



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

December 2, 2015

The Board of Regents
State University of Iowa

Ladies and Gentlemen:

We have audited the financial statements of State University of Iowa, University of Iowa Hospitals and Clinics (UIHC) as of and for the years ended June 30, 2015 and 2014, and have issued our report thereon under date of November 30, 2015. Under our professional standards, we are providing you with the accompanying information related to the conduct of our audits.

Our Responsibility under Professional Standards

We are responsible for forming and expressing an opinion about whether the financial statements, which have been prepared by management with the oversight of the Board of Regents, are presented fairly, in all material respects, in conformity with U.S. generally accepted accounting principles. We have a responsibility to perform our audit of the financial statements in accordance with auditing standards generally accepted in the United States of America. In carrying out this responsibility, we planned and performed the audit to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatement, whether caused by error or fraud. Because of the nature of audit evidence and the characteristics of fraud, we are to obtain reasonable, not absolute, assurance that material misstatements are detected. We have no responsibility to plan and perform the audit to obtain reasonable assurance that misstatements, whether caused by error or fraud, that are not material to the financial statements are detected. Our audits do not relieve management or the Board of Regents of their responsibilities.

In addition, in planning and performing our audit of the financial statements, we considered internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements but not for the purpose of expressing an opinion on the effectiveness of UIHC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of UIHC's internal control.

We also have a responsibility to communicate significant matters related to the financial statement audit that are, in our professional judgment, relevant to the responsibilities of the Board of Regents in overseeing the financial reporting process. We are not required to design procedures for the purpose of identifying other matters to communicate to you.



The Board of Regents
State University of Iowa
December 2, 2015
Page 2 of 3

Accounting Practices and Alternative Treatments

Significant Accounting Policies

The significant accounting policies used by UIHC are described in note 1 to the financial statements. UIHC adopted Governmental Accounting Standards Board (GASB) 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. The adoption of GASB 68 required UIHC to record its proportionate share of pension liability related to its employees' participation in Iowa Public Employee Retirement System (IPERS). The standard was adopted effective July 1, 2014 due to the availability of information from IPERS.

Due to changes in policies related to classification of cash, cash equivalents, and investments, certain reclassifications were made to 2014 balances to conform to 2015 presentation. As permitted by GASB Statement No. 9, certain amounts previously reported as cash and cash equivalents in the prior year have been reclassified as investments to more closely conform to the purpose of those investments. Note 1 to the financial statements for cash and investments describes UIHC's policy for determining, which short-term, highly liquid investments are treated as cash equivalents.

Qualitative Aspects of Accounting Practices

We have discussed with the Board of Regents and management our judgments about the quality, not just the acceptability, of the UIHC's accounting principles as applied in its financial reporting. The discussions generally included such matters as the consistency of the UIHC's accounting policies and their application, and the understandability and completeness of the UIHC's financial statements, which include related disclosures.

Management Judgments and Accounting Estimates

The preparation of the financial statements requires management of UIHC to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period.

Management's estimate of the allowance for doubtful accounts, reserves for contractual allowances on accounts receivable, and settlements with third-party payors are based primarily on historical trends and current reimbursement regulations. We have evaluated key factors and assumptions used to develop these balances, including possible management bias in developing the estimate, and determined that it was reasonable in relation to the financial statements taken as a whole.



The Board of Regents
State University of Iowa
December 2, 2015
Page 3 of 3

Uncorrected and Corrected Misstatements

In connection with our audit of the UIHC's financial statements, we have not identified any significant financial statement misstatements that have not been corrected in the UIHC's books and records as of and for the year ended June 30, 2015 and have communicated that finding to management.

Disagreements with Management

There were no disagreements with management on financial accounting and reporting matters that would have caused a modification of our auditors' report on UIHC's financial statements.

Significant Issues Discussed, or Subject to Correspondence, with Management

Major Issues Discussed with Management prior to Retention

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with you and management each year prior to our retention by you as UIHC's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Material Written Communications

Attached to this letter please find copies of the following material written communications between management and us:

1. Engagement letter
2. Management representation letter

* * * * *

This letter to the Board of Regents is intended solely for the information and use of the Board of Regents and management, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

KPMG LLP



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

Financial Statements

June 30, 2015 and 2014

(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 financial statements of the State University of Iowa, University of Iowa Hospitals and Clinics (UIHC), which comprise the statements of net position as of June 30, 2015 and 2014, and the related statements of revenue, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State University of Iowa, University of Iowa Hospitals and Clinics as of June 30, 2015 and 2014, and the results of its operations and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.



Emphasis of Matters

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, 2015 and 2014, the changes in its financial position and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

As discussed in note 1 to the financial statements, UIHC adopted Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3–8 and the schedules of proportionate share in net pension liability and UIHC contributions on pages 38 – 41 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquires of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

/s/KPMG LLP

November 30, 2015
Des Moines, Iowa

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

Management's Discussion and Analysis

June 30, 2015 and 2014

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, 2015 and 2014. 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

UIHC demonstrated financial success in 2015 with an increase in net position of \$37.4 million (inclusive of cumulative effect of adoption of new accounting standard), or 3.0%, as compared to an increase in net position in 2014 by \$57.9 million, or 5.0%. Operating income in 2015 was \$84.1 million, an increase of \$29.5 million when compared to 2014. Nonoperating revenue and expenses decreased \$45.0 million. Operating income in 2014 was \$54.6 million, an increase of \$17.0 million when compared to 2013. Nonoperating revenue and expenses increased \$27.3 million.

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 – statements of net position; statements of revenue, expenses, and changes in net position; and statements 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.

As discussed in note 1 to the financial statements, UIHC adopted GASB 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. The adoption of GASB 68 required UIHC to record its proportionate share of pension liability related to its employees' participation in Iowa Public Employee Retirement System (IPERS). As a result, beginning net position as of July 1, 2014 was restated by \$16.8 million.

Statements of Net Position and Statements of Revenue, Expenses, and Changes in Net Position

In 2015, net position increased by \$37.4 million (inclusive of cumulative effect of adoption of new accounting standard), or approximately 3.0%, to \$1.26 billion. This is primarily due to net income from operations of \$84.1 million. In 2014, net position increased by \$57.9 million, or approximately 5.0%, to \$1.23 billion. This is primarily due to net income from operations of \$54.6 million. Table 1 provides a summary of UIHC's assets, deferred outflows, liabilities, deferred inflows, and net position as of June 30, 2015, 2014, and 2013.

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

Management's Discussion and Analysis

June 30, 2015 and 2014

Table 1
Condensed Statements of Net Position
(In thousands)

Assets and Deferred Outflows	2015	2014	2013
Current assets	\$ 343,237	369,641	309,444
Noncurrent cash and investments	737,817	780,728	821,666
Capital assets, net	820,650	699,136	634,785
Other assets	1,013	1,020	936
Total assets	1,902,717	1,850,525	1,766,831
Deferred outflows	6,105	452	504
Total assets and deferred outflows	\$ 1,908,822	1,850,977	1,767,335
Liabilities, Deferred Inflows, and Net Position			
Current liabilities	\$ 213,955	211,848	176,497
Long-term debt	356,212	370,579	384,896
Other long-term liabilities	69,827	43,009	38,227
Total liabilities	639,994	625,436	599,620
Deferred inflows	5,928	16	41
Net position:			
Net investment in capital assets	486,161	457,748	427,715
Restricted	5,633	7,571	8,410
Unrestricted	771,106	760,206	731,549
Total net position	1,262,900	1,225,525	1,167,674
Total liabilities, deferred inflows, and net position	\$ 1,908,822	1,850,977	1,767,335

Table 2 shows the changes in net position for 2015 compared to 2014 and 2013.

