

Contact: Andrea Anania

### UIHC AUDIT

**Action Requested:** Receive and discuss the external audit report for the University of Iowa Hospitals and Clinics (UIHC) for the years ended June 30, 2009, and June 30, 2008.

**Executive Summary:** The UIHC report (attached) includes the audit of the basic financial statements on an accrual basis for the fiscal years ended June 30, 2009, and June 30, 2008, as conducted by KPMG LLP, an independent auditing firm, and management's discussion and analysis of the financial activities of UIHC based on currently known facts, decisions, and conditions. (This section is to be read in conjunction with the UIHC audited financial statements and notes to the financial statements.)

For reporting purposes, UIHC includes the following University of Iowa health care units: (1) University Hospital; (2) Psychiatric Hospital; and (3) Center for Disabilities and Development.

The audit indicated that the financial statements present fairly, in all material respects, the financial position of UIHC as of June 30, 2009, and June 30, 2008, and the changes in its net assets and its cash flows for the years then ended. No significant audit adjustments were reported.

A representative from KPMG LLP will be available to answer questions at the Board meeting.

**Additional Information:** Annual audited financial statements of the UIHC are required by Regent Policy Manual §7.09 and by bond covenants.

KPMG LLP conducted the UIHC audit for the fiscal years ended June 30, 2009, and June 30, 2008, in accordance with auditing standards generally accepted in the United States.

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

The financial statements were prepared in accordance with governmental accounting principles generally accepted in the United States. UIHC uses enterprise fund accounting and recognizes revenue and expenses on the accrual basis of accounting using the economic resources measurement focus.

- ◆ As of June 30, 2009, net assets totaled \$968.6 million, which represents a decrease of \$11.2 million (1.1%) from the \$979.8 million from the prior year. A significant component of the change in UIHC's assets is due to the construction or purchase of capital assets totaling \$98.8 million and \$80.7 million during 2009 and 2008, respectively.
- ◆ For FY 2009, operating revenues were \$928.2 million and operating expenses were \$937.0 million, for an operating income of -\$8.8 million (-0.9% of operating revenues). The increases in net patient service revenue were driven by increased patient volumes and pricing. The largest increases in expenses are attributed to salaries and benefits; medical supplies and drugs; and depreciation.
- ◆ Non-operating revenues, expenses, gains, and losses netted -\$3.2 million, which included investment income of \$3.3 million.
- ◆ The majority of long-term debt is from the issuance of hospital revenue bonds and telecommunications facilities revenue bonds totaling \$110.1 million and \$78.9 million as of June 30, 2009, and 2008, respectively; UIHC issued \$37.2 million in revenue bonds during 2009. These bonds are payable solely out of UIHC income.

Related Party Transactions

- ◆ The UIHC purchases certain administrative services, utilities, and other general services from the University. These services are purchased at the approximate cost incurred by the University. For the years ended June 30, 2009, and June 30, 2008, UIHC expensed approximately \$122.5 million and \$105.2 million, respectively, for these services.
- ◆ The UIHC also provides certain administrative services to units of the University. These services include billing, collection, and other physician practice-related clinic overhead expenses. For FY 2009 and FY 2008, the UIHC received revenue of approximately \$29.0 million and \$28.9 million, respectively, for these services.

UIHC and the University's College of Medicine formed a nonprofit corporation, University of Iowa Health System (UIHS), to enhance and support the educational missions of the UIHC and the College of Medicine, particularly as these missions apply to clinical activities and statewide / multi-state network development activities.

- ◆ UIHC supported clinical programs of the University's College of Medicine through transfers of funds of \$0.9 million and \$1.2 million for the years ended June 30, 2009 and June 30, 2008, respectively.

Revenue from Medicare and Medicaid programs accounted for approximately 24% and 13%, respectively, of UIHC's net patient revenue for the year ended 2009, and 23% and 13%, respectively, for the year ended 2008. A reasonable possibility exists that recorded estimates will change by a material amount in the near term due to interpretation of the complex laws and regulations governing the Medicare and Medicaid programs.

The UIHC provided charity care at established hospital rates for the years ended June 30:

|                       | <u>2009</u>     | <u>2008</u>     |
|-----------------------|-----------------|-----------------|
| Indigent patient care | \$216.6 million | \$177.2 million |
| Other charity care    | \$15.9 million  | \$10.9 million  |

The UIHC annual financial report also includes a section on management's discussion and analysis, which provides an objective analysis of the financial activities of the UIHC based on currently known facts, decisions, and conditions. It is presented to be read in conjunction with the audited financial statements and includes the following sections:

- ◆ Overview of the Financial Statements
- ◆ Overall Financial Position and Operations
- ◆ Debt
- ◆ Net Patient Service Revenue
- ◆ Operating Expenses
- ◆ Transactions with Related Parties
- ◆ Non-operating Revenues and Expenses
- ◆ Contacting UIHC's Financial Management

**Bonds Issued Subsequent to FY 2009**

No SUI Hospital Revenue Bonds have been issued thus far in FY 2009.



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

Financial Statements

June 30, 2009 and 2008

(With Independent Auditors' Report Thereon)



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

## **Independent Auditors' Report**

The Board of Regents  
State of Iowa:

We have audited the accompanying balance sheets of the State University of Iowa, University of Iowa Hospitals and Clinics (UIHC) as of June 30, 2009 and 2008, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of UIHC's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As discussed in note 1 to the financial statements, the financial statements of UIHC are intended to present the financial position and the changes in financial position and cash flows of only that portion of the business-type activities of the State University of Iowa that is attributable to the transactions of UIHC. UIHC is a department of the State University of Iowa for financial reporting purposes. The financial statements of UIHC do not purport to, and do not, present fairly the financial position of the State University of Iowa as of June 30, 2009 and 2008, and the changes in its financial position and its cash flows, for the years then ended, in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State University of Iowa, University of Iowa Hospitals and Clinics as of June 30, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

The accompanying management's discussion and analysis on pages 3 through 8 is not a required part of the basic financial statements of UIHC, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

**KPMG LLP**

Des Moines, Iowa  
December 18, 2009

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

June 30, 2009 and 2008

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, 2009 and 2008. 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.

**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 (balance sheets, statements of revenues, expenses, and changes in net assets, and statements of cash flows) present, on a comparative basis, the financial position of UIHC at June 30, 2009 and 2008 (the end of the fiscal year), and the results of its operations and its financial activities for each of the years then ended. These statements report information about UIHC using accounting methods similar to those used by private sector companies. The balance sheets include all of UIHC's assets and liabilities. The statements of revenues, expenses, and changes in net assets reflect each year's activities on the accrual basis of accounting, i.e., when services are provided or obligations are incurred, not when cash is received or paid. These statements report UIHC's net assets and how they have changed. Net assets (the difference between assets and liabilities) is one way to measure financial health or position. The statements of cash flows provide relevant information about each year's cash receipts and cash payments and classify them as operating, noncapital financing, capital, and related financing and investing activities. The financial statements include notes that explain information in the financial statements and provide more detailed data.

