

University of Wisconsin Hospitals and Clinics Authority

Basic Financial Statements as of and
for the Years Ended June 30, 2010 and 2009,
Required Supplementary Information
as of June 30, 2010 and 2009, and
Independent Auditors' Report

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

TABLE OF CONTENTS

	Page
MANAGEMENT'S DISCUSSION AND ANALYSIS	1–13
INDEPENDENT AUDITORS' REPORT	14
BASIC FINANCIAL STATEMENTS:	
Balance Sheets as of June 30, 2010 and 2009	15
Statements of Revenues, Expenses, and Changes in Net Assets for the Years Ended June 30, 2010 and 2009	16
Statements of Cash Flows for the Years Ended June 30, 2010 and 2009	17–18
Notes to Basic Financial Statements as of and for the Years Ended June 30, 2010 and 2009	19–41
REQUIRED SUPPLEMENTARY INFORMATION —	42
Schedule of Plan Funding Progress under GASB Statement No. 45 as of July 1, 2007 (date of adoption) through June 30, 2010	43

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEARS ENDED JUNE 30, 2010 AND 2009

The University of Wisconsin Hospitals and Clinics Authority (the "Hospital") implemented Governmental Accounting Standards Board's (GASB) Statement No. 34, *Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments*, for the annual financial report year ended June 30, 2003. This section of the Hospital's annual financial report presents management's analysis of the Hospital's performance during the fiscal years that ended on June 30, 2009 and 2010, and is designed to focus on the current fiscal year activity, resulting changes, and currently known facts; therefore, please read it in conjunction with the Hospital's financial statements.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Hospital's financial statements, and the notes to the financial statements.

The balance sheets and the statements of revenues, expenses, and changes in net assets, and cash flows, reported on the accrual basis, provide an indication of the Hospital's financial health. The balance sheets include all of the Hospital's assets and liabilities, as well as an indication about which assets can be utilized for general purposes and which are restricted by external donors or for other purposes. The statements of revenues, expenses, and changes in net assets report all of the revenue and expenses during the period indicated. The statements of cash flows report the cash provided and used by operating activities, as well as other cash sources such as investment income and other cash uses, such as repayment of bonds and capital additions. The notes to financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

FINANCIAL HIGHLIGHTS — FISCAL YEAR 2010

- The Hospital's net assets increased by approximately \$68.6 million.
- Net patient service revenues increased by \$60.4 million, or 6.4%. Total operating revenues increased by \$61.1 million, or 6.4%, and total operating expenses increased by \$37.9 million, or 4.1%.
- Operating income for the year was \$65.1 million.
- The Hospital implemented Governmental Accounting Standards Board (GASB) Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* (GASB 53) in fiscal 2010. The Hospital has historically reported the fair value of the swap investments in the footnotes. GASB Statement No. 53 now requires the changes in fair value of the interest rate swaps to be reported in the statement of revenues, expenses and changes in net assets. As a result, the increase in non-operating expense for fiscal 2010, directly related to the implementation, was \$3.9 million.
- Total non-operating revenue (expense) increased by \$10.2 million or 193.6%. The majority of this increase is due to net increase in the fair value of investments and a decrease in interest expense, offset by fair value of interest rate swap agreements and decrease in investment income.
- The excess of revenues over expenses before capital grants, gifts, and donations, additions to permanent endowments, other payments, and special items increased \$33.3 million or 90.9%.

FINANCIAL HIGHLIGHTS — FISCAL YEAR 2009

- The Hospital's net assets increased by approximately \$35.3 million.

- Net patient service revenues increased by \$103.7 million, or 12.4%. Total operating revenues increased by \$104.7 million, or 12.3%, and total operating expenses increased by \$81.7 million, or 9.8%.
- Operating income for the year was \$42.0 million.
- Total nonoperating revenue (expense) decreased by \$12.7 million or 171.1%. The majority of this decrease is due to net decrease in the fair value of investments, a decrease in investment income and other.
- The excess of revenues over expenses before capital grants, gifts, and donations, additions to permanent endowments, other payments, and special items increased \$10.3 million or 39.2%.

HOSPITAL HIGHLIGHTS — FISCAL YEAR 2010

- The Hospital completed implementation of the EPIC-based patient management system at an estimated project cost to the Hospital of \$52.2 million. This system, named UW Health Link, intertwines the clinical components of an electronic health record for clinical documentation, medication management, computerized provider order entry, health information management, and peri-operative modules with business applications such as registration, appointment scheduling, and billing. The Hospital had successful go-lives for the peri-operative modules, hospital billing and the electronic health record in numerous ambulatory clinics in 2010.
- The Hospital purchased the third parcel of land in the American Center business and office park, located on Madison's east side, for \$2.6 million in 2010. The first two parcels of land were purchased in 2006 and 2007 for \$3.4 million and \$2.8 million, respectively. These land acquisitions are intended to address the expansion of hospital services at an undetermined future date.
- The Hospital completed the third phase of the Radiation Oncology relocation and expansion.
- Capital contributions to the University of Wisconsin School of Medicine and Public Health (UWSMPH) included \$2.5 million as the first installment of a \$7.5 million commitment to be paid over three years to acquire space in the Clinical Science Center vacated by occupants of the UWSMPH's Medical Foundation Centennial Building.
- The Hospital ranked in the top three percent of U.S hospitals in seven medical specialties in the U.S. News and World Report, "America's Best Hospitals 2010".
- The Hospital was recognized by Health Information Management Society (HIMSS) as one of 38 hospitals nationwide to have attained Stage 7 (of 0-7) for electronic health record implementation.

HOSPITAL HIGHLIGHTS — FISCAL YEAR 2009

- The Hospital continued to proceed with a fully integrated implementation of the EPIC-based patient management system, UW Health Link. The Hospital had successful go-lives for the clinical documentation, computerized provider order entry, oncology applications and the electronic health record in numerous ambulatory clinics in 2009.
- In September 2008, the Hospital opened the operating room suites in the American Family Children's Hospital.
- In September 2008, the Hospital entered into an equipment financing agreement for \$9.3 million to finance the American Family Children's Hospital operating room equipment.
- In February 2009, the State of Wisconsin established a tax assessment program on acute care hospitals with the intent to improve Medicaid reimbursement for Wisconsin hospitals. This assessment has been approved by the Centers of Medicare and Medicaid Services and was retroactive to July 1, 2008. The net benefit to the Hospital from this Program was approximately \$9.9 million for the year ended June 30, 2009. Due to the tax assessment provisions, implementation of the Program impacted both operating revenues and expenses in the Hospital's statements of revenues, expenses and changes in net assets. For the year ended June 30, 2009, net patient service revenue was increased by approximately \$32 million due to increased Medicaid reimbursement on fee-for-service claims and HMO payments. The tax assessment of approximately \$22.1 million is included in other operating expenses.

- In response to the continued volatility in the bond insurance industry, the Hospital refunded two outstanding debt issues in March 2009. The Hospital issued approximately \$57.1 million in Variable Rate Demand Revenue Refunding Bonds Series 2009A. The Series 2009A bond proceeds were used to refund \$55.6 million of Hospital Revenue Bonds consisting of Short-Term Adjustable Rate Securities, Series 2002A and pay certain costs incurred in connection with the issuance and refunding of the bonds. This transaction resulted in a write-off of the unamortized bond insurance premium of the Series 2002A Bonds in the amount of \$1,652,000 which is reported as a special item and recognition of a deferred loss of \$638,000 for other unamortized financing costs. Also in March 2009, the Hospital issued approximately \$59.3 million of Variable Rate Demand Revenue Refunding Bonds, Series 2009B. The bond proceeds were used to refund \$58.1 million of Variable Rate Demand Revenue Refunding Bonds, Series 2005 and pay certain costs incurred in connection with the issuance and refunding of the bonds. This transaction resulted in a write-off of the unamortized bond insurance premium of the Series 2005 Bonds in the amount of \$889,000 which is reported as a special item and recognition of a deferred loss of \$421,000 for other unamortized financing costs.
- The Hospital purchased an off-campus facility for administrative services. This purchase and the planned renovation of the building was financed with Series 2009C bonds in the amount of \$5.3 million in June 2009.
- The Hospital has essentially met its capital campaign goal of raising \$41.0 million, which began in 2003. The Hospital has approximately \$2.0 million of pledges outstanding as of June 30, 2009.
- The Hospital received a total of \$1.2 million of capital grants, gifts and donations, which includes approximately \$629,000 of cash collected for the American Family Children's Hospital building fund and approximately \$534,000 of donated equipment for other areas of the hospital.
- The Hospital received the Magnet designation by the American Nurses Credentialing Center in 2009.
- The Hospital ranked among the top 50 of the nation's hospitals in five medical specialties in the U.S. News and World Report, "America's Best Hospitals 2009".
- The Hospital was recognized by Health Information Management Society (HIMSS) as one of 42 hospitals nationwide to have attained Stage 6 (of 0-7) for electronic health record implementation.

FINANCIAL ANALYSIS AND RESULTS OF OPERATIONS

At June 30, 2010, the Hospital's assets exceeded liabilities by \$573.9 million, which is an increase in total net assets of \$68.6 million, or 13.6%, from the prior fiscal year-end, after restatement of the 2010 beginning net assets.

At June 30, 2009, the Hospital's assets exceeded liabilities by \$513.7 million, which is an increase in total net assets of \$35.3 million, or 7.4% from the prior fiscal year-end.

Table 1 summarizes assets, liabilities, and net assets at June 30 (in thousands):

	June 30, 2010	June 30, 2009	Dollar Change	Percent Change
Current and other assets	\$ 626,530	\$ 519,977	\$ 106,553	20.5 %
Capital assets	<u>392,004</u>	<u>410,395</u>	<u>(18,391)</u>	(4.5)%
Total assets	<u>\$ 1,018,534</u>	<u>\$ 930,372</u>	<u>\$ 88,162</u>	9.5 %
Long-term debt	\$ 243,158	\$ 249,834	\$ (6,676)	(2.7)%
Other liabilities	<u>201,453</u>	<u>166,879</u>	<u>34,574</u>	20.7 %
Total liabilities	<u>444,611</u>	<u>416,713</u>	<u>27,898</u>	6.7 %
Net assets:				
Invested in capital assets, net of related debt	150,496	163,574	(13,078)	(8.0)%
Restricted	8,415	8,535	(120)	(1.4)%
Unrestricted	<u>415,012</u>	<u>341,550</u>	<u>73,462</u>	21.5 %
Total net assets	<u>573,923</u>	<u>513,659</u>	<u>60,264</u>	11.7 %
Total liabilities and net assets	<u>\$ 1,018,534</u>	<u>\$ 930,372</u>	<u>\$ 88,162</u>	9.5 %

	June 30, 2009	June 30, 2008	Dollar Change	Percent Change
Current and other assets	\$ 519,977	\$ 487,381	\$ 32,596	6.7 %
Capital assets	<u>410,395</u>	<u>398,111</u>	<u>12,284</u>	3.1
Total assets	<u>\$ 930,372</u>	<u>\$ 885,492</u>	<u>\$ 44,880</u>	5.1 %
Long-term debt	\$ 249,834	\$ 239,414	\$ 10,420	4.4 %
Other liabilities	<u>166,879</u>	<u>167,763</u>	<u>(884)</u>	(0.5)
Total liabilities	<u>416,713</u>	<u>407,177</u>	<u>9,536</u>	2.3
Net assets:				
Invested in capital assets, net of related debt	163,574	162,156	1,418	0.9
Restricted	8,535	10,445	(1,910)	(18.3)
Unrestricted	<u>341,550</u>	<u>305,714</u>	<u>35,836</u>	11.7
Total net assets	<u>513,659</u>	<u>478,315</u>	<u>35,344</u>	7.4
Total liabilities and net assets	<u>\$ 930,372</u>	<u>\$ 885,492</u>	<u>\$ 44,880</u>	5.1 %

At June 30, 2010, the Hospital's cash and investments increased \$88.5 million or 26.3% compared to June 30, 2009. The majority of the increase in fiscal 2010 cash and investments is attributable to increases from operating activities and estimated cost report settlements received, offset by purchases of property, plant, and equipment, repayments of long-term debt and interest paid.

At June 30, 2009, the Hospital's cash and investments increased \$18.7 million or 5.9% compared to June 30, 2008. The majority of the increase in fiscal 2009 cash and investments is attributable to increases from operating activities, offset by purchases of property, plant, and equipment (offset by capital donations received and reimbursement from bond proceeds), repayments of long-term debt and interest paid.