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

Management's Discussion and Analysis

June 30, 2015 and 2014

Table 2

Statements of Revenue, Expenses, and Changes in Net Position

(In thousands)

	<u>2015</u>	<u>2014</u>	<u>2013</u>
Operating revenue:			
Net patient service revenue	\$ 1,261,432	1,139,952	1,072,224
Other revenue	52,835	49,580	53,112
Total operating revenue	<u>1,314,267</u>	<u>1,189,532</u>	<u>1,125,336</u>
Operating expenses:			
Salaries and benefits	600,713	568,736	563,686
Medical supplies and drugs	282,719	247,318	222,992
Other supplies and general expenses	272,038	245,250	228,768
Depreciation and amortization	74,712	73,640	72,344
Total operating expenses	<u>1,230,182</u>	<u>1,134,944</u>	<u>1,087,790</u>
Operating income	<u>84,085</u>	<u>54,588</u>	<u>37,546</u>
Nonoperating revenue (expenses):			
Gain (loss) on disposal of capital assets	212	(2,986)	(614)
Noncapital gifts	2	50	2,529
Investment income	7,563	56,837	22,688
Interest expense	(7,490)	(8,607)	(6,635)
Total nonoperating revenue, net	<u>287</u>	<u>45,294</u>	<u>17,968</u>
Excess of revenue over expenses before transfers	84,372	99,882	55,514
Capital gifts and grants	163	300	20
Net transfers out	(30,415)	(42,331)	(46,749)
Increase in net position	<u>54,120</u>	<u>57,851</u>	<u>8,785</u>
Net position, beginning of year	1,225,525	1,167,674	1,158,889
Cumulative effect of adoption of accounting standard	(16,745)	—	—
Net position, beginning of year, as restated	<u>1,208,780</u>	<u>1,167,674</u>	<u>1,158,889</u>
Net position, end of year	<u>\$ 1,262,900</u>	<u>1,225,525</u>	<u>1,167,674</u>

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

Management's Discussion and Analysis

June 30, 2015 and 2014

Net Patient Service Revenue

Net patient service revenue increased from 2014 to 2015 by \$121.5 million, or 10.7%, and \$67.7 million, or 6.3%, from 2013 to 2014. 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 2015 resulted from increases in both inpatient and outpatient areas. There was an increase in outpatient clinic visits from 2014 to 2015 by 33,162, or 3.9%, and an increase in outpatient surgeries of 778, or 2.7%. On the inpatient side, acute admissions were up 1,118, or 3.6%, over 2014 and inpatient surgeries increased by 769, or 6.6%. The increase in 2014 resulted from increases in outpatient areas. There was an increase in outpatient clinic visits from 2013 to 2014 by 28,552, or 3.4%, and an increase in outpatient surgeries of 294, or 1.7%.

The provision for bad debts (a deduction from gross patient charges) decreased \$35.1 million from \$50.9 million in 2014 to \$15.8 million in 2015. The provision for bad debts (a deduction from gross patient charges) increased \$26 million from \$24.9 million in 2013 to \$50.9 million in 2014. The decrease in the provision for bad debts in 2015 was caused by a shift in payor mix from self-pay to other insurers. The increase in the provision for bad debts in 2014 was caused by a shift in payor mix from IowaCare to self-pay.

Operating Expenses

Total operating expenses increased 8.4% from \$1.13 billion in 2014 to \$1.23 billion in 2015. The largest dollar increase in expenses in 2015 was in medical supplies and drugs, which increased \$35.4 million, or 14.3%, when compared to 2014. In 2015, there was a continued effort to expand the outpatient pharmacy specialty drug program, which along with increased volumes and inflation, increased drug expense.

Total operating expenses increased 4.3% from \$1.09 billion in 2013 to \$1.13 billion in 2014. The largest dollar increase in expenses in 2014 was in medical supplies and drugs, which increased \$24.3 million, or 10.9%, when compared to 2013. In addition, other supplies and general expenses increased \$16.5 million, or 7.2%, in 2014 compared with 2013. In 2014, there was a concerted effort to expand the outpatient pharmacy specialty drug program, which along with increased volumes and inflation, increased drug expense.

Nonoperating Revenue and Expenses, Net

Nonoperating revenue consists primarily of gains (losses) on disposals of capital assets, investment income, interest expense, and noncapital gifts. Investment income decreased from 2014 to 2015 by \$49.3 million, or 86.7%, and increased from 2013 to 2014 by \$34.1 million, or 150.5%. During 2015, UIHC recorded overall earnings on the endowment and operating pools of \$27.4 million and a net unrealized loss on investments of \$19.9 million, which decreased investment income accordingly. This compares to the overall earnings on the endowment and operating pools of \$20.4 million and a net unrealized gain on investments of \$36.4 million in the previous year. The increases in these investments follow overall increases in the investment markets.

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

Management's Discussion and Analysis

June 30, 2015 and 2014

Statements of Cash Flows

The statements of cash flows reports cash receipts, cash payments, and net changes in cash resulting from operating, investing, and financing activities. UIHC's overall liquidity decreased during 2015, with a net decrease in cash and cash equivalents of \$5.6 million. In 2015, net cash from operating activities provided cash inflows of \$102.4 million and net cash used in noncapital financing was \$30.4 million. UIHC's overall liquidity increased during 2014 with a net increase in cash and cash equivalents of \$2.7 million. In 2014, net cash from operating activities provided cash inflows of \$150.0 million and net cash used in noncapital financing was \$42.3 million. UIHC's overall liquidity increased during 2013 with a net increase in cash and cash equivalents of \$0.3 million.

Capital Assets and Debt Administration

Capital Assets

At the end of 2015, UIHC had \$820.6 million invested in capital assets, net of accumulated depreciation. This is a \$121.5 million increase when compared to capital assets, net in 2014 of \$699.1 million. This increase is primarily due to the UIHC Children's Hospital. Capital assets, net of accumulated depreciation increased \$64.3 million in 2014 when compared to capital assets, net in 2013 of \$634.8 million. This increase is primarily due to UIHC Children's Hospital.

The major capital asset additions in 2014 and 2015 included the following:

- UIHC Children's Hospital
- Construction of new shelled-in space for John Colloton and John Pappajohn Pavilion levels 7 and 8
- Revenue software module for EPIC Electronic Medical Record System
- Emergency Power Generator for John Pappajohn Pavilion
- Cardiovascular Intensive Care Unit Renovation
- Iowa River Landing Procedure Suite Expansion
- Children's Hospital Equipment
- Ambulatory Surgery Center and Operating Room Expansion
- Iowa River Landing Clinical Expansion

Debt

At June 30, 2015 and 2014, UIHC had \$369.6 million and \$383.9 million, respectively, in bonds and capital lease outstanding. During 2015 and 2014, payments of long-term debt were \$13.3 million and \$8.1 million, respectively.

During 2015 and 2014, UIHC issued no Hospital Revenue Bonds.

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

Management's Discussion and Analysis

June 30, 2015 and 2014

Contacting UIHC's Financial Management

This financial report provides the citizens of Iowa, UIHC 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, 318 CMAB, Iowa City, Iowa 52242.