**Overall Financial Position and Operations**

In 2009, UIHC's net assets decreased by \$11.2 million or 1.1% and increased by \$31.6 million or 3.3% in 2008. UIHC reported a decrease in operating income in 2009 and 2008. Operating income in 2009 decreased by \$27.6 million or 146.6% over the operating income reported in 2008. Operating income in 2008 decreased by \$29.9 million or 61.4% over the operating income reported in 2007. Nonoperating revenues decreased by \$16.1 million or 124.8% in 2009 compared to 2008. Nonoperating revenues decreased by \$17.4 million or 57.5% in 2008 compared to 2007.

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Management's Discussion and Analysis

June 30, 2009 and 2008

Table 1 provides a summary of UIHC's assets, liabilities and net assets as of June 30, 2009, 2008, and 2007.

**Table 1**  
**UNIVERSITY OF IOWA HOSPITALS AND CLINICS**

Condensed Balance Sheet Information

(In thousands)

|   | <u>2009</u>         | <u>2008</u>      | <u>2007</u>      |
|---|---------------------|------------------|------------------|
| <b>Assets:</b>                                  |                     |                  |                  |
| Current assets                                  | \$ 261,739          | 249,603          | 227,734          |
| Noncurrent cash and investments                 | 440,088             | 431,925          | 388,265          |
| Capital assets, net                             | 528,100             | 508,652          | 497,645          |
| Other assets                                    | 2,914               | 2,121            | 1,539            |
| Total assets                                    | <u>\$ 1,232,841</u> | <u>1,192,301</u> | <u>1,115,183</u> |
| <b>Liabilities:</b>                             |                     |                  |                  |
| Current liabilities                             | \$ 154,880          | 134,697          | 136,507          |
| Long-term debt                                  | 105,807             | 76,230           | 28,620           |
| Other long-term liabilities                     | 3,571               | 1,619            | 1,877            |
| Total liabilities                               | <u>264,258</u>      | <u>212,546</u>   | <u>167,004</u>   |
| <b>Net assets:</b>                              |                     |                  |                  |
| Invested in capital assets, net of related debt | 427,073             | 436,169          | 470,297          |
| Restricted                                      | 13,333              | 13,291           | 14,322           |
| Unrestricted                                    | 528,177             | 530,295          | 463,560          |
| Total net assets                                | <u>968,583</u>      | <u>979,755</u>   | <u>948,179</u>   |
| Total liabilities and net assets                | <u>\$ 1,232,841</u> | <u>1,192,301</u> | <u>1,115,183</u> |

A significant component of the change in UIHC's assets is the increase in capital assets. During 2009 and 2008, UIHC constructed or purchased \$98.8 million and \$80.7 million, respectively, of capital assets. The major capital asset additions included:

- Emergency Treatment Center Expansion and Renovation
- Pneumatic Tube System Upgrade
- Interventional OR with Angiograph System
- Intermediate Pulmonary Care Unit Relocation and Expansion
- Additional major equipment additions in 2009 consisted of a SOMATOM Definition Dual Source CT Scanner, CT Scanner for the Emergency Treatment Center, Avanto MRI System, Single Axiom Artis DFC Single Plane Fluoroscopy, and an IBM Server P6-9117 MMA.

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Management's Discussion and Analysis

June 30, 2009 and 2008

**Debt**

At June 30, 2009 and 2008, UIHC had \$110.3 and \$79.1 million, respectively, in revenue bonds and capital lease obligations outstanding. During 2009, reductions of long-term debt were \$6.7 million, which included refinancing the \$4.2 million balance of the Series S.U.I. 2000 Telecommunications Facilities Revenue Bonds. In comparison, during 2008, reductions of long-term debt were \$1.5 million. During 2009, UIHC issued \$33.7 million of Series S.U.I. 2009 Hospital Revenue Bonds and \$3.5 million of Series S.U.I. 2008 Telecommunications Facilities Revenue Bonds to refinance the Series S.U.I. 2000 Telecommunications Facilities Revenue Bonds.

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Management's Discussion and Analysis

June 30, 2009 and 2008

Table 2 shows the changes in net assets for 2009 compared to 2008 and 2007.

**Table 2**

**UNIVERSITY OF IOWA HOSPITALS AND CLINICS**

Condensed Revenues, Expenses, and Changes in Net Assets Information

(In thousands)

|  | <u>2009</u>       | <u>2008</u>    | <u>2007</u>    |
|--|-------------------|----------------|----------------|
| Operating revenues:                                  |                   |                |                |
| Net patient service revenue                          | \$ 883,417        | 826,362        | 776,023        |
| Other revenue  | 44,777            | 44,810         | 38,670         |
| Total operating revenues                             | <u>928,194</u>    | <u>871,172</u> | <u>814,693</u> |
| Operating expenses:                                  |                   |                |                |
| Salaries and benefits                                | 501,040           | 451,927        | 403,955        |
| Medical supplies and drugs                           | 185,722           | 172,265        | 157,230        |
| Other supplies and general expenses                  | 177,217           | 160,032        | 147,603        |
| Depreciation and amortization                        | 72,975            | 68,140         | 57,168         |
| Total operating expenses                             | <u>936,954</u>    | <u>852,364</u> | <u>765,956</u> |
| Operating (loss) income                              | (8,760)           | 18,808         | 48,737         |
| Nonoperating revenues (expenses):                    |                   |                |                |
| Loss on disposal of capital assets                   | (6,312)           | (1,341)        | (1,701)        |
| Noncapital grants and contributions                  | 3,189             | 1,942          | 4,969          |
| Investment income                                    | 3,315             | 13,753         | 27,104         |
| Interest expense                                     | (3,392)           | (1,440)        | (12)           |
| Total nonoperating revenues,<br>(expenses) net       | <u>(3,200)</u>    | <u>12,914</u>  | <u>30,360</u>  |
| Excess of revenues over<br>expenses before transfers | (11,960)          | 31,722         | 79,097         |
| Net transfers in (out)                               | 788               | (145)          | (75)           |
| Increase (decrease) in net assets                    | (11,172)          | 31,577         | 79,022         |
| Net assets, beginning of year                        | <u>979,756</u>    | <u>948,179</u> | <u>869,157</u> |
| Net assets, end of year                              | <u>\$ 968,584</u> | <u>979,756</u> | <u>948,179</u> |

**Net Patient Service Revenue**

Net patient service revenue increased from 2008 to 2009 by \$57.1 million or 6.9% and \$50.3 million or 6.5% from 2007 to 2008. The increases in net patient service revenue were driven by both increases in patient volumes and pricing increases during the same periods. During 2009, acute admissions increased by 193 or 0.7% from

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Management's Discussion and Analysis

June 30, 2009 and 2008

29,349 to 29,542 admissions. UIHC experienced increases in outpatient services during both years. During 2008, acute admissions increased 1,520 or 5.5% from 27,829 to 29,349 admissions.