As of June 30, 2010, the Hospital reports the net present value of pledges receivable totaling \$1.1 million for the American Family Children's Hospital in accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Non-exchange Transactions*. The net present value of pledges as of June 30, 2009, was \$1.9 million.

Other liabilities include \$59.6 million and \$63.2 million at June 30, 2010 and 2009, respectively, of unfunded prior service pension liabilities which are recorded for the unfunded liabilities of participants in the Wisconsin Retirement System, \$12.2 million and \$7.7 million at June 30, 2010 and 2009, respectively, of the net OPEB obligation for retiree health insurance and \$12.2 million at June 30, 2010 of the fair market value of the derivative instruments.

Table 2 compares 2010 revenues and expenses to 2009 and 2009 revenues and expenses to 2008, and shows the increase in net assets (in thousands).

TABLE 2
CONDENSED SCHEDULE OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

	June 30, 2010	June 30, 2009	Dollar Change	Percent Change
Operating revenues:				
Net patient service revenues	\$ 1,002,272	\$ 941,856	\$ 60,416	6.4 %
Other operating revenue	<u>16,346</u>	<u>15,679</u>	<u>667</u>	4.3
Total operating revenues — net	<u>1,018,618</u>	<u>957,535</u>	<u>61,083</u>	6.4
Operating expenses:				
Salaries and benefits	513,335	491,328	22,007	4.5
Medical materials and supplies	198,652	189,271	9,381	5.0
Purchased services and agency costs	103,122	102,652	470	0.5
Depreciation and amortization	48,874	44,209	4,665	10.6
Other	<u>89,512</u>	<u>88,114</u>	<u>1,398</u>	1.6
Total operating expenses	<u>953,495</u>	<u>915,574</u>	<u>37,921</u>	4.1
Operating income	65,123	41,961	23,162	55.2
Nonoperating revenues (expenses):				
Nonoperating revenues	8,151	(3,256)	11,407	350.3
Nonoperating expenses	(8,258)	(10,011)	1,753	17.5
Other	<u>5,031</u>	<u>8,006</u>	<u>(2,975)</u>	(37.2)
Total nonoperating revenues (expenses) — net	<u>4,924</u>	<u>(5,261)</u>	<u>10,185</u>	193.6
Excess of revenues over expenses before capital grants, gifts and donations, additions to permanent endowments, other payments, and special items	70,047	36,700	33,347	90.9
Special items, net loss on unamortized bond insurance premium		(2,541)	2,541	100.0
Capital grants, gifts and donations	1,091	1,163	(72)	(6.2)
Payments to University of Wisconsin School of Medicine and Public Health (UWSMPH) for capital expenditure support	(2,640)		(2,640)	(100.0)
Additions to permanent endowments	<u>111</u>	<u>22</u>	<u>89</u>	404.5
Increase in net assets	68,609	35,344	33,265	94.1
Net assets beginning of year	513,659	478,315	35,344	7.4
Cumulative effect of change in accounting principal for derivative instruments	<u>(8,345)</u>	<u>0</u>	<u>(8,345)</u>	(100.0)
Net assets end of year	<u>\$ 573,923</u>	<u>\$ 513,659</u>	<u>\$ 60,264</u>	11.7 %

TABLE 2
CONDENSED SCHEDULE OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

	June 30, 2009	June 30, 2008	Dollar Change	Percent Change
Operating revenues:				
Net patient service revenues	\$ 941,856	\$ 838,146	\$ 103,710	12.4 %
Other operating revenue	<u>15,679</u>	<u>14,725</u>	<u>954</u>	6.5
Total operating revenues — net	<u>957,535</u>	<u>852,871</u>	<u>104,664</u>	12.3
Operating expenses:				
Salaries and benefits	491,328	461,435	29,893	6.5
Medical materials and supplies	189,271	177,598	11,673	6.6
Purchased services and agency costs	102,652	95,759	6,893	7.2
Depreciation and amortization	44,209	37,959	6,250	16.5
Other	<u>88,114</u>	<u>61,161</u>	<u>26,953</u>	44.1
Total operating expenses	<u>915,574</u>	<u>833,912</u>	<u>81,662</u>	9.8
Operating income	41,961	18,959	23,002	121.3
Nonoperating revenues (expenses):				
Nonoperating revenues	(3,256)	7,821	(11,077)	(141.6)
Nonoperating expenses	(10,011)	(10,820)	809	7.5
Other	<u>8,006</u>	<u>10,398</u>	<u>(2,392)</u>	23.0
Total nonoperating revenues (expenses) — net	<u>(5,261)</u>	<u>7,399</u>	<u>(12,660)</u>	(171.1)
Excess of revenues over expenses before capital grants, gifts and donations, additions to permanent endowments, other payments, and special items	36,700	26,358	10,342	39.2
Special items, net loss on unamortized bond insurance premium	(2,541)	(1,958)	(583)	(29.8)
Capital grants, gifts and donations	1,163	7,710	(6,547)	(84.9)
Payments to University of Wisconsin School of Medicine and Public Health (UWSMPH) for capital expenditure support		(2,042)	2,042	(100.0)
Additions to permanent endowments	<u>22</u>	<u>67</u>	<u>(45)</u>	<u>(67.2)</u>
Increase in net assets	35,344	30,135	5,209	17.3
Net assets beginning of year	<u>478,315</u>	<u>448,180</u>	<u>30,135</u>	6.7
Net assets end of year	<u>\$ 513,659</u>	<u>\$ 478,315</u>	<u>\$ 35,344</u>	7.4 %

Net Patient Service Revenue

Net patient service revenue in 2010 increased \$60.4 million, or 6.4% from the prior year. The primary reasons for the growth in revenue are the increases in the number of patients cared for and third-party payor reimbursement increases which averaged 5.0% during the year, offset by an increase in the provision for charity care and bad debt. Inpatient volume, measured by admissions, increased approximately 500, or 1.8%, and outpatient volume, measured by visits, increased by approximately 11,300 visits, or 2.0%. Patient days increased approximately 40 or 0.0%. The Hospital's case mix index (CMI), which is a measure of patient acuity, calculated on an MS-DRG basis in 2010 and recalculated for 2009, was 1.88 in 2010 compared to 1.85 in 2009.

Sources of net patient service revenue by payor category for fiscal years 2010 and 2009 are depicted below:

**TABLE 3
PAYOR MIX**

	Fiscal Year		Percent Change
	2010	2009	
Medicare	26 %	25 %	4.0
Medicaid	8	8	-
Indemnity	4	5	(20.0)
Managed care — capitated	5	5	-
Managed care — noncapitated	48	48	-
Private pay and other	9	9	-
	100 %	100 %	

Net patient service revenue in 2009 increased \$103.7 million, or 12.4% from the prior year. The primary reasons for the growth in revenue are the additional reimbursement from the Medicaid program as part of the Wisconsin hospital assessment program, increases in the number of patients cared for and third-party payor reimbursement increases which averaged 5.3% during the year, offset by an increase in the provision for charity care and bad debt. Inpatient volume, measured by admissions, increased approximately 500, or 2.1%, and outpatient volume, measured by visits, increased by approximately 12,100 visits, or 2.2%. Patient days increased approximately 4,500 or 3.4%. The Hospital's case mix index (CMI), which is a measure of patient acuity prior to revision in calculation methodology, was 1.79 in 2009 compared to 1.80 in 2009.

Sources of net patient service revenue by payor category for fiscal years 2009 and 2008 are depicted below:

**TABLE 3
PAYOR MIX**

	Fiscal Year		Percent Change
	2009	2008	
Medicare	25 %	25 %	-
Medicaid	8	4	100.0
Indemnity	5	6	(16.7)
Managed care — capitated	5	5	-
Managed care — noncapitated	48	50	(4.0)
Private pay and other	9	10	(10.0)
	100 %	100 %	

Other operating revenue, which includes nonpatient revenue such as cafeteria sales and other auxiliary services, increased nearly \$0.7 million to \$16.3 million in 2010, or 4.3% over prior year and \$1.0 million to \$15.7 million in 2009, or 6.5% over 2008.

Operating Expenses

Operating expenses increased by \$37.9 million in 2010 or 4.1% over the prior year. The categories of expenses that caused the majority of the increases were salaries, wages and benefits, medical materials and supplies and depreciation and amortization. Salaries, wages, and benefits expense increased 4.5% from 2009 due to wage and fringe benefit rate increases. The increase in medical materials and supplies compared to the prior year was primarily in pharmaceuticals, surgical appliances and medical/surgical supplies.

Operating expenses increased by \$81.7 million in 2009 or 9.8% over the prior year. The categories of expenses that caused the majority of the increases were salaries, wages and benefits, medical materials and supplies and other. Salaries, wages, and benefits expense increased 6.5% from 2008 with additional FTEs due to increases in patient volume and coverage for time spent in Health Link training and support during go-live implementations, as well as wage and fringe benefit rate increases. During 2009, the Hospital ratified labor contracts with two of the four labor unions. The increase in medical materials and supplies compared to the prior year was primarily in pharmaceuticals, surgical appliances and medical/surgical supplies. The increase in other expense is due to the \$22.1 million Medicaid tax assessment to the Hospital that was effective July 1, 2008.

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist primarily of income from the Hospital's cash and long-term investments, loss on disposal of capital assets, and the equity interest in gain or loss from joint ventures. Investment income, including the change in fair value of investments, increased to \$12.1 million in 2010, decreased to \$(3.3) million in 2009 from \$7.8 million in 2008. The increase in 2010 is due to the increase in the fair value of investments this year.

The Hospital's investment income and net changes in fair value of investments for 2010, 2009, and 2008, are summarized in Table 4 (in thousands):

TABLE 4
INVESTMENT EARNINGS BY ASSET CATEGORY

	2010	2009	2008
Interest and dividend income:			
Equity investments	\$ 3,165	\$ 2,837	\$ 2,616
Fixed income investments	<u>4,447</u>	<u>6,592</u>	<u>9,006</u>
Total investment income	7,612	9,429	11,622
Net (decrease) increase in fair value of investments	<u>4,442</u>	<u>(12,685)</u>	<u>(3,801)</u>
Total	<u>\$ 12,054</u>	<u>\$ (3,256)</u>	<u>\$ 7,821</u>

The decrease in equity interest in gain/loss of joint ventures from a \$6.5 million gain in 2009 to a gain of \$6.1 million in 2010 is due to the decrease in Unity's net income in 2010 in comparison to 2009, of which the Hospital records 60% of the joint venture's gain or loss. The loss on disposal of capital assets was \$100,000 in 2010 and the gain was \$125,000 in 2009 and the loss was \$384,000 in 2008. These balances are included in nonoperating revenue (expenses). Implementation of GASB Statement No. 53 to record the fair value of the interest rate swap agreements resulted in \$3.9 million non-operating expense in 2010.

Interest expense in 2010 was \$8.3 million, as included in nonoperating expenses. The decrease in interest expense from \$10.0 million in 2009 and \$10.8 million in 2008 is due to the decrease in variable bond interest rates in 2010 and principal payments on outstanding debt.

Capital Assets

At June 30, 2010, the Hospital had \$392.0 million, net of accumulated depreciation and amortization, invested in capital assets. This amount represents a net decrease, including additions and disposals, of \$18.4 million, or 4.5% from 2009. The decrease is due to depreciation expense exceeding the purchase of new capital assets in 2010.

At June 30, 2009, the Hospital had \$410.4 million, net of accumulated depreciation and amortization, invested in capital assets. This amount represents a net increase, including additions and disposals, of \$12.3 million, or 3.1% from 2008. The majority of the increase is related to the completion of the American Family Children's Hospital Phase 2 Operating Room suites, an off-campus building acquisition to be occupied by Information Technology staff, and continuation of construction projects (primarily the Radiotherapy expansion in the Wisconsin Institutes for Medical Research building).

Table 5 shows a summary of capital assets, net of accumulated depreciation and amortization, at June 30, 2010, 2009, and 2008 and major additions by year for the years ended June 30, 2010, 2009, and 2008 (in thousands).