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

Statements of Net Position

June 30, 2015 and 2014

(In thousands)

Assets and Deferred Outflows	2015	2014
Current assets:		
Cash and cash equivalents	\$ 13,383	18,996
Short-term investments	51,886	141,613
Patient accounts receivable, net of estimated uncollectibles \$21,116 in 2015 and \$32,426 in 2014	236,775	176,696
Inventories	23,698	19,266
Current investments for debt service – restricted	1,296	1,581
Other current assets	16,199	11,489
Total current assets	343,237	369,641
Noncurrent cash and investments:		
Limited by bond resolutions	62,224	142,558
Designated by the Board of Regents	670,971	631,880
Restricted by donors	4,622	6,290
	737,817	780,728
Capital assets, net	820,650	699,136
Other assets	1,013	1,020
Total assets	1,902,717	1,850,525
Deferred outflow of resources:		
Deferred outflows	6,105	452
Total assets and deferred outflows	\$ 1,908,822	1,850,977
Liabilities, Deferred Inflows, and Net Position		
Current liabilities:		
Current maturities of long-term debt	\$ 13,416	13,350
Accounts payable and accrued expenses	128,878	118,017
Estimated third-party payor settlements	51,752	55,167
Due to related parties	9,740	14,783
Other current liabilities	5,393	5,592
Accrued interest	4,776	4,939
Total current liabilities	213,955	211,848
Long-term debt, net of current maturities	356,212	370,579
Other long-term liabilities	69,827	43,009
Total liabilities	639,994	625,436
Deferred inflow of resources:		
Deferred inflows	5,928	16
Net position:		
Net investment in capital assets	486,161	457,748
Restricted by donors for specific purposes	4,337	5,990
Restricted for debt service	1,296	1,581
Unrestricted	771,106	760,206
Total net position	1,262,900	1,225,525
Total liabilities, deferred inflows, and net position	\$ 1,908,822	1,850,977

See accompanying notes to financial statements.

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

Statements of Revenue, Expenses, and Changes in Net Position

Years ended June 30, 2015 and 2014

(In thousands)

	2015	2014
Operating revenue:		
Net patient service revenue, net of provision for bad debts of \$15,831 in 2015 and \$50,971 in 2014	\$ 1,261,432	1,139,952
Other revenue	52,835	49,580
Total operating revenue	1,314,267	1,189,532
Operating expenses:		
Salaries and benefits	600,713	568,736
Medical supplies and drugs	282,719	247,318
Other supplies and general expenses	272,038	245,250
Depreciation and amortization	74,712	73,640
Total operating expenses	1,230,182	1,134,944
Operating income	84,085	54,588
Nonoperating revenue (expenses):		
Loss on disposal of capital assets	212	(2,986)
Noncapital gifts	2	50
Investment income	7,563	56,837
Interest expense	(7,490)	(8,607)
Total nonoperating revenue, net	287	45,294
Excess of revenue over expenses before transfers	84,372	99,882
Capital gifts and grants	163	300
Net transfers out	(30,415)	(42,331)
Increase in net position	54,120	57,851
Net position, beginning of year	1,225,525	1,167,674
Cumulative effect of adoption of accounting standard	(16,745)	—
Net position, beginning of year, as restated	1,208,780	1,167,674
Net position, end of year	\$ 1,262,900	1,225,525

See accompanying notes to financial statements.

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

Statements of Cash Flows

Years ended June 30, 2015 and 2014

(In thousands)

	2015	2014
Cash flows from operating activities:		
Receipts from and on behalf of patients	\$ 1,197,937	1,140,599
Other receipts	47,793	62,342
Payments to employees	(582,819)	(563,132)
Payments to suppliers and contractors	(560,505)	(489,807)
Net cash provided by operating activities	102,406	150,002
Cash flows from noncapital financing activities:		
Net transfers	(30,415)	(42,331)
Noncapital gifts	2	50
Net cash used in noncapital financing activities	(30,413)	(42,281)
Cash flows from capital and related financing activities:		
Purchase of capital assets	(197,200)	(138,715)
Proceeds from the sale of capital assets	974	727
Capital gifts and grants received	163	300
Principal paid on long-term debt	(13,350)	(8,108)
Interest paid on long-term debt	(8,605)	(9,665)
Net cash used in capital and related financing activities	(218,018)	(155,461)
Cash flows from investing activities:		
Proceeds from sale of investments	424,542	408,337
Purchase of investments	(311,623)	(378,122)
Interest and dividends received on investments	27,493	20,258
Net cash provided by investing activities	140,412	50,473
Net (decrease) increase in cash and cash equivalents	(5,613)	2,733
Cash and cash equivalents at beginning of year	18,996	16,263
Cash and cash equivalents at end of year	\$ 13,383	18,996
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 84,085	54,588
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	74,712	73,640
Provision for bad debts	15,831	50,971
Changes in assets and liabilities:		
Accounts receivable	(75,911)	(65,724)
Inventories	(4,432)	(147)
Other assets	(10,069)	1,719
Accounts payable and accrued expenses	10,861	1,690
Other liabilities	15,786	5,105
Due to related parties	(5,042)	12,761
Estimated third-party payor settlements	(3,415)	15,399
Net cash provided by operating activities	\$ 102,406	150,002

Noncash investing activity:

During 2015 and 2014, the net appreciation in fair value of investments was \$(19,860) and \$36,526, respectively.

See accompanying notes to financial statements.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(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 State University of Iowa (the University), which are generally referred to as the University Hospital, the Psychiatric Hospital, and the Center for Disabilities and Development. UIHC is part of 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 (UIHS), 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's financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Under this method, revenue is recorded when earned and expenses are recorded at the time liabilities are incurred without regard to receipt or disbursement of cash.

(c) Adoption of New Accounting Standard

UIHC adopted GASB 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. The adoption of GASB 68 required UIHC to record its proportionate share of pension liability related to its employees' participation in Iowa Public Employee Retirement System (IPERS). The standard was adopted effective July 1, 2014 due to the availability of information from IPERS.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

The following represents the changes in net position as of July 1, 2014 as a result of the adoption standard:

	<u>Balances</u> <u>June 30, 2014</u>	<u>Adoption</u> <u>GASB 68</u>	<u>Balances</u> <u>July 1, 2014</u>
Deferred outflows	\$ 452	2,289	2,741
Other long-term liabilities	43,008	19,034	62,042
Net position	1,225,525	(16,745)	1,208,780

(d) 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

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

For purposes of the Statement of Net Position and Statement of Cash Flows, cash and cash equivalents are reported in accordance with Board of Regents, State of Iowa policy Chapter 7.04, Section H.2 (www.regents.iowa.gov/Policies/Chapter%207/Chapter7.04.htm), as amended, which states, in part: to appropriately reflect the Board's overall investment strategy and as outlined in the GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, that all funds held by external investment managers, as defined in Section 7.04.C.4 of the Board's investment policy, shall be reported on the audited financial statements of the Regent institutions as investments. Investments purchased by the institutions through Board authorized brokerage firms that meet the definition of cash equivalents, investments with original purchase dates to maturity of three months or less shall be reported on the audited financial statements of the Regent institutions as cash equivalents.

Undesignated cash equivalents totaling \$13.4 million and \$19.0 million at June 30, 2015 and 2014, respectively, represent money market funds and other short-term investments not held by external investment managers that mature in three months or less from date of purchase.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(f) 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.

(g) 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 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

(h) Deferred Outflows and Inflows of Resources

Deferred outflows of resources represent consumptions of net position that apply to future periods and will not be recognized as an outflow of resources (expense) until then.

Deferred inflows of resources represent acquisitions of net position that apply to future periods and will not be recognized as an inflow of resources (revenue) until then.

(i) 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.

(j) Gifts and Grants

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

(k) 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.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(l) Net Position

Net position of UIHC is classified in four components. Net investment in capital assets consists 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 position restricted by donors for specific purposes is noncapital net position that must be used for a particular purpose, as specified by grantors, or contributors external to UIHC. Net position restricted for debt service is amounts deposited with trustees as required by bond indentures. Unrestricted net position is remaining net position that does not meet the definition of net investment in capital assets or restricted.

