

University of Arkansas for Medical Sciences

Financial Statements June 30, 2013 and 2012

University of Arkansas for Medical Sciences
Index
June 30, 2013 and 2012

	Page(s)
Management's Discussion and Analysis	1-11
Report of Independent Auditors	12
Financial Statements	
Statements of Net Position	14
Statements of Revenues, Expenses, and Changes in Net Position	15
Statements of Cash Flows	16-17
Notes to Financial Statements	18-44

University of Arkansas for Medical Sciences

Unaudited Management's Discussion and Analysis

June 30, 2013 and 2012

This discussion and analysis provides an overview of the financial position and changes in net position of the University of Arkansas for Medical Sciences (UAMS) for the fiscal years ended June 30, 2013 and 2012. UAMS is a state-assisted academic health center composed of:

- The Colleges of Medicine, Pharmacy, Nursing, Health Professions, Public Health, Graduate School, and Northwest Arkansas Satellite Campus with a combined enrollment of 2,867 and faculty numbering 1,396;
- The University Hospital of Arkansas (the Hospital), a tertiary care referral center with 453 acute care beds in use at June 30, 2013;
- Regional programs including Tele-education, Rural Hospital Program, and eight Area Health Education Centers (AHECs) located throughout the state;
- The Winthrop P. Rockefeller Cancer Institute;
- Harvey and Bernice Jones Eye Institute;
- Donald W. Reynolds Institute on Aging;
- Myeloma Institute for Research and Therapy;
- Psychiatric Research Institute (PRI);
- Jackson T. Stephens Spine and Neurosciences Institute; and
- Translational Research Institute.

The UAMS financial statements were prepared in accordance with standards issued by the Governmental Accounting Standards Board (GASB). The financial statement presentation required by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, provides a comprehensive, entity wide perspective of UAMS' assets, liabilities, net position, revenues, expenses, changes in net position, and cash flows. This discussion has been prepared by management and should be read in conjunction with the financial statements and notes following this section.

Overview of the Financial Statements

This financial report consists of three basic financial statements: the Statements of Net Position; the Statements of Revenues, Expenses, and Changes in Net Position; and the Statements of Cash Flows. These statements provide information about UAMS as a whole.

The Statements of Net Position present the financial position of UAMS and include all assets and liabilities. The difference between total assets and total liabilities is net position, which is an indicator of the current financial condition of UAMS. When revenues and other support exceed expenses, the result is an increase in net position. When the reverse occurs, there is a decrease in net position. Over time, increases or decreases in an institution's net position are one, but not the only, indicator of whether its financial health is improving or diminishing.

The Statements of Revenues, Expenses, and Changes in Net Position reflect the results of UAMS' operations. The purpose of these statements is to present the revenues earned and expenses incurred by UAMS, both operating and nonoperating, and any other changes in net position of UAMS.

The Statements of Cash Flows provide relevant information about the cash receipts and cash payments of UAMS. The Statements of Cash Flows also help users assess UAMS' ability to generate future net cash flows, its ability to meet its obligations as they come due, and its needs for external financing.

This discussion and analysis of UAMS' financial statements provides an overview of its financial activities for the fiscal years ended June 30, 2013 and 2012, with comparative information for the fiscal year ended June 30, 2011.

University of Arkansas for Medical Sciences
Unaudited Management's Discussion and Analysis
June 30, 2013 and 2012

Financial Highlights

UAMS' net position continued to improve in fiscal year 2013 with assets of \$1,334,056,000 and liabilities of \$550,465,000. Net position, which represents the residual interest in UAMS' assets after liabilities are deducted, was \$783,591,000 at June 30, 2013. Changes in net position represent the activities of UAMS, which result from revenues, expenses, gains, and losses, and are summarized for the years ended June 30, 2013, 2012, and 2011 as follows:

<i>(in thousands)</i>	2013	2012	2011
Operating revenues	\$ 1,163,244	\$ 1,180,953	\$ 1,111,413
Operating expenses	(1,229,975)	(1,244,286)	(1,140,792)
Nonoperating revenues	79,555	55,343	71,609
Other changes in net position	<u>5,435</u>	<u>41,909</u>	<u>17,237</u>
Increase in net position	<u>\$ 18,259</u>	<u>\$ 33,919</u>	<u>\$ 59,467</u>

Statements of Net Position

The Statements of Net Position present the financial position of UAMS at the end of the fiscal year and include all assets, liabilities, and net position of UAMS. Assets and liabilities are generally measured using current values, except for capital assets, which are stated at historical cost, or fair value at the date of donation, less an allowance for depreciation and amortization.

Net position is divided into three major categories. The first category, invested in capital assets, net of related debt, reflects the equity in property, plant, and equipment owned by UAMS. The next category is restricted net position, which is divided into two subcategories, nonexpendable and expendable. The corpus of nonexpendable restricted resources is only available for investment purposes. Expendable restricted net position is available for expenditure by UAMS, but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The final category is unrestricted net position, which is available for any lawful purpose of UAMS.

From the data presented, readers of the Statements of Net Position are able to determine the assets available to continue the operations of UAMS. They are also able to determine how much UAMS owes vendors and lending institutions. Finally, the Statements of Net Position provide a picture of the net position (assets minus liabilities) and its availability for expenditure by UAMS.

University of Arkansas for Medical Sciences
Unaudited Management's Discussion and Analysis
June 30, 2013 and 2012

A summary of UAMS' assets, liabilities, and net position is as follows:

<i>(in thousands)</i>	June 30,		
	2013	2012	2011
Assets			
Current assets	\$ 320,120	\$ 327,111	\$ 321,028
Noncurrent assets			
Investments	116,267	102,415	93,155
Capital assets, net	831,492	791,808	738,232
Other	66,177	45,939	75,708
Total assets	<u>\$ 1,334,056</u>	<u>\$ 1,267,273</u>	<u>\$ 1,228,123</u>
Liabilities			
Current liabilities	\$ 117,141	\$ 106,135	\$ 106,719
Noncurrent liabilities	433,324	395,806	389,991
Total liabilities	<u>550,465</u>	<u>501,941</u>	<u>496,710</u>
Net position			
Invested in capital assets, net of related debt	488,402	477,589	448,381
Restricted			
Expendable	110,999	112,146	88,905
Nonexpendable	29,868	28,150	27,126
Unrestricted	154,322	147,447	167,001
Total net position	<u>783,591</u>	<u>765,332</u>	<u>731,413</u>
Total liabilities and net position	<u>\$ 1,334,056</u>	<u>\$ 1,267,273</u>	<u>\$ 1,228,123</u>

Current assets consist of cash and cash equivalents, short-term investments, net accounts receivable, inventories, prepaid expenses, and notes and net student loans receivable. Noncurrent assets include long-term investments, notes and net student loans receivable, deposits and funds held in trust by others, net capital assets, and other noncurrent assets. Current liabilities consist primarily of accounts payable and accrued liabilities, deferred revenue, funds held in trust for others, estimated third-party payor settlements (Medicare and Medicaid), the current portion of compensated absences payable, bonds, notes, and capital leases payable. Noncurrent liabilities include primarily compensated absences payable, other postemployment benefits, and bonds, notes, and capital leases payable, net of current portion. Net position represents the residual interest in UAMS' assets after liabilities are deducted.