TABLE 5
CAPITAL ASSETS AT YEAR END (NET OF ACCUMULATED DEPRECIATION AND AMORTIZATION)

	2010	2009	2008
Land	\$ 14,385	\$ 11,780	\$ 11,771
Buildings and land improvements	297,894	299,081	280,697
Equipment	74,937	86,283	82,684
Construction in progress	<u>4,788</u>	<u>13,251</u>	<u>22,959</u>
Total	<u>\$ 392,004</u>	<u>\$ 410,395</u>	<u>\$ 398,111</u>

MAJOR ADDITIONS BY YEAR

	June 30		
	2010	2009	2008
Land acquisition	\$ 2,605	\$	\$ 3,000
Buildings and improvements:			
Purchase off-campus facility	991	4,008	
Radiation Oncology relocation & expansion to the Wisconsin Institutes for Medical Research Building	6,510	10,789	
Data Center Improvements	552	1,938	
Inpatient Unit Remodeling	3,246		4,700
Improvements to new leased facility	1,087		
Outpatient Pharmacy		570	
American Family Children's Hospital OR Suites		11,209	
American Family Children's Hospital			72,550
American Family Children's Hospital Emergency Generator			1,700
Super Elevator			2,300
Equipment:			
Implementation Costs for Patient Management System	3,539	8,215	9,400

Construction in progress at June 30, 2010, consists principally of costs incurred for inpatient unit remodeling and a utility expansion project at the main Hospital building.

For more information about the Hospital's capital asset activity, please see Note 6 to the financial statements. Ongoing capital requirements will be funded primarily from operations. The Hospital's total capital budget for 2011 is \$50.7 million compared to the 2010 capital budget of \$32.9 million.

Long-term Debt

At June 30, 2010, the Hospital had \$235.7 in long-term debt, excluding current installments, compared to \$242.8 million at June 30, 2009 — a decrease of 2.9% due to principal payments on the State of Wisconsin general obligation and refunding bonds, Series 2002B, Series 2008A, Series 2009B, Series 2009C and the GE Loan. Long-term debt, excluding current installments, at June 30, 2008, was \$234.1 million. The increase from 2008 to 2009 resulted from the issuance of the Series 2009A, Series 2009B, Series 2009C and an equipment financing agreement with GE Government Finance, Inc., offset by refunding of Series 2002A and Series 2005 and principal payments on the State of Wisconsin general obligation and refunding bonds, Series 2000, Series 2002B, Series 2005 bonds and the GE Loan.

Table 6 below provides the detail of outstanding long-term debt, excluding current installments, as of June 30, 2010, 2009, and 2008 (in thousands):

TABLE 6
OUTSTANDING LONG-TERM DEBT — AT YEAR-END

	2010	2009	2008
State of Wisconsin general obligation and refunding bonds	\$ 4,157	\$ 5,868	\$ 7,671
Authority Fixed Rate Demand Revenue Bonds, Series 2000			1,315
Authority Short-term Adjustable Rate Revenue Bonds, Series 2002A			55,600
Authority Fixed Rate Revenue Bonds, Series 2002B	3,405	5,205	6,910
Authority Variable Rate Revenue Bonds, Series 2005			58,095
Authority Fixed Rate Revenue Bonds, Series 2008A	49,545	50,060	50,375
Authority Variable Rate Demand Revenue Bonds, Series 2008B	61,000	61,000	61,000
Authority Variable Rate Demand Revenue Bonds, Series 2009A	57,070	57,070	
Authority Variable Rate Demand Revenue Bonds, Series 2009B	56,830	58,790	
Authority Fixed Rate Adjustable Revenue Bonds, Series 2009C	4,931	5,180	
Equipment Loan	6,090	7,335	
Premium on Series 2002B Bonds	176	241	306
Deferred Loss on Refunding of Series 1997 Bonds	(242)	(256)	(270)
Deferred Loss on Refunding of Series 2004 Bonds	(429)	(446)	(464)
Deferred Loss on Refunding of Series 2000 Bonds	(5,856)	(6,168)	(6,481)
Deferred Loss on Refunding of Series 2002A Bonds	(605)	(632)	
Deferred Loss on Refunding of Series 2005 Bonds	(395)	(416)	
Total	<u>\$ 235,677</u>	<u>\$ 242,831</u>	<u>\$ 234,057</u>

Prior to the refunding in 2009, Series 2002A Short-term Adjustable Rate bonds and Series 2005 Variable Rate Demand bonds were insured by Financial Security Assurance, Inc. Prior to the refunding in 2008, Series 1997 bonds were insured by MBIA Insurance Corp., and the Series 2004 Short-term Adjustable Rate bonds were insured by Ambac, Inc. Series 2008B, Series 2009A and Series 2009B bonds are secured by an irrevocable transferable direct pay letter of credit issued by US Bank. The Authority bonds carry an underlying A1 rating from Moody's and an A+ rating from Standard & Poor's. The insured bonds carry an AAA rating from Moody's and Standard and Poor's.

Current legislation requires the Hospital to obtain approval of additional bond issuance from its Board of Directors, maintain an unenhanced bond rating in the category of “A” or better from Standard and Poor’s Corporation and Moody’s Investor Service, Inc., and notify the State Joint Committee on Finance and the Department of Administration. For more information about the Hospital’s outstanding debt, please see Note 7 to the financial statements.

Economic Factors and Next Year’s Budgets and Rates

The Hospital’s senior leadership team considered many variables in developing the 2011 budget and rates. Key strategic goals of maintaining high quality, safety, and service standards, as well as achieving fiscal margins provide the primary objectives in preparing each year’s budget. Fiscal 2011 budget assumptions were particularly difficult due to economic conditions and uncertain government reimbursement, including health care reform. This required a very disciplined approach in preparing the 2011 budget in an effort to keep the work force count consistent with existing levels, improve efficiency and contain cost increases. The 2011 budget, as approved by the Hospital’s board of directors, projects income from operations of \$51.4 million, resulting in an operating margin of 5.0%. Net income is budgeted at \$59.4 million representing a margin of 5.7%. Achieving a 5.7% margin is accomplished through increased volumes, average payment increases of 3.6% across all payor categories and by decreasing the cost per unit of service. The 2011 budget calls for volume increases of 2.3% for inpatient admissions, 2.4% for inpatient days, and 3.8% for outpatient clinic visits.

Requests for Information

This financial report is designed to provide a general overview of University of Wisconsin Hospitals and Clinics Authority’s financial results for all those with an interest in the Hospital’s finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Chief Financial Officer, 600 Highland Avenue, Mail Drop # 8370, Madison, WI 53792.

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
University of Wisconsin Hospitals
and Clinics Authority:

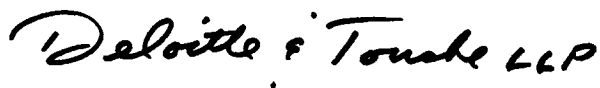
We have audited the accompanying balance sheets of the University of Wisconsin Hospitals and Clinics Authority (the "Hospital"), a component unit of the State of Wisconsin, as of June 30, 2010 and 2009, and the related statements of revenues, expenses, and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Hospital'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 respective 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 the Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective 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.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the University of Wisconsin Hospitals and Clinics Authority as of June 30, 2010 and 2009, and the results of its operations, its changes in net assets, and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, the Hospital adopted Governmental Accounting Standards Board (GASB) Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, as of July 1, 2009.

Management's discussion and analysis on pages 1-13 and Schedule of Plan Funding Progress under GASB Statement No. 45 on page 43 are not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Hospital's management. 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 such information and we do not express an opinion on it.



October 19, 2010

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

BALANCE SHEETS AS OF JUNE 30, 2010 AND 2009 (In thousands)

	2010	2009
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 48,823	\$ 47,051
Patient accounts receivable — net of estimated uncollectible accounts of \$42,000 in 2010 and \$35,000 in 2009	123,873	108,196
Other receivables	8,098	7,416
Estimated receivable from Medicare and Medicaid	-	2,984
Inventories of supplies	8,645	8,537
Prepaid expenses	6,561	5,862
	<u>196,000</u>	<u>180,046</u>
Total current assets		
NONCURRENT CASH AND INVESTMENTS:		
Designated by board for capital replacement, debt retirement, and other long-term investments	366,635	279,269
Held by trustee for capital projects and other purposes	1,650	3,013
Restricted by donors	6,039	5,450
Principal of permanent endowments	1,280	1,169
	<u>375,604</u>	<u>288,901</u>
Total noncurrent cash and investments		
CAPITAL ASSETS:		
Nondepreciable	21,134	26,746
Depreciable — net	370,870	383,649
	<u>392,004</u>	<u>410,395</u>
Capital assets — net		
INVESTMENTS IN JOINT VENTURES	<u>47,900</u>	<u>44,242</u>
PLEDGES RECEIVABLE	<u>1,065</u>	<u>1,888</u>
OTHER ASSETS	<u>5,961</u>	<u>4,900</u>
TOTAL	<u>\$ 1,018,534</u>	<u>\$ 930,372</u>

See notes to financial statements.

	2010	2009
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Current installments of long-term debt	\$ 7,481	\$ 7,003
Accounts payable	22,388	22,068
Accrued expenses	84,003	73,978
Estimated payables to Medicare and Medicaid	<u>10,991</u>	<u>-</u>
Total current liabilities	124,863	103,049
LONG-TERM DEBT — Less current installments	235,677	242,831
OPEB-RELATED LIABILITIES	12,195	7,654
PENSION-RELATED LIABILITIES	59,627	63,179
OTHER LONG-TERM LIABILITES	<u>12,249</u>	<u>-</u>
Total liabilities	<u>444,611</u>	<u>416,713</u>
NET ASSETS:		
Invested in capital assets — net of related debt	150,496	163,574
Restricted — expendable for donor-specified purposes	7,135	7,366
Restricted — nonexpendable	1,280	1,169
Unrestricted	<u>415,012</u>	<u>341,550</u>
Total net assets	573,923	513,659
TOTAL	<u>\$ 1,018,534</u>	<u>\$ 930,372</u>

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS FOR THE YEARS ENDED JUNE 30, 2010 AND 2009 (In thousands)

	2010	2009
OPERATING REVENUES:		
Net patient service revenue (net of provision for bad debts of \$20,911 in 2010 and \$23,140 in 2009)	\$ 1,002,272	\$941,856
Other operating revenue	<u>16,346</u>	<u>15,679</u>
Total operating revenues — net	<u>1,018,618</u>	<u>957,535</u>
OPERATING EXPENSES:		
Salaries and wages	362,189	350,091
Employee benefits	151,146	141,237
Other expenses	64,356	64,426
Repairs, maintenance, and utilities	25,156	23,688
Purchased services and agency costs	103,122	102,652
Medical materials and supplies	198,652	189,271
Depreciation and amortization	<u>48,874</u>	<u>44,209</u>
Total operating expenses	<u>953,495</u>	<u>915,574</u>
OPERATING INCOME	<u>65,123</u>	<u>41,961</u>
NONOPERATING REVENUES (EXPENSES):		
Investment income	7,612	9,429
Net increase (decrease) in fair value of investments	4,442	(12,685)
Interest expense	(8,258)	(10,011)
Equity interest in gain of joint ventures	6,108	6,525
Gain (loss) on disposal of capital assets	(100)	125
Noncapital grants and contributions	519	1,320
Net decrease in fair value of swap agreements	(3,903)	
Other — net	<u>(1,496)</u>	<u>36</u>
Total nonoperating revenues (expenses) — net	<u>4,924</u>	<u>(5,261)</u>
EXCESS OF REVENUES OVER EXPENSES BEFORE CAPITAL GRANTS, GIFTS AND DONATIONS, ADDITIONS TO PERMANENT ENDOWMENTS, OTHER PAYMENTS, AND SPECIAL ITEMS	70,047	36,700
SPECIAL ITEMS — Net loss on unamortized bond insurance premium		(2,541)
CAPITAL GRANTS, GIFTS, AND DONATIONS	1,091	1,163
ADDITIONS TO PERMANENT ENDOWMENTS	111	22
PAYMENT TO UNIVERSITY OF WISCONSIN SCHOOL OF MEDICINE AND PUBLIC HEALTH AND THE SCHOOL OF NURSING FOR CAPITAL EXPENDITURE SUPPORT	<u>(2,640)</u>	<u>-</u>
INCREASE IN NET ASSETS	<u>68,609</u>	<u>35,344</u>
NET ASSETS — Beginning of year	513,659	478,315
Cumulative effect of change in method of accounting for derivative instruments	<u>(8,345)</u>	
NET ASSETS — Beginning of year, as restated	<u>505,314</u>	<u>478,315</u>
NET ASSETS — End of year	<u>\$ 573,923</u>	<u>\$513,659</u>