The State of Iowa (the State) has annually provided funding to UIHC to care for certain uninsured or underinsured individuals, as well as to provide psychiatric services and services to children with disabilities. This funding also helps to assure that a sufficient patient base exists at UIHC to support health professionals' education. Effective July 1, 2005, the state-sponsored indigent care program ended and was replaced with a new Medicaid waiver demonstration program titled "IowaCare." The IowaCare program is approved by the Centers for Medicare and Medicaid Services for a five-year period from July 1, 2005 through June 30, 2010. Appropriations received for these programs in 2009 and 2008 were \$70.1 million and \$59.7 million, respectively. Services provided by UIHC under its charity care programs, measured at established hospital rates, were \$216.6 million and \$177.2 million in 2009 and 2008, respectively. The State is currently in negotiations with the Centers for Medicare and Medicaid Services (CMS) to renew the IowaCare waiver.

The provision for bad debts (a deduction from gross patient charges) decreased \$1.9 million from \$29.4 million in 2008 to \$27.5 million in 2009. The provision for bad debts (a deduction from gross patient charges) increased \$7.5 million from \$21.9 million in 2007 to \$29.4 million in 2008.

### **Operating Expenses**

Total operating expenses increased 9.9% from \$852.4 million in 2008 to \$937.0 million in 2009 and 11.3% from \$766.0 million in 2007 to \$852.4 million in 2008. The largest increases in expenses during these years are attributed to salaries and benefits, medical supplies and drugs, and depreciation.

### **Transactions with Related Parties**

UIHC purchases certain administrative and supervisory services, utilities, and other general services from the State University of Iowa (University). These services are purchased at the approximate cost incurred by the servicing unit. For the years ended June 30, 2009, 2008, and 2007, UIHC expensed approximately \$122.5 million, \$105.2 million, and \$98.8 million, respectively, for these administrative services, utilities, and other services and support requirements.

UIHC also provides certain administrative services to units of the University, particularly to the Roy J. and Lucille A. Carver College of Medicine (College of Medicine). These services include billing, collection, and other physician practice-related clinic overhead expenses. For the years ended June 30, 2009, 2008, and 2007, UIHC received revenue from these units of approximately \$29.0 million, \$28.9 million, and \$27.7 million, respectively, for these services.

UIHC and the College of Medicine have formed a nonprofit corporation, University of Iowa Health System (UIHS), to enhance and support the educational missions of UIHC and the College of Medicine, particularly as these missions apply to clinical activities and statewide and multi-state network development activities. UIHC paid UIHS for certain administrative and other general services in the amount of \$0.9 million, \$1.2 million, and \$0.8 million for the years ended June 30, 2009, 2008, and 2007, respectively.

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Management's Discussion and Analysis

June 30, 2009 and 2008

**Nonoperating Revenues and Expenses**

Nonoperating revenues consist primarily of loss on disposals of capital assets, investment income, and noncapital grants and contributions. Investment income decreased from 2008 to 2009 by \$10.4 million or 75.9% and decreased from 2007 to 2008 by \$13.4 million or 49.4%. During 2009, UIHC recorded overall earnings on the endowment and operating pools of \$6.9 million and a net unrealized loss on investments of \$3.6 million, which decreased investment income accordingly. This compares to the overall earnings on the endowment and operating pools of \$22.8 million and a net unrealized loss of \$9.1 million in the previous year.

**Contacting UIHC's Financial Management**

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

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

Balance Sheets

June 30, 2009 and 2008

| <b>Assets</b>   | <b>2009</b>      | <b>2008</b>   |
|---|------------------|---------------|
| Current assets:   |                  |               |
| Cash and cash equivalents   | \$ 737,425       | 610,197       |
| Short-term investments  | 81,841,579       | 80,560,479    |
| Patient accounts receivable, net of estimated uncollectibles<br>\$21,360,139 in 2009 and \$19,069,133 in 2008 | 130,912,741      | 122,386,095   |
| Accounts receivable managed for the College of Medicine   | 17,923,209       | 12,470,762    |
| Inventories   | 20,573,605       | 20,443,440    |
| Current portion of debt service funds   | 1,030,729        | 1,056,089     |
| Other current assets  | 8,719,327        | 12,075,962    |
| Total current assets  | 261,738,615      | 249,603,024   |
| Noncurrent cash and investments:  |                  |               |
| Designated by the Board of Regents  | 418,475,325      | 413,037,098   |
| Held by trustee for debt service  | 9,309,934        | 6,653,231     |
| Restricted by contributors and grantors for capital acquisitions<br>and research                              | 12,302,640       | 12,234,919    |
|   | 440,087,899      | 431,925,248   |
| Capital assets, net   | 528,100,503      | 508,651,988   |
| Other assets  | 2,914,408        | 2,120,662     |
| Total assets  | \$ 1,232,841,425 | 1,192,300,922 |
| <b>Liabilities and Net Assets</b>   |                  |               |
| Current liabilities:  |                  |               |
| Current maturities of long-term debt and capital lease obligation   | \$ 4,530,288     | 2,906,453     |
| Accounts payable and accrued expenses   | 103,054,152      | 99,706,257    |
| Estimated third-party payor settlements   | 17,992,560       | 10,104,126    |
| Due to related parties  | 21,498,908       | 15,784,049    |
| Other current liabilities   | 5,667,726        | 4,940,818     |
| Accrued interest  | 2,136,585        | 1,255,094     |
| Total current liabilities   | 154,880,219      | 134,696,797   |
| Long-term debt and capital lease obligation, net of current maturities  | 105,807,174      | 76,229,875    |
| Other long-term liabilities   | 3,570,527        | 1,618,855     |
| Total liabilities   | 264,257,920      | 212,545,527   |
| Net assets:   |                  |               |
| Invested in capital assets, net of related debt   | 427,072,975      | 436,168,891   |
| Restricted by donors for specific purposes  | 12,302,640       | 12,234,919    |
| Restricted for debt service   | 1,030,729        | 1,056,089     |
| Unrestricted  | 528,177,161      | 530,295,496   |
| Total net assets  | 968,583,505      | 979,755,395   |
| Total liabilities and net assets  | \$ 1,232,841,425 | 1,192,300,922 |

See accompanying notes to financial statements.