(m) Operating Revenue and Expenses

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

(n) 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 services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors and estimated uncollectible amounts. 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.

(o) 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 revenue in the accompanying statements of revenue, expenses, and changes in net position.

(p) 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.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

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.

(q) Pension - Iowa Public Employees Retirement System

For purposes of measuring the net pension asset, deferred outflows of resources and deferred inflows of resources, and pension expense, information about the fiduciary net position of the Iowa Public Employees Retirement System (IPERS) and additions to/deductions from IPERS' fiduciary net position have been determined on the same basis as they are reported by IPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with benefit terms. Investments are reported at fair value.

(r) 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.

(s) Reclassifications

Certain reclassifications were made to 2014 balances to conform to 2015 presentation. Not all investments that qualify are required to be treated as cash equivalents. As permitted by GASB Statement No. 9, certain amounts previously reported as cash and cash equivalents in the prior year have been reclassified as investments to more closely conform to the purpose of those investments. Note 1 to the financial statements for cash and investments describes UIHC's policy for determining, which short-term, highly liquid investments are treated as cash equivalents.

(2) Deposits and Investments

Investments are made in accordance with Chapter 12B.10A, Section 5d of the Code of Iowa, and Board of Regents, State of Iowa policy. The University's portfolios may be invested in obligations of the U.S. government and its agencies, certificates of deposit, prime bankers' acceptances, commercial paper, repurchase agreements, investments authorized for the Iowa Public Employees' Retirement System in Section 97B.7A of the Code of Iowa, corporate debt, mortgage pass-through, and asset-backed securities, bank loans, an open-end management investment company organized in trust form registered with the S.E.C. under the Investment Company Act of 1940, the Common Fund for nonprofit organizations, commingled vehicles/mutual funds/exchange-traded funds, and common stocks.

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, 2015 and 2014 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.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

Noncurrent cash and investments limited by bond resolutions or designated by the Board were held for the following purposes at June 30, 2015 and 2014:

	2015	2014
Limited by bond resolutions:		
Debt service reserve	\$ 27,080	27,072
Unspent bond proceeds	35,144	115,486
Designated by the Board of Regents:		
Capital projects and equipment and other needs	446,082	386,412
Surplus	1,096	476
Improvement, extension, repair, operation, and maintenance funds	223,793	244,992
Restricted by donors	4,622	6,290
	\$ 737,817	780,728

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 pools with allocations to equities, fixed income, real assets, and liquidity asset classes.

Cash and cash equivalents and short-term investments specifically identified or pooled with the cash and investments of the University totaled \$65.3 million and \$160.6 million at June 30, 2015 and 2014, respectively. Cash equivalents designated by the Board totaled \$233.8 million and \$142.3 million at June 30, 2015 and 2014, respectively.

UIHC's investments are recorded at fair value. As of June 30, 2015, UIHC had the following investments and quality credit ratings (in thousands):

Fixed income	Effective duration (years)	TSY/AGY AAA	AA	A	BBB	BB	B	N/A	Total market value
Corporate notes and bonds	1.63	\$ 1,021	290	2,087	1,194	29	—	—	4,621
U.S. government agencies	1.35	21,375	494	—	—	—	—	—	21,869
U.S. Treasury obligations	1.55	27,570	—	—	—	—	—	—	27,570
Mutual funds	4.14	—	78,680	14,659	33,174	21,174	64,254	—	211,941
		\$ 49,966	79,464	16,746	34,368	21,203	64,254	—	266,001
Other investments:									
Cash and cash equivalents									298,957
U.S. equity mutual funds									54,375
Non-U.S. equity mutual funds									49,772
Real assets									85,093
Private equity									5,380
Repurchase agreement									44,804
Total cash and investments									\$ 804,382

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

UIHC's investments are recorded at fair value. As of June 30, 2014, UIHC had the following investments and quality credit ratings (in thousands):

<u>Fixed income</u>	<u>Effective duration (years)</u>	<u>TSY/AGY AAA</u>	<u>AA</u>	<u>A</u>	<u>BBB</u>	<u>BB</u>	<u>B</u>	<u>N/A</u>	<u>Total market value</u>
Corporate notes and bonds	1.74	\$ 3,109	304	2,231	1,425	—	—	—	7,069
U.S. government agencies	1.37	28,454	—	—	—	—	—	38	28,492
U.S. Treasury obligations	1.97	30,368	—	—	—	—	—	—	30,368
Mutual funds	3.98	—	119,798	13,679	2,393	23,783	73,341	—	232,994
		<u>\$ 61,931</u>	<u>120,102</u>	<u>15,910</u>	<u>3,818</u>	<u>23,783</u>	<u>73,341</u>	<u>38</u>	298,923
Other investments:									
Cash and cash equivalents									302,704
U.S. equity mutual funds									74,078
Non-U.S. equity mutual funds									55,048
Real assets									92,824
Private equity									3,838
Repurchase agreement									115,503
Total cash and investments									<u>\$ 942,918</u>

Interest Rate Risk – Interest rate risk is the risk changes in interest rates will adversely affect the fair value of an investment. This risk is measured using effective duration. At time of purchase, the effective maturity of direct investment purchases by the University 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. As of June 30, 2015, the University's long-term bond funds benchmark is AA (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 University investment portfolios are invested in securities of a single issuer. All direct investment purchases by the University in the operating portfolio are U.S. Treasury and Agency securities.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(3) Capital Assets

Capital assets at June 30, 2015 and 2014 are summarized as follows (in thousands):

	2015	2014
Land	\$ 17,835	15,609
Land improvements	925	925
Infrastructure	54,686	48,999
Buildings and leasehold improvements	944,851	888,365
Equipment and software	448,450	409,833
Construction in progress (nondepreciable)	244,329	166,096
	1,711,076	1,529,827
Less accumulated depreciation	890,426	830,691
	\$ 820,650	699,136

Capital asset additions, retirements, and balances as of and for the years ended June 30, 2015 and 2014 were as follows (in thousands):

Cost basis summary	June 30, 2014 balances	Acquisitions	Sales retirements and transfers	June 30, 2015 balances
Land (nondepreciable)	\$ 15,609	2,226	—	17,835
Land improvements	925	—	—	925
Infrastructure	48,999	5,687	—	54,686
Buildings and leasehold improvements	888,365	56,586	(100)	944,851
Equipment and software	409,833	54,256	(15,639)	448,450
Construction in progress (nondepreciable)	166,096	160,696	(82,463)	244,329
Total at historical cost	1,529,827	279,451	(98,202)	1,711,076
Less accumulated depreciation for:				
Land improvements	776	17	—	793
Infrastructure	41,073	1,678	—	42,751
Buildings and leasehold improvements	532,075	30,367	(100)	562,342
Equipment and software	256,767	42,650	(14,877)	284,540
Total accumulated depreciation	830,691	74,712	(14,977)	890,426
Total capital assets, net	\$ 699,136	204,739	(83,225)	820,650

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

<u>Cost basis summary</u>	<u>June 30, 2013 balances</u>	<u>Acquisitions</u>	<u>Sales retirements and transfers</u>	<u>June 30, 2014 balances</u>
Land (nondepreciable)	\$ 15,596	13	—	15,609
Land improvements	925	—	—	925
Infrastructure	47,890	1,109	—	48,999
Buildings and leasehold improvements	847,328	41,100	(63)	888,365
Equipment and software	403,011	36,289	(29,467)	409,833
Construction in progress (nondepreciable)	102,904	107,300	(44,108)	166,096
Total at historical cost	<u>1,417,654</u>	<u>185,811</u>	<u>(73,638)</u>	<u>1,529,827</u>
Less accumulated depreciation for:				
Land improvements	759	17	—	776
Infrastructure	39,660	1,413	—	41,073
Buildings and leasehold improvements	501,218	30,920	(63)	532,075
Equipment and software	241,232	41,290	(25,755)	256,767
Total accumulated depreciation	<u>782,869</u>	<u>73,640</u>	<u>(25,818)</u>	<u>830,691</u>
Total capital assets, net	<u>\$ 634,785</u>	<u>112,171</u>	<u>(47,820)</u>	<u>699,136</u>