Fiscal Year 2013

UAMS' total assets increased by \$66,783,000 in fiscal year 2013. A review of the Statements of Net Position reveals that the increase consisted primarily of an increase in long-term investments of \$13,852,000, an increase of \$39,684,000 in net capital assets, an increase in noncurrent deposits and funds held in trust by others of \$20,984,000, along with a decrease in current assets of \$6,991,000 and in noncurrent notes and net student loans receivable of \$1,438,000.

The increase in long-term investments is due to a repositioning of investments previously held as cash equivalents and an increase in market values of the investments. The increase in net capital assets is primarily due to construction in progress related to the implementation of a new integrated clinical information system purchased from Epic Systems Corporation (EPIC), which is discussed more fully below. The increase in noncurrent deposits and funds held in trust by others was due to borrowing additional funds which have not yet been spent. The funds are held in escrow and drawn as needed to

University of Arkansas for Medical Sciences

Unaudited Management's Discussion and Analysis

June 30, 2013 and 2012

fund the capital projects. The decrease in noncurrent notes and net student loans receivable was due to scheduled repayments.

The decrease in current assets was primarily due to a decrease in cash and cash equivalents of \$31,684,000, used to fund operating activities and increase long-term investments, offset by increases in net nonpatient accounts receivable of \$20,767,000, primarily due to accrued contract and grant revenue, and prepaid expenses of \$3,074,000, primarily due to the early termination of a medical software maintenance contract which will be expensed in fiscal year 2014 as that contract ends.

Total liabilities increased by \$48,524,000 in fiscal year 2013. The majority of this increase is due to obtaining a \$60,000,000 note to help finance the EPIC license and implementation, as more fully discussed later in the Economic Outlook section. This was offset by the decision in early fiscal year 2013 to no longer provide a sick leave benefit for nonclassified personnel upon their retirement, resulting in a reduction in liabilities and fiscal year 2013 compensation and benefits expense of \$6,671,000.

Current liabilities increased by \$11,250,000 in total, primarily due to increases in accounts payable and accrued expenses of \$9,513,000 and \$9,635,000 in the current portion of bonds, notes, and capital leases payable offset by the decreases of \$4,181,000 in deferred revenue.

Fiscal Year 2012

UAMS' total assets increased by \$39,150,000 for fiscal year 2012. A review of the Statements of Net Position reveals that the increase consisted primarily of an increase in current assets of \$6,083,000, an increase in long-term investments of \$9,260,000, an increase of \$53,576,000 in net capital assets, a decrease in noncurrent deposits and funds held in trust by others of \$28,558,000, and a decrease in noncurrent notes and net student loans receivable of \$1,055,000.

Increases in current assets were noted in: cash and cash equivalents of \$7,978,000 due to the sale of investments; net patient accounts receivable of \$2,938,000 which was due to increased activity at College of Medicine's Faculty Group Practice (FGP); and, net nonpatient accounts receivable of \$3,966,000 primarily due to accrued contract and grant revenue. These increases were offset by decreases in: investments included in current assets of \$5,706,000 due to a repositioning of investments to higher yielding long-term investments; inventories of \$1,872,000 due to efforts to manage supplies more efficiently and prepaid expenses of \$1,241,000 primarily due to the recognition of software maintenance and licenses fees prepaid in the prior year.

The increase in long-term investments is due to a repositioning of investments previously held in short-term investments and an increase in market values of the investments. The decrease in noncurrent deposits and funds held in trust by others was due to the use of funds from bonds and notes for capital construction and purchases. The funds are held in escrow and drawn as needed to fund the capital projects. The decrease in noncurrent notes and net student loans receivable was due to scheduled repayments.

Total liabilities increased by \$5,231,000 in fiscal year 2012. A large portion of this overall increase is due to UAMS' early fiscal 2012 decision to provide nonclassified employees vested accumulated rights to receive sick leave benefits. The liability for this compensated absences benefit at June 30, 2012 totaled \$6,671,000. This decision was subsequently reversed in early fiscal year 2013. Therefore, fiscal year 2012 compensation and benefits expenses increased as a result of this liability.

Other larger contributors to the net increase in total liabilities for fiscal 2012 included \$4,592,000 in deferred revenue, primarily related to the Broadband Technology Opportunities Program (BTOP) federal grant, and \$2,952,000 in liabilities for postemployment benefits. Offsetting these increases were decreases of \$4,182,000 in bonds, notes, and capital leases payable, \$3,850,000 in accounts payable and accrued liabilities and \$3,202,000 in estimated third-party payor settlements.

Current liabilities decreased by \$584,000 in total, primarily due to the increases of \$4,592,000 in deferred revenue and \$1,702,000 in the current portion of bonds, notes, and capital leases payable offset by the

University of Arkansas for Medical Sciences
Unaudited Management's Discussion and Analysis
June 30, 2013 and 2012

decreases of \$3,850,000 in accounts payable and accrued liabilities and \$3,202,000 in estimated third-party payor settlements.

Statements of Revenues, Expenses, and Changes in Net Position

Changes in net position, as presented in the Statements of Net Position, are based on the activity presented in the Statements of Revenues, Expenses, and Changes in Net Position. A summary of UAMS' revenue, expenses, and changes in net position is as follows:

(in thousands)	Years Ended June 30,		
	2013	2012	2011
Operating revenues			
Student tuition and fees, net of scholarship allowances	\$ 29,701	\$ 25,754	\$ 23,576
Net patient services	886,577	876,544	868,685
Meaningful use	4,646	5,581	-
Sponsored programs	173,603	219,911	172,468
Other	68,717	53,163	46,684
Total operating revenues	1,163,244	1,180,953	1,111,413
Operating expenses			
Compensation and benefits (1)	818,921	801,330	757,978
Supplies and other services	353,765	392,072	331,131
Scholarships and fellowships	242	342	258
Depreciation and amortization	57,047	50,542	51,425
Total operating expenses	1,229,975	1,244,286	1,140,792
Operating loss	(66,731)	(63,333)	(29,379)
Nonoperating revenues (expenses)			
State appropriations, net	50,000	42,632	47,709
Gifts	27,370	20,608	19,516
Investment gain (loss), net of expense	14,223	7,062	17,738
Other	(12,038)	(14,959)	(13,354)
Total nonoperating revenues, net	79,555	55,343	71,609
Income (loss) before other changes in net assets	12,824	(7,990)	42,230
Other changes in net position			
Capital gifts and appropriations	3,278	20,634	15,758
Federal grants for capital projects	2,594	22,496	1,479
Interagency disposition	(437)	(1,221)	-
Total other changes in net position	5,435	41,909	17,237
Increase in net position	18,259	33,919	59,467
Net position			
Beginning of year	765,332	731,413	671,946
End of year	\$ 783,591	\$ 765,332	\$ 731,413

(1) Note: Compensation and benefits increased in fiscal 2012 by \$6,671,000 due to UAMS' decision to provide nonclassified employees vested accumulated rights to receive sick leave benefits. This practice was subsequently reversed in early fiscal 2013. Therefore, fiscal year 2013 compensation and benefits expenses were decreased by the same amount as a result of this change.