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

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2009 and 2008

|   | <b>2009</b>    | <b>2008</b> |
|---|----------------|-------------|
| Operating revenues:   |                |             |
| Net patient service revenue, net of provision for bad debts of<br>\$27,512,826 in 2009 and \$29,369,045 in 2008 | \$ 883,416,576 | 826,362,577 |
| Other revenue   | 44,776,895     | 44,810,153  |
| Total operating revenues  | 928,193,471    | 871,172,730 |
| Operating expenses:   |                |             |
| Salaries and benefits   | 501,039,937    | 451,926,998 |
| Medical supplies and drugs  | 185,722,090    | 172,264,882 |
| Other supplies and general expenses   | 177,216,919    | 160,032,622 |
| Depreciation and amortization   | 72,974,749     | 68,140,792  |
| Total operating expenses  | 936,953,695    | 852,365,294 |
| Operating (loss) income   | (8,760,224)    | 18,807,436  |
| Nonoperating revenues (expenses):   |                |             |
| Loss on disposal of capital assets  | (6,311,918)    | (1,340,512) |
| Noncapital grants and contributions   | 3,189,117      | 1,941,363   |
| Investment income   | 3,315,242      | 13,752,929  |
| Interest expense  | (3,392,141)    | (1,439,768) |
| Total nonoperating (expenses) revenues, net   | (3,199,700)    | 12,914,012  |
| Excess (deficiency) of revenues over expenses<br>before transfers   | (11,959,924)   | 31,721,448  |
| Net transfers in (out)  | 788,034        | (145,170)   |
| (Decrease) increase in net assets   | (11,171,890)   | 31,576,278  |
| Net assets, beginning of year   | 979,755,395    | 948,179,117 |
| Net assets, end of year   | \$ 968,583,505 | 979,755,395 |

See accompanying notes to financial statements.

**STATE UNIVERSITY OF IOWA,  
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Statements of Cash Flows

Years ended June 30, 2009 and 2008

|  | <b>2009</b>    | <b>2008</b>   |
|--|----------------|---------------|
| Cash flows from operating activities:  |                |               |
| Receipts from and on behalf of patients  | \$ 875,938,623 | 801,370,595   |
| Receipts from state grants   | 6,839,740      | 6,726,227     |
| Other receipts and payments, net   | 45,039,308     | 36,247,205    |
| Payments to employees  | (465,626,937)  | (444,402,454) |
| Payment to suppliers and contractors   | (389,531,843)  | (332,749,878) |
| Net cash provided by operating activities  | 72,658,891     | 67,191,695    |
| Cash flows from noncapital financing activities:   |                |               |
| Net transfers  | 788,034        | (145,170)     |
| Noncapital grants and contributions  | 3,189,117      | 1,941,363     |
| Net cash provided by noncapital financing activities   | 3,977,151      | 1,796,193     |
| Cash flows from capital and related financing activities:                                      |                |               |
| Purchase of capital assets   | (98,703,935)   | (80,311,271)  |
| Proceeds from the sale of capital assets   | 11,749         | 11,000        |
| Proceeds from the issuance of long-term debt   | 37,235,145     | 50,000,000    |
| Premium received on issuance of long-term debt   | 621,931        | 435,672       |
| Principal paid on long-term debt   | (6,674,877)    | (1,535,350)   |
| Interest paid on long-term debt  | (2,546,459)    | (713,612)     |
| Net cash used in capital and related financing activities                                      | (70,056,446)   | (32,113,561)  |
| Cash flows from investing activities:  |                |               |
| Proceeds from sale of investments  | 86,602,925     | 18,293,011    |
| Purchase of investments  | (101,023,405)  | (78,583,185)  |
| Interest and dividends received on investments   | 7,968,112      | 23,507,194    |
| Net cash used in investing activities  | (6,452,368)    | (36,782,980)  |
| Net increase in cash and cash equivalents  | 127,228        | 91,347        |
| Cash and cash equivalents at beginning of year   | 610,197        | 518,850       |
| Cash and cash equivalents at end of year   | \$ 737,425     | 610,197       |
| Reconciliation of operating income to net cash provided by operating activities:               |                |               |
| Operating (loss) income  | \$ (8,760,224) | 18,807,436    |
| Adjustments to reconcile operating (loss) income to net cash provided by operating activities: |                |               |
| Depreciation and amortization  | 72,974,749     | 68,140,792    |
| Provision for bad debts  | 27,512,826     | 29,369,045    |
| Change in assets and liabilities:  |                |               |
| Accounts receivable  | (41,491,919)   | (39,845,799)  |
| Inventories  | (130,165)      | (1,614,977)   |
| Other assets   | 2,923,856      | (3,380,787)   |
| Accounts payable and accrued expenses  | 3,347,895      | 11,519,815    |
| Other liabilities  | 2,678,580      | 548,120       |
| Due to related parties   | 5,714,859      | (10,621,851)  |
| Estimated third-party payor settlements  | 7,888,434      | (5,730,099)   |
| Net cash provided by operating activities  | \$ 72,658,891  | 67,191,695    |

Noncash investing activities:

UIHC held cash and investments at June 30, 2009 and 2008 with a fair value of \$524,058,599 and \$514,152,013, respectively.

During 2009 and 2008, the net (decrease) increase in fair value of these investments was (\$3,589,643) and (\$9,136,676), respectively.

See accompanying notes to financial statements.

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**(1) Summary of Significant Accounting Policies and Related Matters**

**(a) Reporting Entity**

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

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

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

**(b) Basis of Presentation**

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

**(c) Use of Estimates**

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

**(d) Cash and Investments**

Cash and investments of UIHC include specific investments and other cash and investments that are pooled with the cash and investments of the University and held in the name of the University. UIHC's share of pooled investments and income thereon are determined on a pro rata basis reflecting UIHC's amounts available for investment as compared with the amounts for the overall University.

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Undesignated cash equivalents totaling \$737,425 and \$610,197 at June 30, 2009 and 2008, respectively, represent money market funds and other short-term investments that mature in three months or less from date of purchase.

**(e) Inventories**

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

**(f) Capital Assets**

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

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

**(g) Costs of Borrowing**

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

**(h) Grants and Contributions**

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

**(i) Restricted Resources**

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

**(j) Net Assets**

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

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are remaining net assets that do not meet the definition of invested in capital assets net of related debt or restricted.