At June 30, 2015, 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, 2015 is \$151.4 million. Other projects at June 30, 2015, with an estimated cost of \$289.9 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, 2015 and 2014 were \$6.2 million and \$5.6 million, respectively.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(4) Long-Term Debt

Long-term debt outstanding at June 30, 2015 and 2014 was as follows (in thousands):

	2015	2014
Hospital Revenue Bonds:		
Series S.U.I. 2007 – 4.375% to 5.500%; maturing serially on September 1 through 2027	\$ 18,675	19,750
Series S.U.I. 2007A – 4.000% to 5.500%; maturing serially on September 1 through 2027	18,850	19,850
Series S.U.I. 2009 – 5.500% to 6.125%; maturing serially on September 1 through 2028	26,525	27,825
Series S.U.I. 2010 – 3.000% to 4.500%; maturing serially on September 1 through 2037	27,675	28,475
Series S.U.I. 2011 – 2.000% to 4.000%; maturing serially on September 1 through 2032	24,875	25,850
Series S.U.I. 2011A – 2.000% to 4.125%; maturing serially on September 1 through 2028	17,375	18,355
Series S.U.I. 2012 – 4.000% to 4.000%; maturing serially on September 1 through 2038	184,925	190,000
Net unamortized premium on Hospital Revenue Bonds	12,164	13,116
Telecommunications Facilities Revenue Bonds:		
Series S.U.I. 2008 – 3.100% to 3.375%; maturing serially on July 1 through 2015	297	870
Series S.U.I. 2009 – 3.000% to 4.250%; maturing serially on July 1 through 2036	11,804	12,150
Series S.U.I. 2011 – 2.000% to 4.500%; maturing serially on July 1 through 2032	7,005	7,289
Total long-term bonds	350,170	363,530
Capital lease obligation	19,458	20,399
Total long-term debt	369,628	383,929
Long-term debt, current portion	13,416	13,350
	\$ 356,212	370,579

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

Activity in long-term debt for the years ended June 30, 2015 and 2014 was as follows (in thousands):

	<u>June 30, 2014</u> <u>balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>June 30, 2015</u> <u>balance</u>	<u>Amounts due</u> <u>within</u> <u>one year</u>
Hospital Revenue Bonds, Series 2007	\$ 19,750	—	(1,075)	18,675	1,100
Hospital Revenue Bonds, Series 2007A	19,850	—	(1,000)	18,850	1,050
Hospital Revenue Bonds, Series 2009	27,825	—	(1,300)	26,525	1,350
Hospital Revenue Bonds, Series 2010	28,475	—	(800)	27,675	825
Hospital Revenue Bonds, Series 2011	25,850	—	(975)	24,875	1,000
Hospital Revenue Bonds, Series 2011A	18,355	—	(980)	17,375	1,010
Hospital Revenue Bonds, Series 2012	190,000	—	(5,075)	184,925	5,175
Net unamortized bond premium	13,116	—	(952)	12,164	
Telecommunications Facilities Revenue Bonds:					
Series 2008	870	—	(573)	297	297
Series 2009	12,150	—	(346)	11,804	352
Series 2011	7,289	—	(284)	7,005	288
Total long-term bonds	363,530	—	(13,360)	350,170	12,447
Capital lease obligations	20,399	—	(941)	19,458	969
Total long-term debt \$	<u>383,929</u>	<u>—</u>	<u>(14,301)</u>	<u>369,628</u>	<u>13,416</u>

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

	<u>June 30, 2013</u> <u>balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>June 30, 2014</u> <u>balance</u>	<u>Amounts due</u> <u>within</u> <u>one year</u>
Hospital Revenue Bonds, Series 2007	\$ 20,775	—	(1,025)	19,750	1,075
Hospital Revenue Bonds, Series 2007A	20,800	—	(950)	19,850	1,000
Hospital Revenue Bonds, Series 2009	29,075	—	(1,250)	27,825	1,300
Hospital Revenue Bonds, Series 2010	29,250	—	(775)	28,475	800
Hospital Revenue Bonds, Series 2011	26,800	—	(950)	25,850	975
Hospital Revenue Bonds, Series 2011A	19,310	—	(955)	18,355	980
Hospital Revenue Bonds, Series 2012	190,000	—	—	190,000	5,075
Net unamortized bond premium	14,083	—	(967)	13,116	—
Telecommunications Facilities Revenue Bonds:					
Series 2003	112	—	(112)	—	—
Series 2008	1,426	—	(556)	870	573
Series 2009	12,489	—	(339)	12,150	346
Series 2011	7,571	—	(282)	7,289	285
Total long-term bonds	371,691	—	(8,161)	363,530	12,409
Capital lease obligations	21,313	—	(914)	20,399	941
Total long-term debt	\$ 393,004	—	(9,075)	383,929	13,350

Long-Term Bonds

The Hospital Revenue Bonds are special obligations of the Board 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 at the University, 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, less current expenses (as defined in the resolution authorizing the issuance of the bonds, the Bond Resolution). Hospital Income does not include state appropriations to the University or IowaCare appropriations to the Hospital System. So long as the bonds or parity bonds remain outstanding, the entire Hospital Income 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 \$25.3 million. The maximum amount of Hospital Income pledged representing the undiscounted principal and interest on the bonds is \$502.5 million.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

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.

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

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year(s) ending June 30:			
2016	\$ 12,447	13,728	26,175
2017	12,544	13,235	25,779
2018	12,915	12,723	25,638
2019	13,374	12,205	25,579
2020	13,802	11,675	25,477
2021 through 2025	77,277	49,224	126,501
2026 through 2030	82,040	31,287	113,327
2031 through 2035	63,688	16,508	80,196
2036 through 2039	49,919	3,916	53,835
	<u>\$ 338,006</u>	<u>164,501</u>	<u>502,507</u>

The following are deferred outflows of resources and deferred inflows of resources related to debt refundings as of June 30, 2015:

	<u>Deferred outflows of resources</u>	<u>Deferred inflows of resources</u>
Deferred outflows and inflows from debt refunding:		
Revenue Bonds 2011A Series refunding loss	\$ 402	—
Telecom Bonds 2008 Series refunding gain	—	3
	<u>\$ 402</u>	<u>3</u>

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

Capital Lease Obligations

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

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year(s) ending June 30:			
2016	\$ 969	574	1,543
2017	998	545	1,543
2018	1,027	516	1,543
2019	1,057	486	1,543
2020	1,089	455	1,544
2021 through 2025	5,945	2,438	8,383
2026 through 2030	6,874	1,426	8,300
2031 through 2035	1,499	75	1,574
	<u>\$ 19,458</u>	<u>6,515</u>	<u>25,973</u>

(5) Retirement Benefit Plans

Teachers Insurance and Annuity Association

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 remaining 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.