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED JUNE 30, 2010 AND 2009 (In thousands)

	2010	2009
OPERATING ACTIVITIES:		
Cash received from and on behalf of patients	\$ 986,595	\$ 933,079
Payments to suppliers	(360,510)	(374,007)
Payments to employees	<u>(501,466)</u>	<u>(475,519)</u>
Net cash provided by operating activities	<u>124,619</u>	<u>83,553</u>
NONCAPITAL FINANCING ACTIVITIES:		
Noncapital grants and contributions	538	1,320
Decrease in pension-related liabilities	(686)	(6,578)
Additions to permanent endowments	111	22
Payment to University of Wisconsin School of Medicine and Public Health for capital expenditure support	<u>(2,640)</u>	<u>-</u>
Net cash used in noncapital financing activities	<u>(2,677)</u>	<u>(5,236)</u>
CAPITAL AND RELATED FINANCING ACTIVITIES:		
Capital grants, gifts, and donations received	1,839	1,846
Proceeds from long-term debt refunding		130,998
Deferred financing costs	(20)	(1,619)
Repayment/refunding of principal on long-term debt	(7,003)	(119,809)
Interest paid on long-term debt	(8,139)	(9,300)
Purchases of capital assets	(31,942)	(59,097)
Proceeds from sale of capital assets	<u>43</u>	<u>154</u>
Net cash used in capital and related financing activities	<u>(45,222)</u>	<u>(56,827)</u>
INVESTING ACTIVITIES:		
Proceeds from sales of investments	64,381	6,551
Purchases of investments	(85,969)	(25,078)
Investment income received	7,640	9,471
Increase in investment in joint venture	2,451	2,897
Other — net	<u>(2,496)</u>	<u>(1,964)</u>
Net cash used in investing activities	<u>(13,993)</u>	<u>(8,123)</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	62,727	13,367
CASH AND CASH EQUIVALENTS:		
Beginning of year	<u>90,375</u>	<u>77,008</u>
End of year	<u>\$ 153,102</u>	<u>\$ 90,375</u>

(Continued)

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED JUNE 30, 2010 AND 2009 (In thousands)

	2010	2009
RECONCILIATION OF CASH AND CASH EQUIVALENTS TO BALANCE SHEET:		
Cash and cash equivalents in current assets	\$ 48,823	\$ 47,051
Cash equivalents in noncurrent cash and investments	<u>104,279</u>	<u>43,324</u>
TOTAL CASH AND CASH EQUIVALENTS	<u>\$ 153,102</u>	<u>\$ 90,375</u>
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	<u>\$ 65,123</u>	<u>\$ 41,961</u>
Adjustments to reconcile operating income to cash provided by operating activities:		
Provision for bad debts	20,911	23,140
Depreciation and amortization	48,874	44,209
Amortization of bond premium and deferred loss on bond refinancing	327	295
Other post-employment benefits	4,541	3,506
Changes in assets and liabilities:		
Patient accounts receivable	(37,003)	(31,917)
Other receivables	(320)	1,898
Inventories of supplies	(108)	(1,012)
Prepaid expenses	(699)	(1,311)
Estimated receivable from Medicare and Medicaid	13,975	(3,216)
Other assets	(183)	383
Accounts payable	1,853	(6,686)
Accrued expenses	<u>7,328</u>	<u>12,303</u>
Total adjustments	<u>59,496</u>	<u>41,592</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 124,619</u>	<u>\$ 83,553</u>

NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES:

The Hospital held investments at June 30, 2010 and 2009, with fair values of \$271,325 and \$245,577, respectively. During 2010 and 2009, the net decrease/increase in the fair value of these investments was \$4,442 and \$(12,685), respectively.

The Hospital has pledges receivable of \$1,065 in 2010 and \$1,888 in 2009 related to the American Family Children's Hospital Campaign.

See notes to financial statements.

(Concluded)

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

NOTES TO BASIC FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED JUNE 30, 2010 AND 2009

1. SUMMARY OF ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

The University of Wisconsin Hospitals and Clinics Authority (the “Hospital”) is an academic medical center operating an acute care hospital with 493 available beds, numerous specialty clinics, and four ambulatory facilities providing comprehensive health care to patients, education programs, research, and community service primarily to residents of southern Wisconsin.

Prior to fiscal year 1997, the Hospital was a unit of the University of Wisconsin — Madison (the “University”). Beginning in fiscal year 1997, in accordance with legislation passed by the Wisconsin State Legislature, the Hospital restructured as a Public Authority, a public body corporate and politic created by Wisconsin Statutes. This legislation provided, among other things, for the Board of Regents of the University of Wisconsin System (“Board of Regents”) to execute various agreements with the Hospital. The state of Wisconsin (the “State”) appoints the majority of the board of directors of the Hospital. Based on statutorily mandated relationships with State governmental units, the Hospital is included as a discretely presented component unit in the State’s basic financial statements.

Under the terms of a Lease Agreement, the Hospital leases the facilities that were occupied by the Hospital as of June 29, 1996, for a nominal annual amount for an initial term of 30 years to be renewed annually with automatic extensions of one additional year on each July 1 until action is taken to stop the extensions. In addition, the Hospital is required to repay the State’s outstanding debt obligations on the leased facilities. The leased facilities are included with the Hospital’s capital assets (see Note 6), and the debt obligations on the leased facilities are included with the Hospital’s long-term debt (see Note 7).

An Affiliation Agreement (the “Agreement”) requires the Hospital to continue to support the educational, research, and clinical activities of the University, including the University of Wisconsin School of Medicine and Public Health (UWSMPH) and the University of Wisconsin Schools of Nursing and Pharmacy (see Note 4). Subject to a Contractual Services Agreement and Operating and Service Agreement between the Board of Regents and the Hospital, the two parties have entered into contracts with each other for the continuation of the provision of services in support of programs and operations.

The significant accounting policies of the Hospital are as follows:

Basis of Accounting — The accounting policies of the Hospital conform to accounting principles generally accepted in the United States of America as applicable to governmental entities. The accounts of the Hospital, which are reported similar to an enterprise fund, are used to account for the Hospital’s activities that are financed and operated in a manner similar to a private business enterprise. Accordingly, the Hospital maintains its records on the accrual basis of accounting. Revenues from operations, investments, and other sources are recorded when earned. Expenses, including depreciation and amortization, are recorded when incurred.

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, the Hospital has elected not to apply Financial Accounting Standards Board (FASB) or Accounting Principles Board Opinions (APB), issued on or after November 30, 1989, to the Hospital’s financial statements.

Nonexchange transactions, in which the Hospital receives value without directly giving equal value in return, include grants and contributions. Revenues from grants and contributions are recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year the resources are required to be used or the fiscal year in which use is first permitted, and expenditure requirements, in cases where the resources are provided to the Hospital on a reimbursement basis.

Cash and Cash Equivalents — Cash and cash equivalents are defined as highly liquid investments purchased with an original maturity of three months or less.

Inventories of Supplies — The inventories of supplies are valued at the lower of cost (first-in, first-out) or market.

Investments and Investment Income — Investments in equity securities with readily determinable fair values, all investments in debt securities, and pooled investment funds on deposit with the University of Wisconsin Foundation — Endowment Fund, with the exception of alternative investments, are recorded at fair value based upon quoted market prices. The estimated fair value of alternative investments is determined by management based upon information provided by the University of Wisconsin Foundation and is not solely based upon quoted market prices. The pooled investment funds on deposit with the University of Wisconsin Foundation — Expendable Fund are recorded at cost, plus accrued earnings to date, which approximates fair value. The University of Wisconsin Foundation assumes the market risk for the Hospital's investment in the University of Wisconsin Foundation — Expendable Fund. Interest, dividends, and changes in the fair value of investments are included in nonoperating revenue.

Investments in joint ventures, in which the Hospital has the ability to exercise significant influence over the ventures' operating and financial policies, are recorded using the equity method of accounting.

Capital Assets — Capital assets are stated at cost. Capital assets under capital leases are stated at the present value of minimum lease payments. Donated capital assets are recorded at fair market value at the date of donation, which then becomes the asset's historical cost. Depreciation or amortization on capital assets is calculated on the straight-line method over the shorter of the estimated useful life or the period of the lease term. Gains (losses) on sales of capital assets are recorded as nonoperating revenues (expenses). Costs of repairs and maintenance are expensed as incurred. The estimated useful life of capital assets is as follows:

Buildings and improvements	20–30 years
Equipment	5–10 years

Net interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the costs of acquiring those assets.

Costs of Borrowing — Costs incurred in connection with the issuance of long-term debt have been deferred and are being amortized on the straight-line basis over the term of the bonds, which approximates the interest yield method.

Contributions — From time to time, the Hospital receives contributions from individuals and private organizations. Revenues from contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements, are met. Contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are

restricted for a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported as capital grants, gifts, and donations.

Endowments are provided to the Hospital on a voluntary basis by individuals and private organizations. Permanent endowments require that the principal or corpus of the endowment be retained in perpetuity. If a donor has not provided specific instructions, the net appreciation of the investments of endowment funds are recorded with investment income in nonoperating revenue.

Net Assets — Net assets of the Hospital are classified in four components:

Invested in Capital Assets — Net of Related Debt — which consists of capital assets, net of accumulated depreciation and amortization, and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets.

Restricted, Expendable — which are noncapital net assets that must be used for a particular purpose, as specified by creditors or contributors external to the Hospital.

Restricted, Nonexpendable — which equal the principal portion of permanent endowments.

Unrestricted Net Assets — which are remaining net assets that do not meet the definitions of invested in capital assets, net of related debt, or restricted net assets.

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

Operating Revenues and Expenses — The Hospital's statements of revenues, expenses, and changes in net assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services — the Hospital's principal activity. Nonexchange revenues, including contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than interest expense.

Net Patient Service Revenue — Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Reimbursable amounts from third-party payors are estimated in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Net patient service revenue includes revenue derived from agreements with various managed care organizations to provide medical services to subscribing participants. Under certain of these agreements, the Hospital receives fixed monthly capitation payments (generally adjusted annually) based on the number of each managed care organizations' participants, regardless of services actually performed by the Hospital. The Hospital recognizes, in the year of contractual commitment, any losses on these contracts when it is probable that expected medical and maintenance expense under a group of existing contracts would exceed anticipated premiums and recoveries on these contracts. In other agreements, the managed care organizations make fee for service payments to the Hospital for certain covered services based primarily upon discounted fee schedules.

Charity Care — The Hospital has a policy of providing health care services, without charge or at amounts less than established rates, to those unable to pay all or a portion of their charges and who meet certain eligibility criteria established in the Hospital's charity care policy. Because the Hospital does not

pursue collection of amounts determined to qualify as charity care, they are not reported as patient service revenue.

Risk Management — The Hospital is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. The primary commercial insurance for professional liability is a full deductible policy. Settled claims have not exceeded this commercial coverage in any of the three preceding years. The Hospital is self-insured for workers' compensation (see Note 14). The estimated provision for self-insured workers' compensation includes the ultimate cost for both reported losses and losses incurred but not reported as of the respective balance sheet dates.

Compensated Absences — The Hospital's employees earn vacation days at varying rates depending on years of service. Employees may accumulate vacation time up to a specified maximum. Employees are paid for accumulated vacation time if they terminate employment. Consistent with the compensated absences reporting standards of GASB Statement No. 16, *Accounting for Compensated Absences*, an accrual for certain salary-related payments associated with compensated absences is included in the accrued expenses at June 30, 2010 and 2009.

Income Taxes — The Hospital qualifies as a Section 501(c)(3) not-for-profit institution of the Internal Revenue Code (the "Code") and, therefore, is exempt from federal income taxes pursuant to Section 501(a) of the Code. The Hospital is, however, subject to federal income taxes on any unrelated business income under the provisions of Section 511 of the Code. The Hospital is exempt from state income taxes under Section 71.26(b)(e) of Wisconsin Statutes.

Use of Estimates — The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure 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.

Derivative Instruments — During fiscal year 2010, the Hospital adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. GASB Statement No. 53 establishes standards for the measurement, recognition, and disclosure of derivative instruments. GASB Statement No. 53 now requires derivative instruments be recorded on the balance sheet as either an asset or liability measured at its fair market value with changes in fair market value being included in the statements of revenues, expenses and changes in net assets. Management concluded restating fiscal 2009 financial statements was not practical.