**(k) *Operating Revenues and Expenses***

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

**(l) *Net Patient Service Revenue***

UIHC has agreements with third-party payors that provide for payments to UIHC at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

**(m) *Charity Care***

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

**(n) *Compensated Absences***

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

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

**(o) *Income Taxes***

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

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**(2) Deposits and Investments**

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

UIHC's cash and investments include specific investments and amounts pooled with cash and investments of the University and held in the University's name. UIHC's cash deposits at June 30, 2009 and 2008 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. Chapter 12C provides for additional assessments against the depositories of the pool to ensure that there will be no loss of public funds.

Noncurrent cash and investments limited by bond resolutions or designated by the Board were held for the following purposes at June 30, 2009 and 2008:

|  | <b>2009</b>    | <b>2008</b> |
|--|----------------|-------------|
| Limited by bond resolutions:                                     |                |             |
| Debt service reserve   | \$ 9,309,934   | 6,653,231   |
| Designated by the Board of Regents:                              |                |             |
| Capital projects and equipment and other needs                   | 4,521,869      | 4,308,635   |
| Surplus  | 2,746,601      | 610,619     |
| Improvement, extension, repair, operation, and maintenance funds | 411,206,855    | 408,117,844 |
| Restricted by donors   | 12,302,640     | 12,234,919  |
|  | \$ 440,087,899 | 431,925,248 |

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

Cash and cash equivalents and short-term investments specifically identified or pooled with the cash and investments of the University totaled \$82,579,004 and \$81,170,676 at June 30, 2009 and 2008, respectively. Cash equivalents designated by the Board totaled \$181,995,849 and \$138,263,607 at June 30, 2009 and 2008, respectively.

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UIHC's investments are recorded at fair value, as determined by quoted market price. As of June 30, 2009, UIHC had the following investments and quality credit ratings:

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

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As of June 30, 2008, UIHC had the following investments and quality credit ratings:

|  | <u>Fair market<br/>value</u> | <u>Effective<br/>duration</u> | <u>Quality<br/>rating</u> |
|--|------------------------------|-------------------------------|---------------------------|
| University of Iowa Long-Term Endowment Pool:               |                              |                               |                           |
| Cash and cash equivalents                                  | \$ 1,796,354                 | NA                            | NA                        |
| U.S. obligations   | 6,879                        | 15.88                         | NA                        |
| Agency securities  | 422,951                      | 2.41                          | NR                        |
| Corporate issuance   | 2,608,413                    | 3.84                          | AA                        |
| Mortgage-backed securities                                 | 2,055,889                    | 5.22                          | NR                        |
| Mutual funds – fixed income                                | 7,621,116                    | 3.71                          | BBB+                      |
| Mutual funds – U.S. equity                                 | 18,477,804                   | NA                            | NA                        |
| Mutual funds – international equity                        | 6,745,568                    | NA                            | NA                        |
| Mutual funds – real estate                                 | 2,620,755                    | NA                            | NA                        |
| Subtotal   | <u>42,355,729</u>            |                               |                           |
| University of Iowa Intermediate (Quasi II) Endowment Pool: |                              |                               |                           |
| Cash and cash equivalents                                  | 9,712,975                    | NA                            | NA                        |
| U.S. obligations   | 30,564                       | 15.88                         | NA                        |
| Agency securities  | 1,779,247                    | 2.41                          | NR                        |
| Corporate issuance   | 10,861,050                   | 3.81                          | AA                        |
| Mortgage-backed securities                                 | 8,570,951                    | 5.22                          | NR                        |
| Mutual funds – fixed income                                | 30,196,524                   | 4.16                          | A+                        |
| Subtotal   | <u>61,151,311</u>            |                               |                           |
| University of Iowa Operating Investment Pool:              |                              |                               |                           |
| Cash and cash equivalents                                  | 206,147,323                  | NA                            | NA                        |
| U.S. obligations   | 8,067,879                    | 3.96                          | NA                        |
| Agency securities  | 41,212,193                   | 1.85                          | NR                        |
| Corporate issuance   | 110,085,067                  | 1.96                          | AA+                       |
| Mortgage-backed securities                                 | 18,389,175                   | 2.17                          | NR                        |
| Mutual funds – fixed income                                | 26,743,336                   | 1.90                          | AA+                       |
| Subtotal   | <u>410,644,973</u>           |                               |                           |
| Total investments  | <u>\$ 514,152,013</u>        |                               |                           |

**Interest Rate Risk** – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. This risk is measured using effective duration. The maximum duration of the University’s unrestricted operating portfolio may not exceed the duration of the Merrill 1-3 year Government/Corporate Index by more than 20%. At time of purchase, the effective maturity of securities in the operating portfolio cannot exceed sixty-three months. There is no explicit limit on the average

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maturity of fixed income securities in the endowment portfolios. Each fixed income portfolio is managed to an appropriate benchmark.

**Credit Risk** – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation to the University. The University manages exposure to credit risk by measuring portfolios against benchmarks as established by the Board of Regents. As of June 30, 2009, the operating portfolio benchmark is AAA and the endowment portfolios benchmark is AA1.

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

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

**(3) Capital Assets**

Capital assets at June 30, 2009 and 2008 are summarized as follows:

|   | <u>2009</u>           | <u>2008</u>          |
|---|-----------------------|----------------------|
| Land improvements                         | \$ 782,080            | 741,775              |
| Infrastructure                            | 40,538,941            | 40,487,990           |
| Buildings and leasehold improvements      | 693,912,097           | 638,562,709          |
| Equipment                                 | 310,205,207           | 287,801,234          |
| Software                                  | 69,649,103            | 34,733,843           |
| Construction in progress (nondepreciable) | 29,746,213            | 63,211,532           |
|   | <u>1,144,833,641</u>  | <u>1,065,539,083</u> |
| Less accumulated depreciation             | <u>616,733,138</u>    | <u>556,887,095</u>   |
|   | <u>\$ 528,100,503</u> | <u>508,651,988</u>   |

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Capital asset additions, retirements, and balances for the years ended June 30, 2009 and 2008 were as follows:

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

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| <u>Cost basis summary</u>                    | <u>June 30,<br/>2007<br/>balances</u> | <u>Acquisitions</u>             | <u>Sales<br/>retirements<br/>and transfers</u> | <u>June 30,<br/>2008<br/>balances</u> |
|--|---------------------------------------|---------------------------------|--|---------------------------------------|
| Land improvements                            | \$ 733,795                            | 7,980                           | —  | 741,775                               |
| Infrastructure                               | 38,742,122                            | 1,745,868                       | —  | 40,487,990                            |
| Buildings and leasehold<br>improvements      | 618,748,088                           | 19,814,621                      | —  | 638,562,709                           |
| Equipment and software                       | 298,615,258                           | 42,539,851                      | (18,620,032)                                   | 322,535,077                           |
| Construction in progress<br>(nondepreciable) | 46,605,771                            | 16,605,761                      | —  | 63,211,532                            |
| Total at historical<br>cost                  | <u>1,003,445,034</u>                  | <u>80,714,081</u>               | <u>(18,620,032)</u>                            | <u>1,065,539,083</u>                  |
|  | <u>June 30,<br/>2007<br/>balances</u> | <u>Depreciation<br/>expense</u> | <u>Sales<br/>retirements<br/>and transfers</u> | <u>June 30,<br/>2008<br/>balances</u> |
| Less accumulated depreciation for:           |                                       |                                 |  |                                       |
| Land improvements                            | 733,794                               | 133                             | —  | 733,927                               |
| Infrastructure                               | 29,077,203                            | 2,246,173                       | —  | 31,323,376                            |
| Buildings and leasehold<br>improvements      | 323,254,485                           | 29,467,366                      | (1,383)  | 352,720,468                           |
| Equipment and software                       | 152,734,131                           | 36,427,120                      | (17,051,927)                                   | 172,109,324                           |
| Total accumulated<br>depreciation            | <u>505,799,613</u>                    | <u>68,140,792</u>               | <u>(17,053,310)</u>                            | <u>556,887,095</u>                    |
| Total capital assets,<br>net                 | <u>\$ 497,645,421</u>                 | <u>12,573,289</u>               | <u>(1,566,722)</u>                             | <u>508,651,988</u>                    |

At June 30, 2009, construction in progress related to various projects throughout the UIHC. The estimated cost to complete the current phase of equipment and projects under construction at June 30, 2009 is \$25.6 million. Other projects at June 30, 2009, with an estimated cost of \$255.9 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, 2009 and 2008 were \$977,141 and \$1,913,355, respectively.

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**(4) Long-Term Debt**

Long-term debt outstanding at June 30, 2009 and 2008 was as follows:

|  | <u>2009</u>           | <u>2008</u>       |
|--|-----------------------|-------------------|
| Hospital Revenue Bonds:  |                       |                   |
| Series 2002 – 4.125% to 5.000%; maturing serially on<br>September 1 through 2028         | \$ 21,950,000         | 22,615,000        |
| Series S.U.I. 2007 – 4.375% to 5.500%; maturing<br>serially on September 1 through 2027  | 24,375,000            | 25,000,000        |
| Series S.U.I. 2007A – 4.000% to 5.500%; maturing<br>serially on September 1 through 2027 | 24,225,000            | 25,000,000        |
| Series S.U.I. 2009 – 5.500% to 6.125%; maturing<br>serially on September 1 through 2028  | 33,750,000            | —                 |
| Net unamortized premium on Hospital Revenue Bonds  | 1,002,084             | 415,962           |
| Telecommunications Facilities Revenue Bonds:   |                       |                   |
| Series S.U.I. 2000 – 4.900% to 5.400%; refinanced<br>on July 2008                        | —                     | 4,194,060         |
| Series S.U.I. 2003 – 2.600% to 3.800%; maturing<br>serially on July 1 through 2013       | 1,309,350             | 1,651,650         |
| Series S.U.I. 2008 – 5.000% to 5.400%; maturing<br>serially on July 1 through 2015       | 3,485,145             | —                 |
| Total long-term debt   | <u>110,096,579</u>    | <u>78,876,672</u> |
| Capital lease obligations (net book value of \$220,497)                                  | 240,883               | 259,656           |
|  | <u>110,337,462</u>    | <u>79,136,328</u> |
| Long-term debt, current portion  | 4,530,288             | 2,906,453         |
|  | <u>\$ 105,807,174</u> | <u>76,229,875</u> |

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Activity in long-term debt for the years ended June 30, 2009 and 2008 was as follows:

|   | <b>June 30,<br/>2008<br/>balance</b> | <b>Additions</b>  | <b>Reductions</b>  | <b>June 30,<br/>2009<br/>balance</b> | <b>Amounts<br/>due within<br/>one year</b> |
|---|--------------------------------------|-------------------|--------------------|--------------------------------------|--|
| Hospital Revenue Bonds,<br>Series 2002          | \$ 22,615,000                        | —                 | (665,000)          | 21,950,000                           | 690,000                                    |
| Hospital Revenue Bonds,<br>Series 2007          | 25,000,000                           | —                 | (625,000)          | 24,375,000                           | 825,000                                    |
| Hospital Revenue Bonds,<br>Series 2007A         | 25,000,000                           | —                 | (775,000)          | 24,225,000                           | 800,000                                    |
| Hospital Revenue Bonds,<br>Series 2009          | —                                    | 33,750,000        | —                  | 33,750,000                           | 1,300,000                                  |
| Net unamortized bond premium                    | 415,962                              | 621,931           | (35,809)           | 1,002,084                            | —  |
| Telecommunications Facilities<br>Revenue Bonds: |                                      |                   |                    |                                      |  |
| Series, 2000                                    | 4,194,060                            | —                 | (4,194,060)        | —                                    | —  |
| Series, 2003                                    | 1,651,650                            | —                 | (342,300)          | 1,309,350                            | 351,750                                    |
| Series, 2008                                    | —                                    | 3,485,145         | —                  | 3,485,145                            | 488,175                                    |
| Total long-term debt                            | 78,876,672                           | 37,857,076        | (6,637,169)        | 110,096,579                          | 4,454,925                                  |
| Capital lease obligations                       | 259,656                              | 54,744            | (73,517)           | 240,883                              | 75,363                                     |
|   | <u>\$ 79,136,328</u>                 | <u>37,911,820</u> | <u>(6,710,686)</u> | <u>110,337,462</u>                   | <u>4,530,288</u>                           |
|   |                                      |                   |                    |                                      |  |
|   | <b>June 30,<br/>2007<br/>balance</b> | <b>Additions</b>  | <b>Reductions</b>  | <b>June 30,<br/>2008<br/>balance</b> | <b>Amounts<br/>due within<br/>one year</b> |
| Hospital Revenue Bonds,<br>Series 1983          | \$ 5,000                             | —                 | (5,000)            | —                                    | —  |
| Hospital Revenue Bonds,<br>Series 2002          | 23,250,000                           | —                 | (635,000)          | 22,615,000                           | 665,000                                    |
| Hospital Revenue Bonds,<br>Series 2007          | —                                    | 25,000,000        | —                  | 25,000,000                           | 625,000                                    |
| Hospital Revenue Bonds,<br>Series 2007A         | —                                    | 25,000,000        | —                  | 25,000,000                           | 775,000                                    |
| Net unamortized bond premium                    | —                                    | 435,672           | (19,710)           | 415,962                              | —  |
| Telecommunications Facilities<br>Revenue Bonds: |                                      |                   |                    |                                      |  |
| Series, 2000                                    | 4,610,070                            | —                 | (416,010)          | 4,194,060                            | 435,113                                    |
| Series, 2003                                    | 1,986,600                            | —                 | (334,950)          | 1,651,650                            | 342,300                                    |
| Total long-term debt                            | 29,851,670                           | 50,435,672        | (1,410,670)        | 78,876,672                           | 2,842,413                                  |
| Capital lease obligations                       | 205,446                              | 198,600           | (144,390)          | 259,656                              | 64,040                                     |
|   | <u>\$ 30,057,116</u>                 | <u>50,634,272</u> | <u>(1,555,060)</u> | <u>79,136,328</u>                    | <u>2,906,453</u>                           |