University of Arkansas for Medical Sciences
Unaudited Management's Discussion and Analysis
June 30, 2013 and 2012

Fiscal Year 2013

The Statement of Revenues, Expenses, and Changes in Net Position reflects income before other changes in net position of \$12,824,000, and an increase of \$18,259,000 in net position for fiscal year 2013. Highlights of the information presented in this statement show how the following affected operating revenue:

Net patient services revenue increased by \$10,033,000 or 1.14%. The increase in net patient service revenue is due primarily to a growth in inpatient visits. Hospital patient service revenue was up \$10,795,000 or 2%, College of Medicine patient service revenue was down \$5,904,000 or 2.6%, and the new Radiation Oncology division had net patient revenues of \$6,444,000. Other divisions combined for a slight decrease in patient service revenue. Sponsored Programs, which include federal grants and contracts, state and local grants and contracts, and nongovernmental grants and contracts, decreased by \$46,308,000. Federal grants and contracts decreased by \$50,627,000, approximately \$42,442,000 of which was due to winding down the BTOP grant. Nongovernmental grants and contracts increased by \$2,075,000 primarily due to increased contract activity in the College of Medicine. The total operating revenue decrease was 1.5%.

The following factors affected operating expenses in 2013:

Compensation and benefits expense was a major driver in operating expense in fiscal year 2013, increasing by \$17,591,000 or 2.2%. Compensation and benefits expense related to patient care increased by \$28,482,000 or 6.8%, primarily due to the staffing required to support the increase in emergency room and clinic visits, and the clinical complexity of patients in the hospital. Compensation and benefits related to research increased by \$4,107,000 or 5.2%, primarily due to internally funded research in the College of Medicine. Total supplies and other services decreased by \$38,307,000 or 9.8%. Supplies and other services related to patient care decreased by \$5,292,000 or 2.2%, primarily due to cost containment efforts. Supplies and other services related to public services decreased by \$44,239,000 or 67.2%, primarily due to the winding down of the BTOP grant. The balance of the change in supplies and other services were primarily related to the EPIC project.

The following factors affected nonoperating revenue (expense) in 2013:

Nonoperating revenue (expense) increased by \$24,212,000. This was primarily caused by an increase of \$7,161,000 in net investment income and an increase of \$7,368,000 in net state appropriations. Gross state appropriations were down by \$139,000 or .1%. Offsetting this decrease was a decrease of \$7,507,000 in Medicaid match payments, which are reported as a decrease to state appropriated revenue.

State appropriations are reported in the Statements of Revenues, Expenses, and Changes in Net Position as Nonoperating Revenue, net of the Medicaid match payments required under various contracts between UAMS and the Arkansas Department of Human Services (DHS).

Net state appropriations revenue for the years ended June 30, 2013, 2012, and 2011 was as follows:

<i>(in thousands)</i>	2013	2012	2011
Gross state appropriations revenue	\$ 114,638	\$ 114,777	\$ 114,515
Less: Medicaid match payments	<u>64,638</u>	<u>72,145</u>	<u>66,806</u>
Net state appropriations revenue	<u>\$ 50,000</u>	<u>\$ 42,632</u>	<u>\$ 47,709</u>

University of Arkansas for Medical Sciences

Unaudited Management's Discussion and Analysis

June 30, 2013 and 2012

Fiscal Year 2012

The Statement of Revenues, Expenses, and Changes in Net Position reflects a net loss before other changes in net position of \$7,990,000, and an increase of \$33,919,000 in net position for fiscal year 2012. Highlights of the information presented in this statement show how the following affected operating revenue:

Net patient services revenue increased by \$7,859,000 or 0.9%. The increase in net patient service revenue is due primarily to a growth in outpatient visits. Hospital patient service revenue was down \$1,087,000 or 0.2%, College of Medicine patient service revenue was up \$9,453,000 or 4.4%, and other UAMS divisions had a slight decrease in patient service revenue. Sponsored Programs, which include federal grants and contracts, state and local grants and contracts, and nongovernmental grants and contracts, increased by \$47,443,000. Federal grants and contracts increased by \$45,734,000, of which \$45,413,000 was related to the American Recovery and Reinvestment Act (ARRA) with the balance being from normal grant activity. Nongovernmental grants and contracts increased by \$1,742,000 primarily due to increased contract activity in the College of Medicine. The total operating revenue increase was 6.3%.

The following factors affected operating expenses in 2012:

Compensation and benefits expense was a major driver in operating expense in fiscal year 2012, increasing by \$43,352,000 or 5.7%. Compensation and benefits expense related to patient care increased by \$31,958,000 or 8.2%, primarily due to the staffing required to support the increase in emergency room and clinic visits, and the clinical complexity of patients in the hospital. Compensation and benefits related to research increased by \$10,587,000 or 15.9%, primarily due to internally funded research in the College of Medicine. Total supplies and other services increased by \$60,941,000 or 18.4%. Supplies and other services related to patient care increased by \$6,096,000 or 2.6%, primarily due to the supplies and other services required to support the increase in emergency room and clinic visits, and the clinical complexity of patients in the hospital. Supplies and other services related to public services increased by \$52,968,000 or 410.6%, primarily due to the ARRA stimulus funds for the Broadband Technology Opportunities Program. The balance of the change in supplies and other services were primarily related to auxiliary operations.

The following factors affected nonoperating revenue (expense) in 2012:

Nonoperating revenue (expense) decreased by \$16,266,000. This was primarily caused by a decrease of \$10,676,000 in net investment income and a decrease in net state appropriations. Gross state appropriations were up by \$262,000 or 0.2%. Offsetting the increase of \$5,077,000 was an increase of \$5,339,000 in Medicaid match payments, which are reported as a decrease to state appropriated revenue.