Iowa Public Employees Retirement System

Plan Description – Eligible employees not electing to participate in the Plan are required to participate in the Iowa Public Employees' Retirement System (IPERS), which is a cost-sharing multiple-employer defined-benefit pension plan administered by the State of Iowa (the State). IPERS issues a stand-alone financial report, which is available to the public by mail at 7401 Register Drive P.O. Box 9117, Des Moines, Iowa 50306-9117 or at www.ipers.org. IPERS benefits are established under Iowa Code Chapter 97B and the administrative rules thereunder. Chapter 97B and the administrative rules are the official plan documents. The following brief description is provided for general informational purposes only. Refer to the plan documents for more information.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

Pension Benefits – A regular member may retire at normal retirement age and receive monthly benefits without an early retirement reduction. Normal retirement age is age 65, anytime after reaching age 62 with 20 or more years of covered employment, or when the member’s years of service plus the member’s age at the last birthday equals or exceeds 88, whichever comes first. (Three qualifications must be met on the member’s first month of entitlement to benefits.) Members cannot begin receiving retirement benefits before age 55. The formula used to calculate a Regular member’s monthly IPERS benefit includes:

- A multiplier (based on years of service)
- The member’s highest five-year average salary (for members with service before June 30, 2012, the highest three-year average salary as of that date will be used if it is greater than the highest five-year average salary.)

If a member retires before normal retirement age, the member’s monthly retirement benefit will be permanently reduced by an early retirement reduction. The early retirement reduction is calculated differently for service earned before and after July 1, 2012. For service earned before July 1, 2012, the reduction is 0.25% for each month that the member receives benefits before the member’s earliest normal retirement age. For service earned starting July 1, 2012, the reduction is 0.50% for each month that the member receives benefits before age 65.

Generally, once a member selects a benefit option, a monthly benefit is calculated and remains the same for the rest of the member’s lifetime. However, to combat the effects of inflation, retirees who began receiving benefits prior to July 1990 receive a guaranteed dividend with their regular November benefit payments.

Disability and Death Benefits – A vested member who is awarded federal Social Security disability or Railroad Retirement disability benefits is eligible to claim IPERS benefits regardless of age. Disability benefits are not reduced for early retirement. If a member dies before retirement, the member’s beneficiary will receive a lifetime annuity or a lump-sum payment equal to the present actuarial value of the member’s accrued benefit or calculated with a set formula, whichever is greater. When a member dies after retirement, death benefits depend on the benefit option the member selected at retirement.

Contributions – Effective July 1, 2012, as a result of a 2010 law change, the contribution rates are established by IPERS following the annual actuarial valuation, which applies IPERS’ Contribution Rate Funding Policy and Actuarial Amortization Method. Statute limits the amount rates can increase or decrease each year to 1 percentage point. IPERS Contribution Rate Funding Policy requires that the actuarial contribution rate be determined using the “entry age normal” actuarial cost method and the actuarial assumptions and methods approved by the IPERS Investment Board. The actuarial contribution rate covers normal cost plus the unfunded actuarial liability payment based on a 30-year amortization period. The payment to amortize the unfunded actuarial liability is determined as a level percentage of payroll, based on the Actuarial Amortization Method adopted by the Investment Board.

In fiscal year 2015, pursuant to the required rate, Regular members contributed 5.95% of pay and UIHC contributed 8.93% for a total rate of 14.8%.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

UIHC's contributions to IPERS for the years ended June 30, 2015 and 2014 were \$2,660 and \$2,299, respectively.

Net Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions – At June 30, 2015, UIHC reported a liability of \$15,536 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2014, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. UIHC's proportion of the net pension liability was based on UIHC's share of contributions to the pension plan relative to the contributions of all IPERS participating employers. At June 30, 2014, the University's proportion was 0.3838778%, which was an increase of 0.118728% from its proportion measured as of June 30, 2013.

For the year ended June 30, 2015, the University recognized pension expense of \$1,674. At June 30, 2015, UIHC reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources (in thousands):

	Deferred outflows of resources	Deferred inflows of resources
Difference between expected and actual experience	\$ 169	—
Changes of assumptions	685	—
Net difference between projected and actual earnings on pension plan investments	—	5,925
Changes in proportion and differences between contributions and proportionate share of contributions	2,188	—
Contributions subsequent to the measurement date	2,660	—
Total	<u>\$ 5,702</u>	<u>5,925</u>

\$2,660 reported as deferred outflows of resources related to pensions resulting from UIHC's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows (in thousands):

Year ending June 30:	
2016	\$ (770)
2017	(770)
2018	(770)
2019	(770)
2020	197
	<u>\$ (2,883)</u>

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

There are no nonemployer contributing entities at IPERS.

Actuarial Assumptions – The total pension liability in the June 30, 2014 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Rate of Inflation (effective June 30, 2014)	3.00%
Salary increase (effective June 30, 2014)	4.00% average, including inflation
Investment rate of return (effective June 30, 1996)	7.50% per annum, compounded annually, net of pension plan investment expense, including inflation

The actuarial assumptions used in the June 30, 2014 valuation were based on the results of actuarial experience studies with dates corresponding to those listed above.

Mortality rates were based on the RP-2000 Mortality Table for Males or Females, as appropriate, with adjustments for mortality improvements based on Scale AA.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset class</u>	<u>Asset allocation</u>	<u>Long-term expected real rate of return</u>
Core Plus Fixed Income	28%	2.06%
U.S. Equity	23	6.31
Non-U.S. Equity	15	6.76
Private Equity	13	11.34
Credit opportunities	5	3.67
Real estate	8	3.52
TIPS	5	1.92
Other real assets	2	6.27
Cash	1	(0.69)
Total	<u>100%</u>	

Discount Rate – The discount rate used to measure the total pension liability was 7.50%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the contractually required rate and that contributions from UIHC will be made at contractually required rates,

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of UIHC's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate – The following presents UIHC's proportionate share of the net pension liability calculated using the discount rate of 7.50%, as well as what UIHC's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.5%) or 1-percentage-point higher (8.5%) than the current rate (in thousands).

	1% Decrease (6.5)%	Discount rate (7.5)%	1% Increase (8.5)%
UIHC's proportionate share of the net pension liability	\$ 29,355	15,536	3,872

Pension Plan Fiduciary Net Position – Detailed information about the pension plan's fiduciary net position is available in the separately issued IPERS financial report, which is available on IPERS' Web site at www.ipers.org.

Payables to the Pension Plan – At June 30, 2015, UIHC reported payables to the defined benefit pension plan of \$256 for legally required employer contributions and \$171 for legally required employee contributions, which had been withheld from employee wages but not yet remitted to IPERS.

(6) Post-Employment Benefits

Other postemployment benefits (OPEB) are recorded in the financial statements as noncurrent accrued payroll on the statements of net position and are included as an operating expense in salaries and benefits on the statements of revenue, expenses, and changes in net position.

(a) Annual OPEB Cost and Net OPEB Obligation for Professional & Scientific and Faculty

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 10 or more years of service.

The contribution requirements of plan members and the University are established and may be amended by the Board. 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. For fiscal years 2015 and 2014, UIHC's allocated annual OPEB cost was \$9.2 million and \$6.3 million, respectively, of which \$2.6 million was contributed to the plan in 2015 and \$2.3 million in 2014. The net allocated OPEB obligation at June 30, 2015 and 2014 was \$25.2 million and \$17.3 million,

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

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 72% and 64% of the premium costs in fiscal years 2015 and 2014, respectively. In fiscal years 2015 and 2014, total member contributions were \$4.0 million and \$4.0 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, Iowa 52242

(b) Other Postemployment Benefits

UIHC’s merit employees are participants in the State of Iowa postretirement medical plan (OPEB Plan). The State of Iowa recognized the implicit rate subsidy for the OPEB Plan as required by GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. For fiscal years 2015 and 2014, UIHC’s allocated annual OPEB cost was \$2.3 million and \$2.5 million, respectively, of which \$1.0 million was contributed to the plan in 2015 and \$1.1 million in 2014. UIHC recognized a net OPEB liability of \$13.3 million and \$11.8 million, at June 30, 2015 and 2014, respectively, for other postemployment benefits, which represents UIHC’s portion of the State’s net OPEB liability. UIHC’s portion of the net OPEB liability was calculated using the ratio of full-time equivalent UIHC merit employees compared to all full-time equivalent employees of the State of Iowa.