2. RESTRICTED NET ASSETS AND ENDOWMENTS

Restricted expendable net assets as of June 30, 2010 and 2009, are available for the following purposes (in thousands):

	2010	2009
Capital purposes	\$ 1,938	\$ 2,353
Research and general	<u>5,197</u>	<u>5,013</u>
Total expendable restricted net assets	<u>\$ 7,135</u>	<u>\$ 7,366</u>

Restricted nonexpendable net assets as of June 30, 2010 and 2009, represent the principal amounts of permanent endowments restricted to investment in perpetuity. Investment earnings for the Hospital's permanent endowments are expendable for purposes restricted by the donors primarily for patient assistance purposes.

3. DESIGNATED ASSETS

Of the \$415,012,000 and \$341,550,000 of unrestricted net assets reported as of June 30, 2010 and 2009, respectively, \$155,966,000 and \$155,568,000 as of June 30, 2010 and 2009, respectively, has been designated by the Hospital's board of directors for capital replacement and debt retirement. Designated funds remain under the control of the board of directors, which may, at its discretion, later use the funds for other purposes.

4. TRANSACTIONS WITH RELATED PARTIES

The Hospital receives certain administrative and other general services from the University and provides direct support for the educational, research, and clinical activities of the University through the Affiliation Agreement. Direct costs associated with these services and support approximated \$52,006,000 and \$49,701,000 in 2010 and 2009, respectively. The Hospital committed to support certain UWSMPH and University of Wisconsin School of Nursing capital expenditures as incurred, up to a maximum of \$19,102,000, of which \$10,447,000 was paid through June 30, 2010, with the remaining \$8,655,000 to be paid as the capital projects commence in agreed-upon installments. At June 30, 2010 and 2009, the Hospital had \$2,402,000 and \$2,115,000 in receivables, respectively, and \$5,622,000 and \$6,475,000 in payables, respectively, with the University.

University Health Care, Inc. (UHC) is a Wisconsin nonstock, not-for-profit corporation. UHC primarily is engaged in furthering the teaching, research, and service functions of the Hospital, UWSMPH, and the University of Wisconsin Medical Foundation (UWMF), each of which are members of UHC. UHC acquired 100% of the equity interest of Unity Health Plans effective January 1, 2005. This acquisition was funded 60% by the Hospital and 40% by UWMF. By resolution of UHC and agreement by its members, the Hospital and UWMF shall indirectly hold 60% and 40%, respectively, of the equity and ownership rights of Unity Health Plans. The UWSMPH shall have no ownership rights or funding obligations in and to Unity Health Plans. The super majority rights for governance of Unity Health Plans do not grant control to either the Hospital or UWMF. As such, the Hospital's investment in Unity Health Plans through UHC is accounted for by the equity method. At June 30, 2010 and 2009, the Hospital had \$504,000 and \$328,000 in receivables, respectively, with Unity Health Plans and UHC. The Hospital received payments of \$44,595,000 and \$42,915,000 for the years ended June 30, 2010 and 2009, respectively, from UHC under a capitation agreement with Unity Health Plans.

e-Care of Wisconsin, LLC, was formed in May 2008 as a limited liability company; UHC is the sole member of the LLC. The Board of Managers of e-Care of Wisconsin, LLC consists of three appointees from the Hospital and two appointees each from UWWMF and UHC; as such the Hospital's investment is accounted for on the equity basis. Capital contributions to the LLC are funded 70% by the Hospital and 30% by UWWMF as per resolution of the Board of Directors of UHC. The Hospital has made capital contributions totaling \$2,800,000 to e-Care of Wisconsin, LLC.

UHC was audited as of December 31, 2009 and 2008, and for the years then ended. A summary of certain financial data for UHC as of and for the years ended December 31, 2009 and 2008, is as follows (in thousands):

	2009	2008
Total assets	\$ 117,429	\$ 105,023
Unrestricted net assets	51,816	45,744
Total revenue	353,957	316,246
Excess of revenues over expenses	8,213	3,627

Wisconsin Therapies, Inc., a not-for-profit corporation controlled by the Hospital, was organized for the purpose of forming a limited liability company with Chartwell Midwest. Wisconsin Therapies, Inc. is a holding company that has no assets, liabilities, or operations. The limited liability company is called Chartwell Wisconsin Enterprises, LLC, and is the sole member in Chartwell Midwest Wisconsin, LLC, and a single-member limited liability company providing tertiary home care, infusion therapy and other home health services to acutely and chronically ill patients primarily in Wisconsin. The Hospital's investment in the company is adjusted for equity in undistributed earnings of Chartwell Wisconsin Enterprises, LLC.

Wisconsin Dialysis, Inc., is a not-for-profit corporation which is owned 45%, 45%, and 10% among the Hospital, Meriter Hospital Inc., and UWWMF, respectively. The Hospital's investment is adjusted for equity in undistributed earnings of Wisconsin Dialysis, Inc. At June 30, 2010 and 2009, the Hospital had \$215,000 and \$204,000 in receivables, respectively, from Wisconsin Dialysis, Inc.

On September 30, 2005, the Hospital purchased a 1/3 membership interest in Madison Surgery Center Inc., a nonstock, not-for-profit corporation for \$5,000,000. The other 1/3 members include Meriter Hospital, Inc. and UWWMF. The Hospital's investment in the company is adjusted for equity in undistributed earnings and capital distributions of Madison Surgery Center, Inc.

Sleep Equipment of Wisconsin, LLC, was organized in September 2007 as a Wisconsin limited liability company whose members are Meriter Hospital, Inc. and the Hospital. In December 2007, each member made capital contributions of \$175,000. The Hospital's investment is adjusted for equity in the undistributed earnings/loss of Sleep Equipment of Wisconsin, LLC. Because of proposed regulatory changes regarding durable medical equipment billing, as well as other issues related to the planned business model, the joint venture partners of Sleep Equipment of Wisconsin, LLC, agreed to dissolve the organization with final dissolution in June 2009.

Madison United Healthcare Linen, Ltd., (formerly Madison United Hospital Laundry) was established in 1966 to provide laundry services to hospitals, long-term care facilities and clinics. The Hospital is a 44.5% member, along with three other hospitals. The Hospital's investment in the company is adjusted for equity in undistributed earnings on Madison United Healthcare Linen, Ltd.

Madison Environmental Resourcing, Inc., (formerly Madison Energy Recovery), was established in 1986 to provide waste treatment and disposal of solid waste material for member organizations operating in the healthcare industry. The Hospital is a 40.9% member, together with Meriter Hospital, Inc. and St. Mary's Hospital. The Hospital's investment in the company is adjusted for equity in undistributed earnings in Madison Environmental Resourcing, Inc.

Investments in joint ventures as of June 30, 2010 and 2009, is comprised of the following (in thousands):

	2010	2009
University Health Care, Inc.	\$ 32,390	\$ 28,186
e-Care of Wisconsin, LLC	895	1,473
Wisconsin Therapies, Inc.	1,348	1,440
Wisconsin Dialysis, Inc.	1,788	1,717
Madison Surgery Center, Inc.	6,934	7,034
Madison United Healthcare Linen, Ltd.	3,933	3,790
Madison Environmental Resourcing, Inc.	<u>612</u>	<u>602</u>
 Total	 <u>\$ 47,900</u>	 <u>\$ 44,242</u>

5. DEPOSITS AND INVESTMENTS

The Hospital's deposits and investments at June 30, 2010 and 2009, are categorized to give an indication of the level of custodial credit risk assumed by the Hospital (in thousands):

Bank Deposits	2010	2009
FDIC — Insured	\$ 141	\$ 141
Uninsured, collateralized, or collateralized by securities held by the pledging institution or by its trust department or agent in other than the Hospital's name	45,918	61,993
Petty cash	<u>78</u>	<u>77</u>
 Total bank balances	 <u>\$46,137</u>	 <u>\$62,211</u>
 Carrying amount	 <u>\$50,049</u>	 <u>\$49,317</u>

Investments — The board of directors has authorized management to invest in debt and equity securities through an investment in the University of Wisconsin Foundation — Restricted Fund, the University of Wisconsin Foundation — Endowment Fund, and Intermediate Term Bond Fund managed by an investment advisor (in thousands):

	2010	2009
Uninsured and unregistered — cash equivalents and investment in an intermediate term bond fund:		
Cash equivalents	\$ 51,664	\$ 7,692
Investments	<u>74,481</u>	<u>62,271</u>
	<u>126,145</u>	<u>69,963</u>
Interest in cash equivalents and investments with the University of Wisconsin Foundation, which are uncategorized:		
Cash equivalents	52,616	35,632
Investments	<u>195,617</u>	<u>181,040</u>
	<u>248,233</u>	<u>216,672</u>
Total	<u>\$ 374,378</u>	<u>\$ 286,635</u>
Carrying amount	<u>\$ 374,378</u>	<u>\$ 286,635</u>

Cash and investments with the University of Wisconsin Foundation are uncategorized as ownership does not depend on control of individual securities. The carrying amounts of deposits and investments shown above are included in the Hospital's balance sheets at June 30, 2010 and 2009, as follows (in thousands):

	2010	2009
Deposits	\$ 50,049	\$ 49,317
Investments	<u>374,378</u>	<u>286,635</u>
Total	<u>\$ 424,427</u>	<u>\$ 335,952</u>

The amounts of deposits and investments are included at June 30, 2010 and 2009, in the following balance sheet captions (in thousands):

	2010	2009
Cash and cash equivalents	\$ 48,823	\$ 47,051
Noncurrent cash and investments	<u>375,604</u>	<u>288,901</u>
Total cash, cash equivalents, and investments	<u>\$ 424,427</u>	<u>\$ 335,952</u>

Noncurrent cash and investments are invested at June 30, 2010 and 2009, as follows (in thousands):

	2010	2009
Pooled investment funds on deposit with the University of Wisconsin Foundation:		
Pooled Restricted Fund	\$ 159,786	\$ 159,114
Pooled Endowment Fund	87,987	56,774
Funds held with trustee money market fund	1,650	3,013
Intermediate term bond fund	126,145	69,963
Other	<u>36</u>	<u>37</u>
 Total	 <u>\$ 375,604</u>	 <u>\$ 288,901</u>

6. CAPITAL ASSETS

Capital asset additions, retirements, and balances for the year ended June 30, 2010, were as follows (in thousands):

	Balance June 30, 2009	Additions and Transfers	Retirements	Balance June 30, 2010
Capital assets not being depreciated:				
Land	\$ 11,780	\$ 2,605	\$ -	\$ 14,385
Land improvements	1,715	246	-	1,961
Construction in progress	<u>13,251</u>	<u>(8,463)</u>	<u>-</u>	<u>4,788</u>
Total	<u>26,746</u>	<u>(5,612)</u>	<u>-</u>	<u>21,134</u>
Capital assets being depreciated:				
Buildings and improvements	481,477	17,094	(60)	498,511
Equipment	<u>228,828</u>	<u>19,197</u>	<u>(7,481)</u>	<u>240,544</u>
Total	<u>710,305</u>	<u>36,291</u>	<u>(7,541)</u>	<u>739,055</u>
Less accumulated depreciation and amortization for:				
Buildings and improvements	184,111	18,528	(60)	202,579
Equipment	<u>142,545</u>	<u>30,204</u>	<u>(7,143)</u>	<u>165,606</u>
Total	<u>326,656</u>	<u>48,732</u>	<u>(7,203)</u>	<u>368,185</u>
Total capital assets being depreciated — net	<u>383,649</u>	<u>(12,441)</u>	<u>(338)</u>	<u>370,870</u>
Total capital assets	<u>\$ 410,395</u>	<u>\$ (18,053)</u>	<u>\$ (338)</u>	<u>\$ 392,004</u>

Construction in progress at June 30, 2010, consisted principally of costs incurred for the inpatient unit remodeling and a utility expansion project at the main hospital building. The construction projects are being financed with cash from operations.