State appropriations are reported in the Statements of Revenues, Expenses, and Changes in Net Position as Nonoperating Revenue, net of the Medicaid match payments required under various contracts between UAMS and the Arkansas Department of Human Services (DHS). The increase in Medicaid match payments was primarily due to the phase out of the ARRA stimulus funding.

Net state appropriations revenue for the years ended June 30, 2012, 2011, and 2010 was as follows:

University of Arkansas for Medical Sciences
Unaudited Management's Discussion and Analysis
June 30, 2013 and 2012

<i>(in thousands)</i>	2012	2011	2010
Gross state appropriations revenue	\$ 114,777	\$ 114,515	\$ 114,213
Less: Medicaid match payments	<u>72,145</u>	<u>66,806</u>	<u>57,396</u>
Net state appropriations revenue	<u>\$ 42,632</u>	<u>\$ 47,709</u>	<u>\$ 56,817</u>

Results of Operations

Fiscal Year 2013

In fiscal year 2013, UAMS experienced a net income before other changes in net position of \$12,824,000 and an increase in net position of \$18,259,000. UAMS benefitted from two significant nonrecurring transactions during fiscal year 2013: (1) the recognition, as other operating revenue, of \$13,551,000 in IRS refunds of Federal Insurance Contributions Act (FICA) taxes paid by UAMS on wages earned for services performed by medical residents for calendar years 1996 through 1999 with interest, more fully described in Note 17 to the financial statements; and (2) the removal of a liability in the amount of \$6,671,000 for the vested accumulated rights of nonclassified employees to receive sick leave benefits upon retirement, as noted above, which lowered compensation and benefits expense by this amount. Without these two transactions, UAMS would have experienced a net loss before other changes in net position of \$7,398,000 and a decrease in net position of \$1,963,000. Primary drivers of other changes in net position were capital gifts, primarily for the Donald W. Reynolds Institute on Aging, and Federal capital grants for the BTOP project.

Although the overall financial position improved in 2013, there were some occurrences that adversely affected the financial position:

Operating expense related to patient services increased by \$23,190,000 or 3.5%, primarily due to the staffing required to support the increase in emergency room and clinic visits, and the clinical complexity of patients in the hospital. However, net patient service revenue increased by \$10,033,000 or 1.1%. Net patient service revenue was adversely impacted by a 14.5% increase in charity care and bad debt expense.

Gross state appropriations decreased by \$139,000, and continued to decline as a share of UAMS revenue to approximately 9.1% and 9.2% for fiscal years 2013 and 2012, respectively.

Fiscal Year 2012

In fiscal year 2012, UAMS experienced a net loss before other changes in net position of \$7,990,000 and an increase in net position of \$33,919,000. Excluding the increase in compensation and benefits of \$6,671,000 due to UAMS' decision in fiscal year 2012 to provide nonclassified employees vested accumulated rights to receive sick leave benefits, as noted above, UAMS would have experienced a net loss before other changes in net position of \$1,319,000 and an increase in net position of \$40,590,000. Primary drivers of other changes in net position were the BTOP grant and capital gifts for the expansion of the Winthrop P. Rockefeller Cancer Institute, Donald W. Reynolds Institute on Aging, and other renovation and construction projects.

Although the overall financial position improved in 2012, there were some occurrences that adversely affected the financial position:

Operating expense related to patient services increased by \$38,054,000 or 6.1%, primarily due to the staffing required to support the increase in emergency room and clinic visits, and the clinical complexity of patients in the hospital. However, net patient service revenue increased by \$7,859,000 or 0.9%. Net patient service revenue was adversely impacted by a 15.2% increase in charity care and bad debt expense.

University of Arkansas for Medical Sciences
Unaudited Management's Discussion and Analysis
June 30, 2013 and 2012

Gross state appropriations increased by \$262,000, and continue to decline as a share of UAMS revenue to approximately 9.2% and 9.6% for fiscal years 2012 and 2011, respectively.

Capital Assets and Debt Administration

Capital Assets

At June 30, 2013, UAMS had \$831,492,000 invested in capital assets, net of accumulated depreciation and amortization of \$507,537,000. Depreciation and amortization charges totaled \$57,047,000 for the fiscal year ended June 30, 2013.

UAMS' capital additions totaled \$97,665,000 in fiscal year 2013. Capital additions primarily comprised replacement, renovation, and new construction of academic, research, and hospital facilities, as well as investments in equipment. Major capital additions in fiscal year 2013 and the sources that funded their acquisition included:

<i>(in thousands)</i>	Amount of Additions	Funding Source
Project		
Radiation Oncology Center equipment	\$ 9,800	Capital lease
Central energy plant upgrade	8,000	UAMS and ABA loan
Donald W. Reynolds Institute on Aging	3,009	Donald W. Reynolds Foundation
BTOP equipment	2,970	Grant
Construction in progress:		
EPIC information system implementation	29,207	UAMS and loan
Hospital surgical suite renovation	5,601	Bonds
AHEC Magnolia clinic renovation	2,646	UAMS

As noted above, construction in progress at June 30, 2013, which totaled \$44,722,000, was dominated by the EPIC implementation. More detailed information about UAMS' capital assets is presented in Note 7 to the financial statements.

Debt Administration

At June 30, 2013, UAMS had \$390,378,000 in outstanding debt, as shown in the following table:

<i>(in thousands)</i>	Amount Outstanding
Obligation	
Bonds payable	\$ 282,927
Notes payable	68,447
Obligations under capital leases	39,004
Total debt	<u>\$ 390,378</u>

Moody's Investors Service raised the rating of the University of Arkansas System from Aa3 to Aa2 in May 2010, which was affirmed on October 5, 2012. UAMS, as one of the colleges in the University of Arkansas System, will benefit from this rating increase. More detailed information about current and long-term liabilities is presented in Notes 8 and 9 to the financial statements.

Economic Outlook

UAMS' financial position improved in fiscal year 2013 as evidenced by an \$18,259,000 increase in net position. UAMS had a net margin (Income before other changes in net position) of \$12,824,000 for the fiscal year. As discussed above, fiscal year 2013 was a challenging year for UAMS. As we move into fiscal year 2014, UAMS faces a changing health care environment with the *Patient Protection and Affordable Care Act* (PPACA) and the challenges of converting to a new integrated clinical information

University of Arkansas for Medical Sciences Unaudited Management's Discussion and Analysis June 30, 2013 and 2012

system and a new student information system. Additionally, UAMS is undertaking an institution-wide effort to examine its work processes and organizational structure to improve efficiency and effectiveness and reduce waste (Performance Excellence). Each of these initiatives will be discussed in more detail below.

UAMS has a diverse revenue stream to fund operations, including tuition, patient services revenue, state appropriations, investment income, and philanthropic support from individuals, foundations, and corporations. However, UAMS is highly dependent on patient service revenue, which represents 70.7% of total revenue.