Details of the OPEB Plan are provided on a statewide basis and are available in the State of Iowa’s Comprehensive Annual Financial Report. The report may be obtained by writing to the Iowa Department of Administrative Services, Hoover State Office Building, Des Moines, Iowa 50319.

UIHC recognized a net OPEB liability of \$25.3 million for the University retiree benefit plan and a liability of \$13.3 million for its allocation portion of the State’s net OPEB liability, for a total net OPEB liability of \$38.5 million.

(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 liability, professional liability, and general (tort) 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.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

UIHC's portion of the health insurance liability, which is included in accounts payable and accrued expenses, is \$5.2 million and \$4.7 million as of June 30, 2015 and 2014, respectively, as follows (in thousands):

	2015	2014
Liability for unpaid healthcare claims at beginning of year	\$ 4,733	4,244
Healthcare expenses incurred during the year	74,123	69,866
Healthcare payments to the University during the year	(73,706)	(69,377)
Liability for unpaid healthcare claims at end of year	\$ 5,150	4,733

The University of Iowa and other Board of Regents institutions are self-insured for automobile liability up to \$250,000. Losses in excess of \$250,000 are paid by the State of Iowa, as provided in Chapter 669 of the Code of Iowa.

UIHC is an agency of the State of Iowa and is covered by the State's self-insurance for tort liability. Tort claims against the State of Iowa are handled as provided in the Iowa Tort Claims Act (Iowa Code, Chapter 669), which also sets forth the procedures by which tort claims may be brought. Claims under Chapter 669 may be filed against the State on account of wrongful death, personal injury, or property damage incurred by reason of the negligence of the UIHC or its employees while acting within the scope of employment. By interagency agreement, tort liability claims under \$5,000 may be administered by the UIHC subject to a maximum expenditure of \$100,000 per year. All other tort claims may be paid from the State's general fund.

The State maintains an employee fidelity bond where the first \$100,000 in losses is the responsibility of UIHC. Under the State coverage, losses in excess of the \$100,000 deductible are insured up to \$2,000,000. The University maintains separate fidelity and crime coverage, which extends to all employees, and includes coverage for robbery and theft. The University's bond provides an additional \$8,000,000 in coverage over the state bond.

(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, 2015 and 2014, UIHC expensed approximately \$165.0 million and \$148.7 million, respectively, for these administrative services, utilities, and other services and support requirements. At June 30, 2015 and 2014, approximately \$6.1 million and \$11.8 million, respectively, were due to the Carver College of Medicine. At June 30, 2015 and 2014, \$3.7 million and \$3.0 million, respectively, were due to the University of Iowa for services and support.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

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, 2015 and 2014, UIHC received revenue from these units of approximately \$16.0 million and \$16.1 million, respectively, for these services, which is recorded in other revenue in the statement of revenue, expense, and changes in net position.

UIHC transfers to and receives transfers from Non-UIHC University of Iowa units. Net transfers to these units totaled \$30.4 million and \$42.3 million for the years ended June 30, 2015 and 2014, respectively.

University of Iowa Health System and Subsidiaries (UIHS) was incorporated under the provisions of the Iowa Nonprofit Corporations Act on December 2, 1994. UIHS was formed 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 multistate network development activities. UIHC paid UIHS for certain administrative and other general services in the amount of \$1.9 million and \$1.6 million for the years ended June 30, 2015 and 2014, respectively. For the years ended June 30, 2015 and 2014, UIHC transferred \$12.1 million and \$0, respectively, which is recorded in net transfers in the statements of revenue, expenses, and changes in net position.

(9) Net Patient Service Revenue

Net patient service revenue, as reflected in the accompanying statements of revenue, expenses, and changes in net position, consists of the following (in thousands):

	<u>2015</u>	<u>2014</u>
Gross patient charges:		
Inpatient charges	\$ 1,716,806	1,530,196
Outpatient charges	1,635,429	<u>1,547,944</u>
Total gross patient charges	<u>3,352,235</u>	<u>3,078,140</u>
Less deductions from gross patient charges:		
Contractual adjustments – Medicare, Medicaid, and other	2,074,972	1,887,219
Provision for bad debt	<u>15,831</u>	<u>50,969</u>
Net patient service revenue	<u>\$ 1,261,432</u>	<u>1,139,952</u>

The provision for uncollectible patient accounts is based upon UIHC's management's assessment of expected net collections considering the accounts receivable aging, historical collections experience, economic conditions, trends in healthcare coverage, and other collection indicators. Management periodically assesses the adequacy of the allowances for uncollectible accounts and contractual adjustments based upon historical write-off experience. The results of these reviews are used to establish the net realizable value of patient accounts receivable. UIHC follows established guidelines for placing certain patient balances with collection agencies. Self-pay accounts are written off as bad debt at the time of transfer to the collection agency. Deductibles and coinsurance are classified as either third-party or self-pay receivables on the basis

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

of which party has the primary remaining financial responsibility, while the total gross revenue remains classified based on the primary payor at the time of service. Net patient accounts receivable have been adjusted to the estimated amounts expected to be collected.

Patient service revenue (net of contractual allowances and discounts but before the provision for bad debts), recognized in 2015 and 2014 from these major payor sources, is as follows:

	2015	2014
Patient (self-pay)	\$ 23,971	57,928
Less provision for bad debt	15,831	50,971
Self-pay (net of contractual allowance, discounts, and provision for bad debts)	8,140	6,957
Medicaid	226,258	200,343
Medicare	321,083	302,110
Commercial insurance and other third-party payors	705,951	630,542
Patient service revenue (net of contractual allowance, discounts, and provision for bad debts)	\$ 1,261,432	1,139,952

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 is as follows:

(a) 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.

(b) 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 26% and 18%, respectively, of UIHC's net patient revenue for the year ended 2015, and 27% and 18%, respectively, of UIHC's net patient revenue for the year ended 2014. 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. The 2015 net patient service revenue increased approximately \$3.5 million due to prior year retroactive adjustments in excess of amounts previously estimated. The 2014 net patient service revenue increased approximately \$1.0 million due to prior year retroactive adjustments in excess of amounts previously estimated.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(c) IowaCare

The IowaCare program serves people between the ages of 19 and 64 with income up to 200% of the federal poverty level who do not have other sources of healthcare coverage. This program was initially approved by the Centers for Medicare and Medicaid Services (CMS) as a Section 1115 Medicaid demonstration program to operate from July 1, 2005 through June 30, 2010. CMS has subsequently reauthorized the IowaCare program through December 31, 2013. Inpatient and outpatient services rendered to IowaCare program beneficiaries are primarily paid at prospectively determined rates per discharge. The amount of revenue UIHC received for this program in 2015 and 2014 was zero and \$39.9 million, respectively, which is included in commercial and other third-party payors in the table above, which describes patient service revenue by major payor sources.

(d) Commercial

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.