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The Hospital Revenue Bonds are special obligations of the Board of Regents payable solely out of Hospital Income, the general purpose of which is to expand and improve UIHC facilities. "Hospital Income" is defined as the gross income and funds received by the Hospital System, including the proceeds of rates, fees, charges, and payments for healthcare provider activities for patient care services rendered by the University's hospitals, clinics, laboratories, and ancillary facilities after deduction of current expenses. Hospital Income does not include State appropriations to the University or Hospital System. So long as the bonds or parity bonds remain outstanding, the entire Hospital System income and revenues shall be deposited to the revenue fund and shall be disbursed to the following funds in the following order: (1) the operation and maintenance fund, (2) the sinking fund, (3) the reserve fund, and (4) the system fund. The reserve fund requirement is at least equal to the maximum annual amount of the principal and interest coming due on the bonds and any parity bonds, or \$8,652,219. The maximum amount of Hospital Income pledged representing the undiscounted principal and interest on the bonds is \$169,197,666.

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

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

|                      | <u>Principal</u>      | <u>Interest</u>   |
|----------------------|-----------------------|-------------------|
| Year ending June 30: |                       |                   |
| 2010                 | \$ 4,454,925          | 5,589,253         |
| 2011                 | 4,371,650             | 5,068,431         |
| 2012                 | 4,576,985             | 4,871,193         |
| 2013                 | 4,512,265             | 4,670,251         |
| 2014                 | 4,713,445             | 4,464,672         |
| 2015 through 2019    | 24,090,225            | 18,870,321        |
| 2020 through 2024    | 29,260,000            | 12,408,237        |
| 2025 through 2029    | 33,115,000            | 4,160,813         |
|                      | <u>\$ 109,094,495</u> | <u>60,103,171</u> |

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***Capital Lease Obligations***

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

|                                    |    |         |  |
|------------------------------------|----|---------|--|
| Year ending June 30:               |    |         |  |
| 2010                               | \$ | 94,849  |  |
| 2011                               |    | 89,998  |  |
| 2012                               |    | 58,130  |  |
| 2013                               |    | 29,230  |  |
| 2014                               |    | 11,205  |  |
| Total minimum payments<br>required |    | 283,412 |  |
| Less amounts representing interest |    | 42,529  |  |
|                                    | \$ | 240,883 |  |

**(5) Retirement Benefit Plans**

Substantially all UIHC employees meeting eligibility requirements participate in the University of Iowa Retirement Plan (the Plan). The Plan is a defined contribution retirement plan providing benefits through the Teachers Insurance and Annuity Association and the College Retirement Equity Fund (TIAA-CREF). UIHC contributions to the Plan are 10% of employee compensation after the first five years of employment. During the first five years of employment, UIHC's contribution is 6.67% of the first \$4,800 of compensation and 10.00% of the balance of employee compensation. Employees are required to contribute an amount equal to 50.00% of UIHC's contribution. All contributions to the Plan are immediately 100% vested.

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

The University internally accounts for employee benefits using a benefits pool. Each department, including UIHC, is assessed a total amount to be paid into the pool covering all employee benefits, which approximated \$30.2 million and \$27.4 million for contributions to TIAA-CREF and IPERS in 2009 and 2008, respectively.

**(6) Health Insurance Benefits for Retirees**

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

All UIHC employees meeting eligibility requirements participate in the University of Iowa Health Insurance Benefits for Retirees. The University of Iowa's defined benefit postemployment healthcare plan provides medical and dental benefits to eligible retired employees, which include employees who retire

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from the University after attaining age 55 and before reaching age 62, or who retire after attaining age 62 with ten or more years of service.

The contribution requirements of plan members and the University are established and may be amended by the Board of Regents. The terms and conditions governing the postemployment benefits to which employees are entitled are in the sole authority and discretion of the University's Board of Regents. For fiscal year 2009 and 2008, UIHC's allocated annual OPEB cost was \$4.7 million and \$3.8 million, respectively, of which \$2.2 million was contributed to the plan each year. The net allocated OPEB obligation at June 30, 2009 and 2008 was \$4.4 million and \$1.6 million, respectively. Although there is no requirement to fund the OPEB liability, the University has chosen to fund it on a "pay as you go" basis. University Policy dictates the payment of retiree claims as they become due. Plan members receiving benefits contributed 55% of the premium costs. In fiscal year 2009 and 2008, total member contributions were \$2.6 million and \$2 million, respectively.

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

**(7) Risk Management**

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

UIHC's portion of the health insurance liability, which is included in accounts payable and accrued expenses, is \$3,631,515 and \$3,761,143 as of June 30, 2009 and 2008, respectively, as follows:

|   |    | <u>2009</u>         | <u>2008</u>         |
|---|----|---------------------|---------------------|
| Liability for unpaid healthcare claims at beginning of year | \$ | 3,761,143           | 3,313,891           |
| Healthcare expenses incurred during the year                |    | 40,862,825          | 38,432,936          |
| Healthcare payments to the University during the year       |    | <u>(40,992,453)</u> | <u>(37,985,684)</u> |
| Liability for unpaid healthcare claims at end of year       | \$ | <u>3,631,515</u>    | <u>3,761,143</u>    |

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

The State Appeals Board, subject to the advice and approval of the Attorney General, is authorized to settle tort claims against the State of Iowa as set forth in Chapter 669 of the Code of Iowa. Tort liability claims settled in excess of \$5,000 must have the unanimous approval of all the members of the State Appeals Board, the State Attorney General, and the District Court of the State of Iowa for Polk County. By interagency agreement, tort liability claims (including professional liability) under \$5,000 may be

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administered by the University, subject to a maximum expenditure of \$100,000 per year. All other tort claims are paid from the State of Iowa's general fund and are not an obligation of UIHC.