Also on the horizon is Arkansas' plan to implement the Medicaid expansion part of PPACA by using Medicaid funds as premium assistance to purchase coverage for some or all newly eligible Medicaid beneficiaries in marketplace plans. This is expected to be a significant driver of patient service revenue in fiscal year 2014 and future years. It creates opportunities to have more UAMS patients insured, which may improve the overall payor mix for UAMS' clinical programs. Challenges include the possible reduction in federal payments to safety net providers, like UAMS, who provide care to indigent patients, and the need to develop the necessary infrastructure required to comply with PPACA and participate in new opportunities, such as an Accountable Care Organization or developing a clinically integrated network. At this time, UAMS is unable to quantify the effect on payor mix or patient service revenue.

UAMS must continue significant investments in clinical and campus infrastructure in order to generate necessary productivity gains to more closely manage clinical practice and outcomes, continue to increase patient safety, and to remain compliant with an ever-growing regulatory burden. To this end, the Board of Trustees of the University of Arkansas approved a proposal by UAMS to enter into a license and support agreement with Epic Systems Corporation for an integrated clinical information system with a cost not to exceed \$87,000,000 from institutional reserves, plus borrowing in the amount of \$60,000,000 at an interest rate of 1.66% per annum for a period of 7 years. Additionally, UAMS entered into a license and support agreement with Oracle Corporation, in August 2013, for a student information system (SIS) with a projected cost of \$7,844,000 to be paid from institutional reserves.

The first wave of clinics and departments went live in July and August 2013 on EPIC, which included patient scheduling, outpatient registration, the outpatient pharmacy, professional billing for physicians, and a number of outpatient clinics. All outpatient and inpatient clinical services are expected to be converted to EPIC by the end of March 2014.

The planning is underway for the conversion to the SIS from an internally developed system that has been in use by UAMS for many years. The conversion is expected to be completed in time to register students in the fall of 2015.

The Performance Excellence program, initiated in the spring 2013, will apply business process improvement strategies using Lean Six Sigma principles and methodologies to improve efficiency and effectiveness. UAMS has contracted with a company that specializes in Lean Six Sigma, which will train UAMS employees on how to evaluate work processes leading to improvements in performance. UAMS' intent is to become self-sufficient in training its staff by transitioning from a contracted program to a UAMS internal-resourced program. The primary goal of this effort in the first year is to develop opportunities to increase revenues, reduce costs and improve overall performance. The longer term strategy is to develop internal capabilities through cultural transformation of management practices at UAMS in order for the university to thrive in a changing healthcare environment.

On the national scene, many of UAMS' revenue streams may be at risk. Department of Health and Human Services (DHHS) funding is being threatened with budget cuts. DHHS provided \$69,494,000 in funds to UAMS during fiscal 2013. Medicare reimbursement is at risk on many fronts. Physician payments and annual updates are being reviewed with a goal of reducing payments. All Medicare patient care reimbursements are the subject of heightened audits by contractors seeking opportunities to recoup funding from providers. Graduate Medical Education and, specifically, Indirect Medical Education, are

University of Arkansas for Medical Sciences Unaudited Management's Discussion and Analysis June 30, 2013 and 2012

targeted for 10% reductions. Federal health officials have released a final rule that calls for a \$1.1 billion reduction in Medicaid disproportionate share hospital (DSH) payments over the next two years. Medicaid will adopt a formula for state-specific reductions that favor hospitals that treat a large number of uninsured patients or have high Medicaid volumes. UAMS' net patient service revenue included \$61,330,000 in DSH payments during fiscal 2013. However, the potential effect of these changes on UAMS revenue in future years is unknown at this time. The continued drive for national deficit reduction is almost certain to impact federal reimbursement in the form of Medicaid, Medicare, DHHS, and other agency funding.

State operating support, which represents 9.1% of UAMS' revenue, is also under pressure due to current economic conditions. UAMS' state operating support was reduced by \$1,600,000 for fiscal year 2014. While efforts are underway to have all or a portion of this funding restored in fiscal year 2014, it is uncertain whether or not this will continue as a permanent reduction in UAMS' state appropriations support as the university heads into fiscal year 2015.

On June 29, 2012, UAMS completed the purchase of substantially all of the assets owned by CARTI and used exclusively in the operation of the CARTI radiation oncology treatment facility located on the UAMS campus. The purchase price was \$9,500,000. On July 1, 2012, the radiation oncology treatment facility opened as the UAMS Radiation Oncology Center (ROC). In fiscal year 2013, ROC installed new treatment equipment at a cost of \$10,201,000. In the first full year of operations, ROC had a break even operating margin and is expected to generate positive operating margins in future years.

Management understands its current operating challenges and is committed to maintaining an operating margin that will position UAMS to deal with the impact of healthcare reform and allow for investment in technology, research, and human capital.

Requests for Information

This financial report is designed to provide a general overview of UAMS' finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to William R. Bowes, Vice Chancellor for Finance and Chief Financial Officer, 4301 West Markham, #632, Little Rock, Arkansas 72205.



Report of Independent Auditors

To the Board of Trustees of
The University of Arkansas System:

We have audited the accompanying financial statements of the University of Arkansas for Medical Sciences ("UAMS"), a campus of the University of Arkansas, as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, which collectively comprise UAMS' basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of UAMS at June 30, 2013 and 2012, and the respective changes in financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



Other Matters

The accompanying management's discussion and analysis on pages 1 through 11 are required by accounting principles generally accepted in the United States of America to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

PricewaterhouseCoopers LLP

Dallas, Texas
October 2, 2013

University of Arkansas for Medical Sciences
Statements of Net Position
June 30, 2013 and 2012

