicare, Medicaid, and other	1,203,621,839	1,105,447,892
Net patient service revenue	\$ 899,705,992	883,416,576

Included in net patient service revenue are certain amounts received from the State of Iowa in support of indigent care. State reimbursements are received annually to provide acute patient care, psychiatric, and developmental patient care services to patients. Patients are referred from a variety of sources, such as their home county, state institutions, and school districts. For the years ended June 30, 2010 and 2009, amounts received from the State of Iowa were \$74.3 million and \$70.1 million, respectively.

(10) Charity Care

The State of Iowa (the State) has annually provided funding to UIHC to care for certain uninsured or underinsured individuals, as well as to provide psychiatric services and services to children with disabilities. This funding also helps to assure that a sufficient patient base exists at UIHC to support health professionals' education. Effective July 1, 2005, the state-sponsored indigent care program ended and was replaced with a new Medicaid waiver demonstration program titled "IowaCare." The IowaCare program is approved by the Centers for Medicare and Medicaid Services for a five-year period from July 1, 2005 through June 30, 2010. Appropriations received for these programs in 2010 and 2009 were \$74.3 million and \$70.1 million, respectively. The State extended the IowaCare program to December 2013. The amount of charges foregone for services and supplies furnished under UIHC's charity policy aggregated to \$260.4 million and \$232.5 million for 2010 and 2009, respectively.

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(11) Concentrations of Credit Risk

UIHC grants credit without collateral to its patients, most of whom are Iowa residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at June 30, 2010 and 2009 was as follows:

	2010	2009
Commercial pay	26%	30%
Medicare	21	16
Self-pay	5	5
Medicaid	13	13
Blue Cross/Blue Shield	23	25
IowaCare	10	8
Other	2	3
	100%	100%

(12) Operating Leases

UIHC uses certain capital assets under noncancelable operating leases. In most cases, management expects that, in the normal course of operations, the leases will be renewed or replaced by other leases. Total rent expense under operating leases for the years ended June 30, 2010 and 2009 was \$4,878,262 and \$5,522,263, respectively.

The following is a schedule by year of future minimum rental payments required under noncancelable operating leases as of June 30, 2010:

	Year ending June 30:	
	2011	\$ 2,690,936
	2012	758,032
	2013	583,760
	2014	323,760
	2015	323,760
	Total minimum payments required	\$ 4,680,248

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(13) Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses reported as current liabilities at June 30, 2010 and 2009 consisted of the following amounts:

<u>Accounts payable and accrued expenses</u>	<u>2010</u>	<u>2009</u>
Payable to employees (including payroll taxes)	\$ 51,054,334	52,365,447
Payable to suppliers	26,622,371	27,981,482
Other	1,965,401	1,828,853
Total accounts payable and accrued expenses	<u>\$ 79,642,106</u>	<u>82,175,782</u>

(14) Law and Regulations

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that UIHC is in compliance with government laws and regulations as they apply to the areas of fraud and abuse. While no regulatory inquiries have been made that are expected to have a material effect on UIHC's financial statements, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory action unknown or unasserted at this time.

(15) Subsequent Events

UIHC issued \$30,000,000 of Series S.U.I. 2010 Hospital Revenue Bonds in October 2010. The proceeds of the Bonds will be used by the UIHC for the costs of constructing, improving, remodeling, repairing, furnishing, and equipping inpatient and outpatient care facilities, including construction of a new medical office building and related space, including finish materials, fixtures, furnishings, equipment, and appliances, funding a deposit to the Reserve Fund, and paying the costs of issuance of the bonds.

UIHC has reviewed subsequent events through December 6, 2010, the date the financial statements were issued, and concluded that there were no events or transactions during this period that would require recognition or disclosure in the financial statements other than those already disclosed.