Capital asset additions, retirements, and balances for the year ended June 30, 2009, were as follows (in thousands):

	Balance June 30, 2008	Additions and Transfers	Retirements	Balance June 30, 2009
Capital assets not being depreciated:				
Land	\$ 11,771	\$ 9	\$ -	\$ 11,780
Land improvements	1,659	56	-	1,715
Construction in progress	<u>22,959</u>	<u>(9,708)</u>	<u>-</u>	<u>13,251</u>
Total	<u>36,389</u>	<u>(9,643)</u>	<u>-</u>	<u>26,746</u>
Capital assets being depreciated:				
Buildings and improvements	445,679	35,988	(190)	481,477
Equipment	<u>208,426</u>	<u>30,464</u>	<u>(10,062)</u>	<u>228,828</u>
Total	<u>654,105</u>	<u>66,452</u>	<u>(10,252)</u>	<u>710,305</u>
Less accumulated depreciation and amortization for:				
Buildings and improvements	166,641	17,660	(190)	184,111
Equipment	<u>125,742</u>	<u>26,344</u>	<u>(9,541)</u>	<u>142,545</u>
Total	<u>292,383</u>	<u>44,004</u>	<u>(9,731)</u>	<u>326,656</u>
Total capital assets being depreciated — net	<u>361,722</u>	<u>22,448</u>	<u>(521)</u>	<u>383,649</u>
Total capital assets	<u>\$398,111</u>	<u>\$12,805</u>	<u>\$ (521)</u>	<u>\$410,395</u>

Construction in progress at June 30, 2009, consisted principally of costs incurred for the expansion of radiotherapy into the Wisconsin Institutes for Medical Research building, remodeling for Clinic expansions at the main hospital building, and improvements to the off-campus facility. The construction projects are being financed with cash from operations and Series 2009C bonds for the off-campus facility renovation.

Total remaining commitments on capital asset purchases and the renovation and construction projects approximated \$571,000 at June 30, 2010.

The creation of the American Family Children's Hospital represented the Hospital's first major facility funded in partnership with private donors. Building on a \$10 million founding gift from American Family Insurance Corp., a \$41 million campaign for the construction of the new Children's Hospital began in 2003. As of June 30, 2010 and 2009, \$37.5 million and \$37.1 million, respectively, has been received and \$1.1 million and \$1.9 million, respectively, of net present value pledges receivable has been recorded in the financial statements as a capital donation in accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*.

7. LONG-TERM DEBT

Changes in long-term debt for the years ended June 30, 2010 and 2009, were as follows (in thousands):

	Balance June 30, 2009	Additions	Payments and Amortization	Balance June 30, 2010	Amounts Due Within One Year
Amounts payable to the State under capital lease agreements for:					
General Obligation Bonds	\$ 281	\$ -	\$ 6	\$ 275	\$ 6
Refunding Bonds	<u>7,390</u>	<u>-</u>	<u>1,797</u>	<u>5,593</u>	<u>1,705</u>
Total payable to the State	7,671	-	1,803	5,868	1,711
Hospital Revenue Bonds:					
Series 2000	1,315	-	1,315	-	-
Series 2002B	6,910	-	1,705	5,205	1,800
Series 2008A	50,375	-	315	50,060	515
Series 2008B	61,000	-	-	61,000	-
Series 2009A	57,070	-	-	57,070	-
Series 2009B	59,345	-	555	58,790	1,960
Series 2009C	5,300	-	120	5,180	249
Hospital Equipment Loan	<u>8,525</u>	<u>-</u>	<u>1,190</u>	<u>7,335</u>	<u>1,246</u>
Total long-term debt	257,511	-	7,003	250,508	7,481
Series 2000 Refunding Deferred Loss	(6,168)	-	(312)	(5,856)	-
Series 1997 Refunding Deferred Loss	(256)	-	(14)	(242)	-
Series 2004 Refunding Deferred Loss	(446)	-	(17)	(429)	-
Series 2002A Refunding Deferred Loss	(632)	-	(27)	(605)	-
Series 2005 Refunding Deferred Loss	(416)	-	(21)	(395)	-
Premium on long-term debt	<u>241</u>	<u>-</u>	<u>64</u>	<u>177</u>	<u>-</u>
Long-term debt including premium	<u>\$249,834</u>	<u>\$ -</u>	<u>\$ 6,676</u>	<u>\$243,158</u>	<u>\$7,481</u>

	Balance June 30, 2008	Additions	Payments and Amortization	Balance June 30, 2009	Amounts Due Within One Year
Amounts payable to the State under capital lease agreements for:					
General Obligation Bonds	\$ 286	\$ -	\$ 5	\$ 281	\$ 6
Refunding Bonds	<u>9,432</u>	<u>-</u>	<u>2,042</u>	<u>7,390</u>	<u>1,797</u>
Total payable to the State	9,718	-	2,047	7,671	1,803
Hospital Revenue Bonds:					
Series 2000	2,515	-	1,200	1,315	1,315
Series 2002A	55,600	-	55,600	-	-
Series 2002B	8,525	-	1,615	6,910	1,705
Series 2005	58,590	-	58,590	-	-
Series 2008A	50,375	-	-	50,375	315
Series 2008B	61,000	-	-	61,000	-
Series 2009A	-	57,070	-	57,070	-
Series 2009B	-	59,345	-	59,345	555
Series 2009C	-	5,300	-	5,300	120
Hospital Equipment Loan	<u>-</u>	<u>9,283</u>	<u>758</u>	<u>8,525</u>	<u>1,190</u>
Total long-term debt	246,323	130,998	119,810	257,511	7,003
Series 2000 Refunding Deferred Loss	(6,481)	-	(313)	(6,168)	-
Series 1997 Refunding Deferred Loss	(270)	-	(14)	(256)	-
Series 2004 Refunding Deferred Loss	(464)	-	(18)	(446)	-
Series 2002A Refunding Deferred Loss	-	(641)	(9)	(632)	-
Series 2005 Refunding Deferred Loss	-	(423)	(7)	(416)	-
Premium on long-term debt	<u>306</u>	<u>-</u>	<u>65</u>	<u>241</u>	<u>-</u>
Long-term debt including premium	<u>\$239,414</u>	<u>\$129,934</u>	<u>\$119,514</u>	<u>\$249,834</u>	<u>\$7,003</u>

The amounts payable to the State under capital lease agreements represent portions of the respective obligations for which repayment has been assigned to the Hospital in connection with the financing of the Hospital's facilities and equipment (see Note 1).

In March 2000, the Hospital issued \$56,500,000 of Hospital Revenue Bonds, Series 2000 ("Series 2000 Bonds"). In September 2005, the Hospital refunded \$52,460,000 of the outstanding bonds with Variable Rate Demand Hospital Revenue Bonds, Series 2005. Principal payments on the remaining Series 2000 Bonds were paid in April 2010. Interest rates range from 5.35% to 5.50% and interest was payable semiannually on April 1 and October 1 of each year. The effective annual interest rate was 5.50% and 5.70% in 2010 and 2009, respectively.

In October 2002, the Hospital issued \$68,500,000 of Hospital Revenue Bonds, Series 2002 ("Series 2002 Bonds") consisting of \$55,600,000 Series 2002A Short-term Adjustable Securities and \$12,900,000 Series 2002B Fixed Interest Rate Bonds. The bond proceeds were designated to finance-qualified capital projects. In March 2009, the Hospital refunded \$55,600,000 of the outstanding Series 2002A bonds with Variable Rate Demand Revenue Bonds, Series 2009A. The refunding of the Series 2002A bonds resulted in the recognition of a loss of \$1,652,000 due to the unamortized insurance premium and recognition of a deferred loss of \$641,000 for other unamortized deferred costs of the Series 2002A. Principal payments on the remaining Series 2002B Bonds range from \$1,505,000 to \$1,900,000 due annually in April 2011 through April 2013. Interest rates for the Series 2002B Bonds range from 5.25% to 5.50% and interest is payable semiannually on April 1 and October 1 of each year. The effective annual interest rate of the Series 2002A Bonds was 2.50% in 2009. The effective annual interest rate of the Series 2002B Bonds was 5.90% in 2010 and 5.50% in 2009.

In October 2002, the Hospital entered into an interest rate swap in order to convert a portion of the Series 2002A Short-term Adjustable Rate Securities to fixed rates. The notional amount of this swap agreement was \$21,350,000 at June 30, 2010 and 2009, which matures on April 1, 2022. This swap has been applied to the Series 2009A with the refunding of the Series 2002A bonds. The terms of the swap agreement are for the Hospital to pay the counterparty a fixed rate of 3.85% per annum, payable semiannually, and the Hospital to receive a floating rate of 70% of one-month London InterBank Offered Rate (LIBOR) per annum, payable monthly. In 2010 and 2009, the effective interest rate received by the Hospital was 0.20% and 1.00%, respectively. The Hospital will be exposed to variable rates if the counterparty to the swap defaults or if the swap is terminated. The swap agreement includes a bilateral additional termination event provision. Under the provision, either party has the option, but not the obligation, to terminate the swap transaction if the other party gets downgraded below BBB- by S&P or below Baa3 by Moody's. At June 30, 2010, the Hospital's rating is A+ from S&P and A1 from Moody's and the counterparty's rating is AA- from S&P and Aa1 from Moody's. The Hospital does not intend to terminate this agreement. The swap exposes the Hospital to basis risk should the relationship between LIBOR and weekly variable rate converge, changing the synthetic rate on the bonds. The fair value of the swap agreement was \$(2,965,250) and \$(2,132,882) at June 30, 2010 and 2009, respectively. As of June 30, 2010 and 2009, the Hospital was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap becomes positive, the Hospital would be exposed to credit risk in the amount of the swap's fair value. With the adoption of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* in fiscal year 2010, the fair value of the swap agreement is reflected in other long-term liabilities on the financial statements at June 30, 2010. GASB Statement No. 53 also requires that derivative instruments be evaluated for effectiveness. The Hospital has elected to classify the swap agreement as ineffective and reports the change in the fair value of the swap agreement as nonoperating revenue (expense) on the Statement of Revenues, Expenses and Changes in Net Assets for the year-ended June 30, 2010.

In November 2004, the Hospital entered into an interest rate swap in order to convert a portion of the Series 1997 Variable Rate Demand Bonds to fixed rates. This swap has been applied to the 2008B bonds with the refunding of Series 1997 bonds. The notional amount of this swap agreement was \$26,450,000 and \$26,750,000 at June 30, 2010 and 2009, respectively, which matures on April 1, 2021. The terms of the swap agreement are for the Hospital to pay the counterparty a fixed rate of 3.45% per annum, payable semiannually, and the Hospital to receive a floating rate of 70% of one-month LIBOR per annum, payable monthly. In 2010 and 2009, the effective interest rate received by the Hospital was 0.20% and 1.00%, respectively. The Hospital will be exposed to variable rates if the counterparty to the swap defaults or if the swap is terminated. The swap agreement includes a bilateral additional termination event provision. Under the provision, either party has the option, but not the obligation, to terminate the swap transaction if the other party gets downgraded below BBB- by S&P or below Baa3 by Moody's. At June 30, 2010, the Hospital's rating is A+ from S&P and A1 from Moody's and the counterparty's rating is AA- from S&P and Aa1 from Moody's. The Hospital does not intend to terminate this agreement. The swap exposes the Hospital to basis risk should the relationship between LIBOR and variable rate converge, changing the synthetic rate on the bonds. The fair value of the swap agreement was \$(2,843,861) and \$(1,863,602) at June 30, 2010 and 2009, respectively. As of June 30, 2010 and 2009, the Hospital was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap becomes positive, the Hospital would be exposed to credit risk in the amount of the swap's fair value. With the adoption of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* in fiscal year 2010, the fair value of the swap agreement is reflected in other long-term liabilities on the financial statements at June 30, 2010. GASB Statement No. 53 also requires that derivative instruments be evaluated for effectiveness. The Hospital has elected to classify the swap agreement as ineffective and reports the change in the fair value of the swap agreement as nonoperating revenue (expense) on the Statement of Revenues, Expenses and Changes in Net Assets for the year-ended June 30, 2010.

In September 2005, the Hospital issued \$59,770,000 of Variable Rate Demand Hospital Revenue Bonds, Series 2005 (“Series 2005 Bonds”). The bond proceeds were designated to refund a portion of the Series 2000 Bonds. Interest was payable monthly. In 2009, the effective interest rate was 3.10%. In March 2009, the Hospital refunded \$58,095,000 of the outstanding Series 2005 bonds with Variable Rate Demand Hospital Revenue Bonds, Series 2009B and transferred the April 2009 principal payment of \$495,000 into escrow. The refunding of the Series 2005 Bonds resulted in the recognition of a loss of \$889,000 due to the unamortized insurance premium and recognition of a deferred loss of \$423,000 for other unamortized deferred costs of the Series 2005 Bonds.