<i>(in thousands)</i>	2013	2012
Assets		
Current assets		
Cash and cash equivalents (Note 4)	\$ 63,030	\$ 94,714
Investments (Note 5)	67,606	66,968
Patient accounts receivable, net (Note 2)	108,398	108,772
Nonpatient accounts receivable (net of allowances of \$3,198 in 2013 and \$977 in 2012)	52,175	31,408
Supplies	19,602	18,703
Notes and student loans receivable, net (Notes 6 and 14)	2,387	2,698
Prepaid expenses	6,922	3,848
Total current assets	<u>320,120</u>	<u>327,111</u>
Noncurrent assets		
Investments (Note 5)	116,267	102,415
Notes and student loans receivable, net (Notes 6 and 14)	14,476	15,914
Deposits and funds held in trust by others (Note 5)	47,921	26,937
Capital assets, net (Note 7)	831,492	791,808
Other noncurrent assets	3,780	3,088
Total noncurrent assets	<u>1,013,936</u>	<u>940,162</u>
Total assets	<u>\$ 1,334,056</u>	<u>\$ 1,267,273</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (Note 8)	\$ 76,500	\$ 66,987
Deferred revenue	8,886	13,067
Funds held in trust for others	498	461
Estimated third-party payor settlements (Note 2)	267	4,043
Compensated absences payable, current portion (Note 9)	2,881	2,859
Bonds, notes, and capital leases payable, current portion (Notes 9 and 10)	28,353	18,718
Total current liabilities	<u>117,385</u>	<u>106,135</u>
Noncurrent liabilities		
Deposits	185	180
Compensated absences payable, net of current portion (Note 9)	44,150	49,625
Liability for other postemployment benefits (Notes 9 and 12)	24,809	22,225
Federal Capital Contribution for Perkins Loan Program	1,911	1,911
Bonds, notes, and capital leases payable, net of current portion (Notes 9 and 10)	362,025	321,865
Total noncurrent liabilities	<u>433,080</u>	<u>395,806</u>
Total liabilities	<u>550,465</u>	<u>501,941</u>
Commitments and contingencies (Notes 10 and 15)		
Net Position		
Net investment in capital assets	488,402	477,589
Restricted		
Expendable		
Scholarships	10,563	15,236
Research	15,968	25,699
Capital projects	83,970	70,635
Other	498	576
Nonexpendable		
Endowments	29,474	27,756
Scholarships, fellowships, student loans	394	394
Unrestricted	154,322	147,447
Total net position	<u>783,591</u>	<u>765,332</u>
Total liabilities and net position	<u>\$ 1,334,056</u>	<u>\$ 1,267,273</u>

The accompanying notes are an integral part of these financial statements.

University of Arkansas for Medical Sciences
Statements of Revenues, Expenses, and Changes in Net Position
Years Ended June 30, 2013 and 2012

<i>(in thousands)</i>	2013	2012
Revenues		
Operating revenues		
Student tuition and fees (net of scholarship allowances of \$4,029 in 2013 and \$4,347 in 2012)	\$ 29,701	\$ 25,754
Net patient services (Note 2)	886,577	876,544
Meaningful use revenue	4,646	5,581
Sponsored programs		
Federal grants and contracts	96,037	146,664
State and local grants and contracts	22,363	20,119
Nongovernmental grants and contracts	55,203	53,128
Sales and services of educational departments	30,972	31,279
Auxiliary enterprises		
Housing and food service	8,559	8,443
Bookstore	613	674
Other auxiliary enterprises	2,526	2,623
Other operating revenue (Note 17)	26,047	10,144
Total operating revenues	<u>1,163,244</u>	<u>1,180,953</u>
Expenses		
Operating expenses (Note 16)		
Compensation and benefits	818,921	801,330
Supplies and other services	353,765	392,072
Scholarships and fellowships	242	342
Depreciation and amortization (Note 7)	57,047	50,542
Total operating expenses	<u>1,229,975</u>	<u>1,244,286</u>
Operating loss	<u>(66,731)</u>	<u>(63,333)</u>
Nonoperating revenues (expenses)		
State appropriations, net (Note 3)	50,000	42,632
Gifts	27,370	20,608
Investment income, net of investment expense (Notes 4 and 5)	14,223	7,062
Interest on debt	(11,696)	(14,706)
Loss on disposal of capital assets	(342)	(253)
Total nonoperating revenues, net	<u>79,555</u>	<u>55,343</u>
Income (loss) before other changes in net position	<u>12,824</u>	<u>(7,990)</u>
Other changes in net position		
Capital gifts	2,822	20,634
Capital appropriations	456	-
Federal grants for capital projects	2,594	22,496
Other	(437)	(1,221)
Total other changes in net position	<u>5,435</u>	<u>41,909</u>
Increase in net position	18,259	33,919
Net position		
Beginning of year	<u>765,332</u>	<u>731,413</u>
End of year	<u>\$ 783,591</u>	<u>\$ 765,332</u>

The accompanying notes are an integral part of these financial statements.

University of Arkansas for Medical Sciences
Statements of Cash Flows
Years Ended June 30, 2013 and 2012

<i>(in thousands)</i>	2013	2012
Cash flows from operating activities		
Tuition and fees (net of scholarships)	\$ 25,013	\$ 26,585
Patient and insurance payments	873,740	865,055
Sponsored programs	169,514	222,082
Collection of loans and interest	2,392	2,217
Auxiliary enterprise revenue		
Housing and food service	8,553	8,446
Bookstore	613	674
Other auxiliary enterprises	2,698	2,810
Other receipts	60,779	43,966
Payments to suppliers	(338,266)	(379,360)
Payments to employees	(668,115)	(643,016)
Payments of employee benefits	(150,686)	(148,469)
Loans issued to students	(3,078)	(3,117)
Scholarships and fellowships	(242)	(342)
Other payments	(10,961)	(10,050)
Net cash and cash equivalents used in operating activities	<u>(28,046)</u>	<u>(12,519)</u>
Cash flows from noncapital financing activities		
State appropriations	43,642	43,639
Gifts and grants	30,194	45,072
Repayment of loans	141	(587)
Other agency funds (net)	37	(89)
Net cash and cash equivalents provided by noncapital financing activities	<u>74,014</u>	<u>88,035</u>
Cash flows from capital and related financing activities		
Proceeds from issuance of debt	196,092	17,911
Federal grants for capital projects	2,594	22,496
Capital appropriations	400	-
Proceeds from sale of capital assets	102	75
Purchases of capital assets	(81,569)	(98,557)
Principal paid on capital debt and leases	(161,177)	(27,470)
Interest and paying agent fees paid on debt and capital leases	(12,702)	(14,646)
Net cash and cash equivalents used in capital and related financing activities	<u>(56,260)</u>	<u>(100,191)</u>

The accompanying notes are an integral part of these financial statements.