(10) Charity Care and Uncompensated Cost of Services

UIHC provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Certain accounts are classified as charity care and, therefore, are not reported as revenue. Charges forgone for services and supplies furnished under UIHC's charity policy for the years ended June 30, 2015 and 2014 are as follows:

	<u>2015</u>	<u>2014</u>
Charity care	\$ 25,502	34,083
Charity care for state institution patients	<u>7,232</u>	<u>9,899</u>
Charity care charges forgone	<u>\$ 32,734</u>	<u>43,982</u>

UIHC also provides reduced price services and free programs throughout the year. The total uncompensated costs of services other than charity care, for the years ended June 30, 2015 and 2014, approximate the following:

	<u>2015</u>	<u>2014</u>
Medicare	\$ 30,646	28,200
Medicaid	21,783	21,103
Medicaid out of state	2,069	960
IowaCare	<u>—</u>	<u>16,276</u>
Uncompensated costs of services	<u>\$ 54,498</u>	<u>66,539</u>

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(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, 2015 and 2014 was as follows:

	2015	2014
Blue Cross/Blue Shield	29%	26%
Commercial pay	28	32
Medicare	25	22
Medicaid	15	15
Self-pay	1	3
Other	2	2
	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, 2015 and 2014 was \$5.6 million and \$4.7 million, respectively.

The following is a schedule by year of future minimum rental payments required under noncancelable operating leases as of June 30, 2015 (in thousands):

Year ending June 30:	
2016	\$ 7,083
2017	7,664
2018	6,641
2019	5,151
2020	5,119
2021–2025	23,690
2026–2030	23,690
2031–2035	7,655
Total	\$ 86,693

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(13) Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses reported as current liabilities at June 30, 2015 and 2014 consisted of the following amounts (in thousands):

	2015	2014
Payable to employees (including payroll taxes)	\$ 82,546	80,014
Payable to suppliers	38,491	32,799
Other	7,841	5,204
Total accounts payable and accrued expenses	\$ 128,878	118,017

(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.

The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments beginning in 2011 to certain hospitals and professionals that implement and achieve meaningful use of certified electronic health record (EHR) technology in ways that demonstrate improved quality and effectiveness of care. Eligibility for annual Medicare incentive payments is dependent on providers demonstrating meaningful use of EHR technology in each period over a four-year period. An initial Medicaid incentive payment is available to providers that adopt, implement, or upgrade certified EHR technology. However, in order to receive additional Medicaid incentive payments in subsequent years, providers must demonstrate continued meaningful use of EHR technology.

The UIHC accounts for meaningful use incentive payments as a nonexchange transaction. Medicare EHR incentive payments are recognized as revenue when eligible providers demonstrate meaningful use of certified EHR technology and the cost report information for the full cost report year that will determine the full calculation of the incentive payment is available. Medicaid EHR incentive payments are recognized as revenue when an eligible provider demonstrates meaningful use of certified EHR technology. During the years ended June 30, 2015 and 2014, UIHC recognized \$.8 million and \$2.0 million, respectively, of Medicare meaningful use revenue and \$1.4 million and \$2.6 million, respectively, of Medicaid meaningful use revenue in its statements of revenue, expenses, and changes in net position.

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

Notes to Financial Statements

June 30, 2015 and 2014

(Dollars in tables in thousands)

(15) Subsequent Events

UIHC has reviewed subsequent events through November 30, 2015 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.

**STATE UNIVERSITY OF IOWA,
UNIVERSITY OF IOWA HOSPITALS AND CLINICS**
Schedule of Proportionate Share of the Net Pension Liability
Iowa Public Employees' Retirement System

Last Fiscal Year *

(In thousands)

Required Supplementary Information

June 30, 2015

(Unaudited)

UIHC's proportion of the net pension liability		0.38388%
UIHC's proportionate share of the net pension liability	\$	15,536
UIHC's covered-employee payroll		29,902
UIHC's proportionate share of the net pension liability as a percentage of its covered-employee payroll		52.0%
Plan fiduciary net position as a percentage of the total pension liability		87.61%

The amounts presented for each fiscal year were determined as of June 30.

* Note:

GASB Statement No. 68 requires ten years of information to be presented in this table.

However, until a full 10-year trend is compiled, UIHC will present information for those years for which information is available.

See accompanying independent auditors' report.

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

Schedule of UIHC Contributions

Iowa Public Employees' Retirement System

Last 10 Fiscal Years

(In thousands)

Required Supplementary Information

June 30, 2015

(Unaudited)

	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>
Statutorily required contribution	\$ 2,660	2,299	1,896	1,528	976	665	587	470	423	391
Contributions in relation to the statutorily required contribution	<u>(2,660)</u>	<u>(2,299)</u>	<u>(1,896)</u>	<u>(1,528)</u>	<u>(976)</u>	<u>(665)</u>	<u>(587)</u>	<u>(470)</u>	<u>(423)</u>	<u>(391)</u>
Contribution deficiency (excess)	<u>\$ —</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
UIHC's covered-employee payroll	\$ 29,902	25,706	21,965	18,748	13,521	9,854	9,159	7,740	7,212	6,775
Contributions as a percentage of the covered-employee payroll	8.9%	8.9%	8.6%	8.1%	7.2%	6.7%	6.4%	6.1%	5.9%	5.8%

See accompanying independent auditors' report.

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

Notes to Required Supplementary Information

June 30, 2015

(Unaudited)

Changes of Benefit Terms

Legislation passed in 2010 modified benefit terms for current Regular members. The definition of final average salary changed from the highest three to the highest five years of covered wages. The vesting requirement changed from four years of service to seven years. The early retirement reduction increased from 3% per year measured from the member's first unreduced retirement age to a 6% reduction for each year of retirement before age 65.

In 2008, legislative action transferred four groups – emergency medical service providers, county jailers, county attorney investigators, and National Guard installation security officers – from Regular membership to the protection occupation group for future service only.

Benefit provisions for sheriffs and deputies were changed in the 2004 legislative session. The eligibility for unreduced retirement benefits was lowered from age 55 by one year each July 1 (beginning in 2004) until it reached age 50 on July 1, 2008. The years of service requirement remained at 22 or more. Their contribution rates were also changed to be shared 50-50 by the employee and employer, instead of the previous 40-60 split.

Changes of Assumptions:

The 2014 valuation implemented the following refinements as a result of a quadrennial experience study:

- Decreased the inflation assumption from 3.25% to 3.00%.
- Decreased the assumed rate of interest on member accounts from 4.00% to 3.75% per year.
- Adjusted male mortality rates for retirees in the Regular membership group.
- Reduced retirement rates for sheriffs and deputies between the ages of 55 and 64.

Moved from an open 30-year amortization period to a closed 30-year amortization period for the unfunded actuarial liability (UAL) beginning June 30, 2014. Each year thereafter, changes in the UAL from plan experience will be amortized on a separate closed 20-year period.

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

Notes to Required Supplementary Information

June 30, 2015

(Unaudited)

The 2010 valuation implemented the following refinements as a result of a quadrennial experience study:

- Adjusted retiree mortality assumptions.
- Modified retirement rates to reflect fewer retirements.
- Lowered disability rates at most ages.
- Lowered employment termination rates
- Generally increased the probability of terminating members receiving a deferred retirement benefit.
- Modified salary increase assumptions based on various service duration.

The 2007 valuation adjusted the application of the entry age normal cost method to better match projected contributions to the projected salary stream in the future years. It also included in the calculation of the UAL amortization payments the one-year lag between the valuation date and the effective date of the annual actuarial contribution rate.

The 2006 valuation implemented the following refinements as a result of a quadrennial experience study:

- Adjusted salary increase assumptions to service based assumptions.
- Decreased the assumed interest rate credited on employee contributions from 4.25% to 4.00%.
- Lowered the inflation assumption from 3.50% to 3.25%.

Lowered disability rates for sheriffs and deputies and protection occupation members.