In September 2005, the Hospital entered into an interest rate swap in order to convert the Series 2005 Variable Rate Demand Hospital Revenue Bonds to fixed rates. This swap has been applied to the Series 2009B with the refunding of the Series 2005 Bonds. The notional amount of the swap agreement was \$59,770,000 at June 30, 2010, and \$58,095,000 at June 30, 2009, which matures on April 1, 2029. The terms of the swap agreement are for the Hospital to pay the counterparty a fixed rate of 3.31% per annum, payable monthly, and the Hospital will receive a floating rate of 58.3% of one-month LIBOR per annum plus 0.36%, payable monthly. In 2010 and 2009, the effective interest rate received by the Hospital was 0.50% and 1.20%, respectively. The Hospital will be exposed to variable rates if the counterparty to the swap defaults or if the swap is terminated. The swap agreement includes a bilateral additional termination event provision. Under the provision, either party has the option, but not the obligation, to terminate the swap transaction if the other party gets downgraded below BBB- by S&P or below Baa3 by Moody’s. At June 30, 2010, the Hospital’s rating is A+ from S&P and A1 from Moody’s and the counterparty’s rating is A from S&P and A1 from Moody’s. The Hospital does not intend to terminate this agreement. The swap exposes the Hospital to basis risk should the relationship between LIBOR and variable rate converge, changing the synthetic rate on the bonds. The fair value of the swap agreement was \$(6,439,493) and \$(4,349,009) at June 30, 2010 and 2009, respectively. As of June 30, 2010 and 2009, the Hospital was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap becomes positive, the Hospital would be exposed to credit risk in the amount of the swap’s fair value. With the adoption of GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* in fiscal year 2010, the fair value of the swap agreement is reflected in other long-term liabilities on the financial statements at June 30, 2010. GASB Statement No. 53 also requires that derivative instruments be evaluated for effectiveness. The Hospital has elected to classify the swap agreement as ineffective and reports the change in the fair value of the swap agreement as nonoperating revenue (expense) on the Statement of Revenues, Expenses and Changes in Net Assets for the year-ended June 30, 2010.

In March 2009, insurance on the 2005 swap agreement was removed and the collateral posting provisions of the swap agreement became effective. The collateral amount required is determined based on the fair value of the swap, less the applicable threshold of \$7,000,000 at the Hospital’s current rating. Collateral valuations are performed daily, based on the official market closing curve. While the counterparty holds the collateral, the funds will earn the overnight Federal Funds interest rate, payable monthly.

In May 2008, the Hospital issued \$50,375,000 of Fixed Rate Bonds, Series 2008A (“Series 2008A Bonds”) through a private placement. The bond proceeds were used to refund \$50,000,000 of Variable Rate Demand Hospital Revenue Bonds, Series 1997. Principal payments on the Series 2008A Bonds, ranging from \$515,000 to \$5,245,000, are due annually in April 2011 through April 2026. Interest is payable semi-annually. In 2010 and 2009, the effective interest rate was 5.30% and 5.30%, respectively.

In June 2008, the Hospital issued \$61,000,000 of Series 2008B Bonds. The bonds proceeds were used to refund \$60,000,000 of Hospital Revenue Bonds consisting of Short-term Adjustable Rate Securities, Series 2004. Principal payments on the Series 2008B Bonds, ranging from \$9,950,000 to \$15,275,000, are due annually in April 2030 through April 2034. Series 2008B Bonds bear interest at a daily rate

determined by a remarketing agent. Interest is payable monthly. In 2010 and 2009, the effective interest rate was 0.20% and 1.10%, respectively.

In September 2008, the Hospital entered into an equipment financing agreement with GE Government Finance, Inc., in the amount of \$9,283,434. Principal and interest payments are made monthly commencing on November 1, 2008, for seven years. In 2010 and 2009, the effective interest rate was 4.50% and 4.60%, respectively.

In March 2009, the Hospital issued \$57,070,000 of Variable Rate Demand Revenue Refunding Bonds, Series 2009A (“Series 2009A Bonds”), secured by an irrevocable transferable direct-pay letter of credit issued by a commercial bank. The bond proceeds were used to refund \$55,600,000 of Hospital Revenue Bonds consisting of Short-Term Adjustable Rate Securities, Series 2002A. Principal payments on the Series 2009A Bonds, ranging from \$500,000 to \$4,035,000, are due annually in April 2013 through April 2032. Series 2009A Bonds bear interest at a weekly rate determined by a remarketing agent. Interest is payable monthly. In 2010 and 2009, the effective interest rate was 0.20% and 0.40%, respectively.

In March 2009, the Hospital issued \$59,345,000 of Variable Rate Demand Revenue Refunding Bonds, Series 2009B (“Series 2009B Bonds”). The bond proceeds were used to refund \$58,095,000 of Variable Rate Demand Revenue Refunding Bonds, Series 2005. Principal payments on the Series 2009B Bonds, ranging from \$1,960,000 to \$8,195,000, are due annually in April 2011 through April 2029. Series 2009B Bonds bear interest at a weekly rate determined by a remarketing agent. Interest is payable monthly. In 2010 and 2009, the effective interest rate was 0.20% and 0.40%, respectively.

In June 2009, the Hospital issued \$5,300,000 of Fixed Rate Hospital Revenue Bonds, Series 2009C (“Series 2009C Bonds”) through a private placement. The bond proceeds were designated to finance qualified capital projects. Principal payments on the Series 2009C Bonds, ranging from \$248,000 to \$478,000, are due bi-annually beginning in April 2011 through October 2024. Series 2009C Bonds bear interest from June 30, 2009 through October 1, 2012, at the initial fixed rate of 5.07% per annum. The interest rate will be reset every three years and is payable bi-annually. In 2010, the effective interest rate was 5.10%.

The Series 2000 Bonds, Series 2002 Bonds, Series 2008A Bonds, Series 2008B, Series 2009A Bonds, and Series 2009B Bonds are collateralized by a security interest in substantially all of the Hospital’s revenue. The borrowing agreements contain various covenants and restrictions, including compliance with the terms and conditions of a Lease Agreement (see Note 1) and provisions limiting the amount of additional indebtedness that may be incurred. The borrowing agreements also require the establishment and maintenance of certain funds under the control of a trustee (see Note 5). UWHCA is in compliance with all debt covenants at June 30, 2010 and 2009.

The Series 2008B, Series 2009A Bonds, and Series 2009B Bonds with variable interest rates are secured by irrevocable transferable direct-pay letters of credit issued by a commercial bank. The initial letter of credit agreements have stated expiration dates of five (5) years. The letter of credit securing the 2008B bonds requires draws to be repaid on the earliest of the following dates to occur: (a) the date the bond is remarketed; (b) the date sixty (60) months from the date of the draw; or (c) the stated expiration date of the letter of credit. The letters of credit securing the 2009A and 2009B bonds do not require any principal payments within the first year of the draw; interest payments are due monthly. Outstanding principal payments under the letters of credit would revert to a Term Out Loan after the first year. Any obligations under the Term Out Loans are repayable in equal quarterly installments based on a four year straight-line amortization commencing on the 367th day after the draw with final payments of the outstanding balances on the earliest to occur of: (a) the date on which the letter of credit is replaced or substituted; (b) five (5) years following the date of the draw preceding such Term Out Loan; (c) the date

the bonds are successfully remarketed; or (d) the date on which all amounts due have been accelerated pursuant to the letters of credit. At June 30, 2010 and 2009, there were no amounts outstanding under the letters of credit.

Legislation (see Note 1) which had limited the Hospital's total borrowings, exclusive of amounts payable to the State, to \$235,000,000, with limited exceptions, was amended in April 2008. The statute now requires the Hospital to obtain approval of additional bond issuance from its Board of Directors, maintain an unenhanced bond rating in the category of "A" or better from Standard and Poor's Corporation and Moody's Investor Service, Inc., and notify the State Joint Committee on Finance.

Scheduled principal and interest repayments on long-term debt, including the effect of the swaps based on the effective interest rate at June 30, 2010, are as follows (in thousands):

Years Ending June 30	Principal	Interest	Interest Rate Swap — Net	Total
2011	\$ 7,481	\$ 4,107	\$ 3,147	\$ 14,735
2012	7,840	3,817	3,076	14,733
2013	8,190	3,528	2,995	14,713
2014	8,562	3,247	2,882	14,691
2015	8,931	3,038	2,685	14,654
2016–2020	41,955	12,266	9,922	64,143
2021–2025	49,863	6,694	4,360	60,917
2026–2030	58,700	1,261	1,222	61,183
2031–2034	58,985	287		59,272
Deferred loss on refunding of Series 2000 Bonds	(5,856)			(5,856)
Deferred loss on refunding of Series 1997 Bonds	(242)			(242)
Deferred loss on refunding of Series 2004 Bonds	(428)			(428)
Deferred loss on refunding of Series 2002A Bonds	(605)			(605)
Deferred loss on refunding of Series 2005 Bonds	(395)			(395)
Premium on 2002B bonds	177			177
	<u>\$ 243,158</u>	<u>\$ 38,245</u>	<u>\$ 30,289</u>	<u>\$ 311,692</u>

8. DEFEASANCE OF DEBT

On September 20, 2005, the Hospital issued \$59,770,000 in Variable Rate Demand Revenue Refunding Bonds, Series 2005 with an initial interest rate of 2.69% per annum at the time of issuance to advance refund \$52,460,000 of outstanding Bond Issue Series 2000 with an interest rate range of 5.6% to 5.85%. The net proceeds of \$58,180,000 (after payment of \$1,590,000 in issuance costs) were used to purchase state and local government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the refunded portion of the Fixed Rate Serial and Term Hospital Revenue Bonds, Series 2000 with maturity dates on or after April 1, 2011. As a result, the refunded portion of the Bond Issue Series 2000 are considered to be defeased and the

liability for those bonds has been removed from the balance sheet. The amount outstanding related to the defeased portion of the 2000 Series Bond is \$0 at June 30, 2010 and \$52,460,000 at June 30, 2009.

Although the advance refunding resulted in the recognition of a deferred loss of \$7,339,000, the Hospital in effect reduced its aggregate debt service payments over the next 24 years by over \$14,000,000 and obtained an economic gain (difference between the present values of the debt service payments on the old and the new debt) of approximately \$9,000,000. The Hospital is amortizing the deferred loss to interest expense over the term of the debt using the straight-line method.

9. NET PATIENT SERVICE REVENUE

The Hospital has agreements with third-party payors that provide for reimbursement at amounts different from the Hospital's established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the Hospital's established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursements with major third-party payors is as follows:

Medicare — Inpatient acute care services rendered to Medicare beneficiaries and defined capital costs are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient services are reimbursed based on prospectively determined rates with separate payment classifications established for each distinct service rendered within the encounter. Inpatient nonacute services, medical education, and certain organ acquisition costs related to Medicare beneficiaries are paid based upon cost reimbursement methods, established fee screens, or a combination thereof. The Hospital is reimbursed for cost reimbursement items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits by the Medicare fiscal intermediary. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2006. The estimated receivables and payables to Medicare included in the financial statements include those cost reports that have not been audited by the Medicare fiscal intermediary.

Net patient service revenue for the years ended June 30, 2010 and 2009, included approximately \$1,870,000 and \$4,022,000, respectively, of retrospectively determined settlements from third-party payors and changes in estimates.

Medicaid — Inpatient services rendered to Medicaid beneficiaries are reimbursed similar to the method for Medicare inpatient acute care services. Differences from the Medicare method pertain to reimbursements for organ transplants, capital costs, and medical education costs. Medicaid outpatient services are paid on a predetermined rate per visit.

In February 2009, the State of Wisconsin established a tax assessment program on acute care hospitals with the intent to improve Medicaid reimbursement for Wisconsin hospitals. This assessment program has been approved by the Centers for Medicare and Medicaid Services and was retroactive to July 1, 2008.

The percentage of net patient service revenue applicable to services provided to Medicare and Medicaid patients was approximately 34% in 2010 and 33% in 2009.

Laws and regulations governing 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 impact of any change in estimates is recorded in the year the

change is determined. In management's opinion, the ultimate disposition of these uncertainties will not have a material adverse effect on the financial position of the Hospital or results of operations.

Other — The Hospital has also entered into reimbursement agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for reimbursements under these agreements includes capitation, prospectively determined rates per discharge, discounts from established rates, and prospectively determined per diem rates.

Capitation revenue with third-party payors comprised approximately 5% of net patient service revenue for each of the years ended June 30, 2010 and 2009.