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

**(8) Transactions with Related Parties**

UIHC receives certain administrative services, utilities, and other general services from the University. The services and support costs include amounts due to the University's Carver College of Medicine for support of graduate medical education, specific clinical services, and other services. These services are charged to UIHC at the approximate cost incurred by the servicing unit. For the years ended June 30, 2009 and 2008, UIHC expensed approximately \$122.5 million and \$105.2 million, respectively, for these administrative services, utilities, and other services and support requirements. At June 30, 2009 and 2008, approximately \$1.1 million and \$0.9 million, respectively, was due to the Carver College of Medicine for services and support.

UIHC also provides certain administrative services to units of the University. These services include billing, collection, and other physician practice-related clinic overhead expenses. These services are charged to units of the University at the approximate cost incurred by the servicing unit. For the years ended June 30, 2009 and 2008, UIHC received revenue from these units of approximately \$29.0 million and \$28.9 million, respectively, for these services.

UIHC and the College of Medicine have formed a nonprofit corporation, University of Iowa Health System (UIHS), to enhance and support the educational missions of the UIHC and the College of Medicine, particularly as these missions apply to clinical activities and statewide and multi-state network development activities. UIHC paid UIHS for certain administrative and other general services in the amount of \$0.9 million and \$1.2 million for the years ended June 30, 2009 and 2008, respectively.

The Faculty Practice Plan (the Practice Plan) is a clinical component of the University's College of Medicine. The UIHC performs billing and collection services for the Practice Plan. At June 30, 2009 and 2008, accounts receivable outstanding for the Practice Plan was \$17,923,209 and \$12,470,762, respectively. These amounts are also included in due to related parties at June 30, 2009 and 2008.

**(9) Net Patient Service Revenue**

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

**Medicare**

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

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**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 24% and 13%, respectively, of UIHC's net patient revenue for the year ended 2009, and 23% and 13%, respectively, of UIHC's net patient revenue for the year ended 2008. 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 2009 and 2008 net patient service revenue decreased approximately \$2.2 million and \$6.4 million, respectively, due to prior year retroactive adjustments in excess of amounts previously estimated.

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

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

|   | <b>2009</b>      | <b>2008</b>   |
|---|------------------|---------------|
| Gross patient charges:                                  |                  |               |
| Inpatient charges                                       | \$ 1,115,977,290 | 991,691,988   |
| Outpatient charges                                      | 872,887,178      | 753,173,887   |
| Total gross patient charges                             | 1,988,864,468    | 1,744,865,875 |
| Less:   |                  |               |
| Deductions from gross patient charges:                  |                  |               |
| Contractual adjustments – Medicare, Medicaid, and other | 1,105,447,892    | 918,503,298   |
| Net patient service revenue                             | \$ 883,416,576   | 826,362,577   |

Included in net patient service revenue are certain amounts received from the State of Iowa in support of indigent care. State reimbursements are received annually to provide acute patient care, psychiatric, and developmental patient care services to patients. Patients are referred from a variety of sources, such as their home county, state institutions, and school districts. For the years ended June 30, 2009 and 2008, amounts received from the State of Iowa were \$70.1 million and \$59.7 million, respectively.

**(10) Charity Care**

The State of Iowa has made annual appropriations to UIHC to care for certain uninsured or underinsured individuals, as well as to provide psychiatric services and services to children with disabilities. This funding also helps to assure that a sufficient patient base exists at UIHC to support health professionals' education and provides partial funding of charges foregone related to these services. The amount of

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charges foregone for services and supplies furnished under UIHC's charity policy aggregated to \$232.5 million and \$188.1 million for 2009 and 2008, respectively.

**(11) Disclosures about the Fair Value of Financial Instruments**

Financial instruments are described as cash, contractual obligations, or rights to pay or receive cash. The fair value for certain financial instruments approximates the carrying value because of the short-term maturity of those instruments, which include receivables, accounts payable, accrued liabilities, estimated settlements to third-party payors, and other current liabilities.

Investments are recorded at fair value. The estimated fair value of the long-term debt was calculated by discounting future cash flows using borrowing rates currently available for debt of similar maturity. Carrying amount and estimated fair value of long-term debt at June 30, 2009 were \$110,096,579 and \$108,938,182, respectively, and at June 30, 2008 were \$78,876,672 and \$83,137,092, respectively. Other assets and obligations are insignificant, and carrying amounts are assumed to approximate fair value.

Fair value estimates are made at a specific point in time based on relevant market information. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

**(12) 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, 2009 and 2008 was as follows:

|                        | <u>2009</u> | <u>2008</u> |
|------------------------|-------------|-------------|
| Commercial pay         | 30%         | 30%         |
| Medicare               | 16          | 17          |
| Self-pay               | 5           | 4           |
| Medicaid               | 13          | 12          |
| Blue Cross/Blue Shield | 25          | 25          |
| Iowa Care              | 8           | 10          |
| Other                  | 3           | 2           |
|                        | <u>100%</u> | <u>100%</u> |

**(13) 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, 2009 and 2008 was \$5,522,263 and \$4,811,709, respectively.

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The following is a schedule by year of future minimum rental payments required under noncancelable operating leases as of June 30, 2009:

|                                    |    |           |
|------------------------------------|----|-----------|
| Year ending June 30:               |    |           |
| 2010                               | \$ | 2,773,354 |
| 2011                               |    | 2,660,450 |
| 2012                               |    | 751,832   |
| 2013                               |    | 583,760   |
| 2014                               |    | 323,760   |
| Total minimum payments<br>required | \$ | 7,093,156 |

**(14) Accounts Payable and Accrued Expenses**

Accounts payable and accrued expenses reported as current liabilities at June 30, 2009 and 2008 consisted of the following amounts:

| <b>Accounts payable and accrued expenses</b>   | <b>2009</b>    | <b>2008</b> |
|--|----------------|-------------|
| Payable to employees (including payroll taxes) | \$ 73,243,817  | 69,894,357  |
| Payable to suppliers                           | 27,981,482     | 28,204,340  |
| Other  | 1,828,853      | 1,607,560   |
| Total accounts payable and accrued expenses    | \$ 103,054,152 | 99,706,257  |

**(15) 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.

**(16) Subsequent Events**

The State University of Iowa issued \$25,000,000 of Telecommunications Facilities Revenue Bonds in December 2009. UIHC's share of the bonds issued was 51.3% or \$12,825,000. The proceeds of the Bonds will be used to pay costs of constructing, installing, and extending certain improvements to the Telecommunications System of the University.

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UIHC has reviewed subsequent events through December 18, 2009, the date the financial statements were issued, and concluded that there were no events or transactions during this period that would require recognition or disclosure in the financial statements other than those already disclosed.