University of Arkansas for Medical Sciences
Statements of Cash Flows (continued)
Years Ended June 30, 2013 and 2012

<i>(in thousands)</i>	2013	2012
Cash flows from investing activities		
Proceeds from sales and maturities of investments	76,183	68,155
Interest on investments (net of fees)	946	1,011
Purchases of investments	<u>(98,521)</u>	<u>(36,513)</u>
Net cash and cash equivalents (used in) provided by investing activities	<u>(21,392)</u>	<u>32,653</u>
Net (decrease) increase in cash and cash equivalents	(31,684)	7,978
Cash and cash equivalents		
Beginning of year	<u>94,714</u>	<u>86,736</u>
End of year	<u><u>\$ 63,030</u></u>	<u><u>\$ 94,714</u></u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (66,731)	\$ (63,333)
Adjustments to reconcile net operating loss to net cash and cash equivalents (used in) provided by operating activities		
Depreciation and amortization	57,047	50,542
Changes in assets and liabilities		
Patient and nonpatient accounts receivable, net	(14,271)	(8,732)
Supplies	(899)	1,872
Other assets	(2,195)	1,363
Accounts payable and accrued liabilities	9,827	(3,753)
Deferred revenue	(4,182)	762
Deposits	4	160
Compensated absences payable	(7,057)	8,850
Other liabilities	<u>411</u>	<u>(250)</u>
Net cash and cash equivalents used in operating activities	<u><u>\$ (28,046)</u></u>	<u><u>\$ (12,519)</u></u>
Noncash transactions		
Capital assets acquired by capital gift	\$ 2,822	\$ 20,633
Capital asset acquisition paid for by State of Arkansas	56	-
Capital assets acquired by incurring capital lease obligations	10,726	5,377
Capital assets acquired by notes payable	2,492	9,570

The accompanying notes are an integral part of these financial statements.

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

1. Summary of Significant Accounting Policies

The University of Arkansas (University) for Medical Sciences (UAMS) is one of thirteen campuses operating within the University of Arkansas System, organized under various laws of the State of Arkansas and governed by the University's ten-member Board of Trustees (UA Board).

Basis of Presentation

UAMS accounts for its activities through the use of an enterprise fund. Enterprise funds are used to account for activities similar to those found in the private sector, where the determination of a change in financial position is necessary or useful for sound financial administration. The accounting records of UAMS are organized on the basis of funds as prescribed by U.S. generally accepted accounting principles (GAAP) applicable to governmental colleges and universities as established by the Governmental Accounting Standards Board (GASB).

UAMS has adopted GASB Statement No. 62 (GASB 62), *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. GASB 62 requires enterprise funds to adhere to all applicable GASB pronouncements as well as those statements and interpretations of the Financial Accounting Standards Board (FASB), Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure, issued on or before November 30, 1989, which do not conflict with or contradict GASB pronouncements.

UAMS is a state-assisted academic health center composed of:

- The Colleges of Medicine, Pharmacy, Nursing, Health Professions, Public Health, Graduate School and Northwest Arkansas Satellite Campus;
- The University Hospital of Arkansas (the Hospital), a tertiary care referral center with 453 acute care beds in use at June 30, 2013;
- Regional programs including Tele-education, Rural Hospital Program, and eight Area Health Education Centers (AHECs) located throughout the state;
- The Winthrop P. Rockefeller Cancer Institute;
- Harvey and Bernice Jones Eye Institute;
- Donald W. Reynolds Institute on Aging;
- Myeloma Institute for Research and Therapy;
- Psychiatric Research Institute;
- Jackson T. Stephens Spine Neurosciences Institute; and
- Translational Research Institute.

The Little Rock campus includes approximately 5,460,000 square feet of office, clinical, research, educational, workshop, and general-purpose space, excluding space utilized at Arkansas Children's Hospital and leased space in the community.

Accrual Accounting

The financial statements are prepared on the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when incurred.

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

Cash and Cash Equivalents

Cash and cash equivalents include short-term, highly liquid investments that are readily convertible to cash and have a maturity at acquisition of three months or less.

Investments

Investments and funds held in trust by others of marketable securities are reported at fair value as established by major securities markets. The fair value of venture capital and other investments is based on the most current information reported to UAMS by the respective investment managers. All investment income, including changes in the fair value of investments, is reported as nonoperating revenue.

The UA Board and the University of Arkansas Foundation Board of Trustees established an external investment pool (the Pool). This arrangement commingles (pools) the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio. The governmental external investment pool is exempt from registration with the SEC. The UA Board and the University of Arkansas Foundation Board of Trustees are the sponsors of this investment pool and are responsible for operation and oversight for the pool. All participation in this investment pool is voluntary. Participation in or withdrawal from the cash segment of the Pool is based on the daily market value of the units within the Pool. Participation in or withdrawal from the investment segment of the Pool is based on the market value per unit at the beginning of the calendar quarter in which the transaction takes place. Income from the Pool is allocated to the participants in the Pool based on the market value per unit from the previous day. Detailed disclosure information about the Pool may be obtained by writing or calling the University of Arkansas System, 2404 North University Avenue, Little Rock, Arkansas 72207-3608, 501-686-2500.

Patient Accounts Receivable

Patient accounts receivable are shown net of contractual adjustments and an allowance for doubtful accounts. Credit balances representing refunds due are reported as accounts payable. The amount of the allowance for doubtful accounts is based upon management's assessment of historical and expected net collections, business and economic conditions, trends in federal and state governmental care coverage and other collection indicators.

Nonpatient Accounts Receivable

Nonpatient accounts receivable represent primarily amounts due from other organizations and the State of Arkansas.

Notes and Student Loans Receivable

Notes and student loans receivable represent the unpaid balances of student loans receivable, net of allowances, and notes receivable from related parties.

Loan Funds

Loan funds, included in cash and cash equivalents in the statements of net position, consist of resources made available for financial loans to students of UAMS. These resources include federal funds, funds from other external sources, and UAMS funds.

Supplies

Supplies, consisting primarily of medical supplies and drugs, are carried at the lower of cost or market on either the first-in, first-out (FIFO) basis or average-cost basis.

Capital Assets

Capital assets are stated at cost at the date of acquisition or estimated fair value at the date of donation. Interest on borrowings to finance facilities is capitalized during construction, net of any

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

investment income earned through the temporary investment of project borrowings. UAMS has established a capitalization threshold of \$5,000 for all capital assets other than software. The software capitalization threshold is \$1,000,000 for purchased and internally developed software. Depreciation and amortization are calculated using the straight-line method over the lesser of the estimated useful lives as established by the American Hospital Association or the lease term as follows:

Buildings and fixtures	15 to 40 years
Equipment	3 to 15 years
Leased assets	Dependent on lease term; generally, 3 to 10 years
Other	3 to 15 years

Amortization of amounts under capital lease is included in depreciation and amortization expense.

Compensated Absences

Vested or accumulated vacation and sick leave of UAMS employees are recorded as an expense and liability as the benefits are earned. Amounts recorded include salary expense as well as salary-related payments (e.g., FICA taxes, retirement, etc.). No liability is recorded for nonvested accumulated rights to receive sick leave benefits. The current portion of compensated absences is determined using the average balance paid in the prior two-year period. In fiscal 2013, UAMS extended vested accumulated rights to receive sick leave benefits, already granted to classified employees, to nonclassified employees. This increased fiscal 2012 expenses by \$6,671,000. A decision to reverse this extension was made in fiscal 2013, resulting in a decrease in expense by the same amount.