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

	2010	2009
Medicare	27 %	23 %
Medicaid	14	9
Managed care	44	43
Indemnity	6	7
Other	<u>9</u>	<u>18</u>
Total	<u>100 %</u>	<u>100 %</u>

10. CHARITY CARE

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under its charity care policy. The approximate level of charity care provided (based on charges) during the years ended June 30, 2010 and 2009, was \$47,041,000 and \$40,306,000, respectively.

11. PENSION PLAN

Virtually all Hospital employees participate in the Wisconsin Retirement System (WRS), a cost sharing, multiple employer, defined-benefit public employee retirement system governed by Chapter 40 of the Wisconsin Statutes. All permanent employees expected to work over 600 hours per year are eligible to participate in the WRS. The Hospital employees participating in WRS are categorized as either Hospital Board or Hospital Authority employees. Covered general employees are required by statute to contribute 5% of their salary to the plan; however, the Hospital funds these contributions to the plan on behalf of the employees. The Hospital is required to contribute the remaining amounts necessary to pay the projected cost of defined future benefits.

The payroll for employees covered by WRS for the year ended June 30, 2010, was \$348,955,000; the employer's total payroll was \$362,189,000. The total required contributions, paid entirely by the employer, for the year ended June 30, 2010, were \$44,387,000.

The payroll for employees covered by WRS for the year ended June 30, 2009, was \$338,393,000; the employer's total payroll was \$350,091,000. The total required contributions, paid entirely by the employer, for the year ended June 30, 2009, were \$42,947,000.

Employees who retire at or after age 65 are entitled to receive a retirement benefit. Employees may retire at age 55 and receive reduced benefits. Retirement benefits are calculated as 1.6% of final average earnings for each year of creditable service. Final average earnings is the average of the employee's three highest year's earnings. Employees terminating covered employment before becoming eligible for a retirement benefit may withdraw their contributions and, by doing so, forfeit all rights to any subsequent benefit. For employees beginning participation on or after January 1, 1990, and no longer actively employed on or after April 24, 1998, creditable service in each of five years is required for eligibility for a retirement annuity. Participants employed prior to 1990 and on or after April 24, 1998, are immediately vested.

Each participating employer (including the Hospital) is required to make periodic payments to the WRS in respect of that employer's share of the unfunded prior service liability and sick leave conversion credit of the WRS. The statutorily required payments are based upon a percentage of covered wages. This percentage was designed to amortize the unfunded liability over 40 years, with 21 years remaining as of fiscal 2010. Each employer's total obligation is increased each year by an amount of interest, currently equal to 7.8% of the amount of the unfunded liability.

In December 2003, the State issued general obligation bonds and used the proceeds to retire the State's portion (including the Hospital Board employees) of the unfunded pension liability with WRS. The Hospital is required to reimburse the State for the Hospital's pro-rata share of the liability. The Hospital has recognized a liability of \$33,605,000 as of June 30, 2010, of which \$4,805,000 is payable in 2011 and is recorded in accrued expenses and \$28,800,000 is recorded in pension-related liabilities, payable in annual principal and interest payments to the State over approximately 21 years. The Hospital has recognized a liability of \$32,648,000 as of June 30, 2009, of which \$1,940,000 is payable in 2010 and is recorded in accrued expenses and \$30,708,000 is recorded in pension-related liabilities, payable in annual principal and interest payments to the State over approximately 22 years. Amounts payable to the State for the years 2011 through 2016 range from approximately \$2,800,000 to \$3,400,000.

The pension related liabilities for the Hospital as of June 30, 2010 and 2009, were \$64,432,000 and \$65,118,000, respectively, including current portion. The liability is made up of the Hospital Board portion, payable to the State as discussed above, and the Hospital Authority portion of \$30,827,000 and \$32,470,000, payable to WRS, as of June 30, 2010 and 2009, respectively.

Copies of the separately issued WRS financial report, that includes financial statements and required supplementary information, may be obtained by writing to Department of Employee Trust Funds, 801 West Badger Road, P.O. Box 7931, Madison, WI 53707-7931

12. RETIREE HEALTH INSURANCE PLAN

Plan Description — The Hospital is a part of the State's Health Insurance Program, which is an employer-sponsored program offering group medical coverage to eligible employees and retirees of the State and participating local government employers. Created under Chapter 40 of the Wisconsin State Statutes, the State Department of Employee Trust Funds and the Group Insurance Board have program administration and oversight responsibilities under Wis. Stat. Sections 15.165(2) and 40.03(6).

Under this plan, retired employees of the Hospital are allowed to pay the same healthcare premium as active employees, creating an implicit rate subsidy for retirees. This implicit rate subsidy, which is calculated to cover pre-age 65 retirees (since at age 65, retirees are required to enroll in Medicare when eligible), is treated as another postemployment benefit (OPEB). Retirees over age 65 may purchase Medicare supplemental and prescription benefit coverage through the plan.

The Department of Employee Trust funds issues a publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by writing to Department of Employee Trust Funds, 801 West Badger Road, PO Box 7931, Madison, WI 53707-7931.

Funding Policy — The health insurance plan is currently on as a “pay-as-you-go-basis.” GASB Statement No. 45 does not require funding of the OPEB expense and the Hospital does not intend to fund the net OPEB obligation. Retirees pay premiums directly to the plan either out-of-pocket or with their accumulated sick leave conversion credits. For fiscal year 2010, the Hospital contributed \$1.9 million to the plan for current assessments of the sick leave conversion credit benefit available to retirees for health insurance and approximately \$3.5 million of the payments due for the Hospital’s pension-related liabilities (as described in footnote 11) apply to sick leave conversion credits.

Annual OPEB Cost — The Hospital’s annual OPEB cost (expense), dollar amount of contributions, and components of the annual OPEB cost was as follows (in thousands):

	Hospital Authority	Hospital Board
Annual Required Contribution (ARC)	\$ 3,965	\$ 2,114
Interest on the net OPEB obligation	282	139
ARC adjustment with interest	<u>(276)</u>	<u>(136)</u>
Annual OPEB cost	3,971	2,117
Employer contribution	<u>(924)</u>	<u>(623)</u>
Change in the net OPEB obligation	3,047	1,494
Net OPEB obligation beginning balance	<u>5,122</u>	<u>2,532</u>
Net OPEB obligation ending balance	<u>\$ 8,169</u>	<u>\$ 4,026</u>

The Hospital’s annual OPEB cost, percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2010 was as follows:

	Fiscal Year Ended	Annual OPEB Cost	Percent of Annual OPEB Contributed	Net OPEB Obligation
Hospital Authority	6/30/2010	\$ 3,971	23.3 %	\$ 8,169
Hospital Authority	6/30/2009	3,319	29.4	5,122
Hospital Board	6/30/2010	2,117	29.4	4,026
Hospital Board	6/30/2009	1,828	36.4	2,532

Funded Status and Funding Progress — The funded status of the plan as of July 1, 2009, was as follows:

	Hospital Authority	Hospital Board
Actuarial accrued liability (AAL)	\$ 26,203	\$ 13,043
Actuarial value of plan assets	<u>-</u>	<u>-</u>
Unfunded actuarial accrued liability (UAAL)	<u>\$ 26,203</u>	<u>\$ 13,043</u>
Funded ratio (actuarial value of plan assets/AAL)	- %	- %
Covered payroll (active plan members)	\$ 241,556	\$ 104,731

Funded Status and Funding Progress — The funded status of the plan as of July 1, 2007, was as follows:

	Hospital Authority	Hospital Board
Actuarial accrued liability (AAL)	\$ 19,761	\$ 10,747
Actuarial value of plan assets	<u>-</u>	<u>-</u>
Unfunded actuarial accrued liability (UAAL)	<u>\$ 19,761</u>	<u>\$ 10,747</u>
Funded ratio (actuarial value of plan assets/AAL)	- %	- %
Covered payroll (active plan members)	\$ 223,332	\$ 96,830

The actuarial accrued liability calculation considers the retiree drug subsidy (RDS) provisions of Medicare Part D as a separate transaction. Therefore, the actuarial accrued liability, the annual required contribution of the employer (ARC), and the annual OPEB costs are determined without reduction of RDS payments. At June 30, 2010, the Medicare Part D portion included in the actuarial accrued liability is \$6.8 million.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents the transition year trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions — Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of the valuation and the historical pattern of sharing the benefit costs between employer and plan members to that point. In the actuarial valuation for fiscal year 2009-2010, the projected unit credit method was used. The actuarial assumptions included a 5.5% discount rate and an annual healthcare cost trend rate of 7.0% initially, reduced by decrements to an ultimate rate of 5.5% after 15 years. The unfunded actuarial accrued liability is being amortized as a 30-

year level percentage of pay amortization periods on a closed basis for the initial UAAL. The remaining amortization period was 28 years at June 30, 2010.

13. MALPRACTICE INSURANCE

The Hospital has occurrence-based coverage for July 1, 2002 through June 30, 2003, and has claims-made or tail coverage under various policies for claims made before and after that period. Losses in excess of the professional liability insurance are fully covered through the Hospital’s mandatory participation in the Injured Patient and Families Compensation Fund of the State of Wisconsin. The Injured Patient and Families Compensation Fund pays that portion of a medical malpractice claim which is in excess of the legal primary insurance limit prescribed under law, or the maximum liability limit for which the health provider is insured, whichever limit is greater. Most qualified health care providers permanently practicing or operating in the State of Wisconsin are required to pay Injured Patient and Families Compensation Fund operating fees. Risk of loss is retained by the fund. Noneconomic damages are capped in the State of Wisconsin. The Hospital has recorded in the financial statements its best estimate for the ultimate cost discounted at 4% of professional liability claims, including incurred but not reported claims.

14. LIABILITIES FOR WORKERS’ COMPENSATION CLAIMS

A reconciliation of changes in the aggregate liabilities for workers’ compensation claims for the years ended June 30, 2010 and 2009, is as follows (in thousands):

	Amount of Claims Liabilities Beginning of Year	Incurred Claims and Changes in Estimates	Payments on Claims	Amount of Claims Liabilities End of Year
2010	\$ 5,931	\$ 2,562	\$ (1,487)	\$ 7,006
2009	5,134	2,939	(2,142)	5,931

Workers’ compensation claim expense is included with employee benefits expense in the statements of revenues, expenses, and changes in net assets and accrued expenses in the balance sheets.

15. COMMITMENTS AND CONTINGENCIES

Leases — The Hospital leases buildings, equipment, and helicopter transport services under operating leases. Rental expense for cancelable and noncancelable operating leases was approximately \$18,383,000 and \$18,407,000 for 2010 and 2009, respectively, and is included in other expenses.

Future minimum payments for the next five years under operating leases that have initial or remaining noncancelable lease terms in excess of one year and under license agreements that have remaining noncancelable terms in excess of one year as of June 30, 2010, are as follows (in thousands):

2011	\$ 12,032
2012	5,563
2013	2,657
2014	1,318
2015	1,074
2016–2020	<u>4,267</u>
Total	<u>\$ 26,911</u>

Regulatory Investigations — The U.S. Department of Justice and other federal agencies are increasing resources dedicated to regulatory investigation and compliance audits of health care providers. The Hospital is subject to these regulatory efforts. Management is currently unaware of any regulatory matters which will have a material adverse effect on the Hospital's financial position or results of operations.

Other — The Hospital is subject to various legal proceedings and claims which are incidental to its normal business activities. In the opinion of management, the amount of ultimate liability with respect to these actions will not have a material adverse effect on the Hospital's financial position or results of operations.

* * * * *

REQUIRED SUPPLEMENTARY INFORMATION

UNIVERSITY OF WISCONSIN HOSPITALS AND CLINICS AUTHORITY

REQUIRED SUPPLEMENTARY INFORMATION

SCHEDULE OF PLAN FUNDING PROGRESS UNDER GASB STATEMENT NO. 45

AS OF JULY 1, 2007 (DATE OF ADOPTION) THROUGH JUNE 30, 2010

(In thousands)

	Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percent of Covered Payroll
Hospital Authority	7/1/2007	\$ -	\$ 19,761	\$ 19,761	- %	\$ 223,332	8.8 %
Hospital Authority	7/1/2009	\$ -	\$ 26,203	\$ 26,203	- %	\$ 241,556	10.8 %
Hospital Board	7/1/2007	\$ -	\$ 10,747	\$ 10,747	- %	\$ 96,830	11.1 %
Hospital Board	7/1/2009	\$ -	\$ 13,043	\$ 13,043	- %	\$ 104,731	12.5 %