UAMS has, from time to time, negotiated voluntary early retirement agreements with faculty and staff which may include the provision of a stipend and healthcare or other benefits for future periods. At June 30, 2013, the amount of liability established for these type agreements was \$801,000.

Deferred Revenue

Deferred revenue consists of student tuition and fees and other revenue applicable to subsequent accounting periods.

Operating Versus Nonoperating Revenue

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of healthcare services and education are reported as operating revenue and expenses. Operating revenue consists of tuition and fees, patient services revenue, operating grants and contracts, educational department sales and services, as well as various auxiliary services. Nonoperating revenue consists of revenue that results from nonexchange transactions or investment-related activities, including state appropriations (net of appropriations used for Medicaid match), nonoperating gifts, grants and bequests, capital contributions, loss on disposal of capital assets, investment income, interest on debt, and additions to endowments.

Net Patient Services Revenue

Net patient services revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Retroactive adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted as final settlements are determined.

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

Charity Care

UAMS provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because UAMS does not pursue collection of amounts determined to qualify as charity care, these amounts are accounted for as a reduction of patient services revenue at the time the services are rendered.

Grants and Contracts

UAMS has been awarded grants and contracts for operations for which the moneys have not been received or expended. These awards have not been reflected in the financial statements but represent commitments of sponsors to provide funds for specific research and training projects.

Federal research grants and contracts normally provide for the recovery of direct and indirect costs, subject to adjustment based upon review by the granting agencies. UAMS recognizes revenue associated with direct costs as the related costs are incurred. The recovery of indirect costs is recorded at predetermined rates negotiated with the federal government that are effective from July 1, 2010 through June 30, 2013.

Student Financial Aid

Revenue and expenditures for student financial aid are recognized as such in the period earned. Tuition and fees are shown net of applicable scholarship allowances.

Endowment Income

Endowment funds are subject to the restrictions of gift instruments requiring that the principal be invested in perpetuity and only the income be utilized. Term endowment funds are similar to endowment funds except that, upon the passage of a stated period of time or the occurrence of a particular event, all or part of the principal may be expended. While quasi-endowment funds have been established by the UA Board for the same purposes as endowment funds, any portion of quasi-endowment funds may be expended. As such, the expired portion of term endowments and all quasi-endowments are reflected as unrestricted net position in the statements of net position. UAMS employs a total-return policy in determining the amount of investment income to be spent.

Income Taxes

UAMS is part of the University of Arkansas System and, as such, is exempt from federal income taxes except for tax on unrelated business income. Management of UAMS is not aware of any significant unrelated business income. Accordingly, no provision for income taxes is made in the accompanying financial statements.

Use of Restricted Resources

When both restricted and unrestricted resources are available for use, it is UAMS' policy to use restricted resources first, then unrestricted resources as they are needed.

Net Position

Net Position restricted by outside sources is distinguished from unrestricted funds allocated for specific purposes by action of the UA Board. Externally restricted funds may only be utilized in accordance with the purposes established by the donor or grantor, whereas unrestricted funds may be used by UAMS in achieving any of its institutional purposes.

Use of Estimates

The preparation of financial statements in conformity with GAAP and governmental accounting standards 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

Accounting Pronouncements

In June 2011, the GASB issued GASB Statement No. 63, *Financial Reporting and Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* (GASB No. 63). GASB No. 63 improves financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. It alleviates uncertainty about reporting those financial statement elements by providing guidance where none previously existed. The provisions of GASB No. 63 are effective for financial statements for periods beginning after December 15, 2011. UAMS adopted GASB No. 63 on July 1, 2012. The adoption of GASB No. 63 did not have a significant impact on the financial statements of UAMS as there were no deferred inflows or outflows.

In March 2012, the GASB issued GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* (GASB No. 65). GASB No. 65 establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities. GASB No. 65 also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations, and limits the use of the term 'deferred' in financial statements. The provisions of GASB No. 65 are effective for financial statements for periods beginning after December 15, 2012. UAMS is currently evaluating the impact GASB No. 65 will have on its financial statements.

2. Net Patient Services Revenue and Charity Care

The Hospital is a division of UAMS, and the Faculty Group Practice (FGP) is the collective body of the College of Medicine faculty involved in professional practice at UAMS. FGP is an integral component of UAMS, functioning as an unincorporated division of the College of Medicine. As such, it is subject to the policies and regulations of the College of Medicine, UAMS, and the UA Board. Patient care operations are included in the accompanying financial statements under accounting principles generally followed by governmental colleges and universities. Patient accounts receivable at June 30, 2013 and 2012 are recorded net of an allowance for doubtful accounts of \$425,204,000 and \$497,497,000, respectively.

Net patient services revenue for the years ended June 30, 2013 and 2012 is as follows:

<i>(in thousands)</i>	2013	2012
Gross patient revenue	\$ 2,006,148	\$ 1,962,329
Less: Patient services contractual allowances	1,029,435	1,012,931
Less: Provision for bad debts	<u>90,136</u>	<u>72,854</u>
Net patient services revenue	<u>\$ 886,577</u>	<u>\$ 876,544</u>

UAMS provided approximately \$141,296,000 and \$129,258,000 in charity care, based on established rates, during the years ended June 30, 2013 and 2012, respectively. Because UAMS does not pursue collection of amounts determined to qualify as charity care, they are not included in gross patient revenue above. Net patient services revenue for the years ended June 30, 2013 and 2012 includes approximately \$71,722,000 and \$74,044,000, respectively, from the Medicaid program representing payments relating to Upper Payment Limit and Disproportionate Share reimbursements. These payments are available to state-operated teaching hospitals under Medicaid regulations. Net patient services revenue for the years ended June 30, 2013 and 2012

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

includes approximately \$28,906,000 and \$31,402,000, respectively, of net revenue from the Supplemental Medicaid program.

The Hospital, FGP, and AHECs have agreements with governmental and other third-party payors that provide for reimbursement at amounts different from their established rates. Contractual adjustments under third-party reimbursement programs represent the difference between the billings at established rates for services and amounts reimbursed by third-party payors. A summary of the basis of reimbursement with significant third-party payors is as follows:

Hospital

Medicare

Inpatient acute care services rendered to program beneficiaries 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. Some transplantation services are paid based upon a cost reimbursement methodology. Outpatient services are paid based on a prospective payment system where services are classified into groups called Ambulatory Payment Classifications (APC). Services in each APC are similar clinically and in terms of the resources they require. The Hospital is paid for cost-reimbursable items at a tentative rate with final settlement determined after submission of an annual cost report by the Hospital and audit by the Medicare fiscal intermediary. As of June 30, 2013, the Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2010.

Medicaid

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed based upon a cost reimbursement methodology. The Hospital is paid at a tentative rate with final settlement determined after submission of an annual cost report by the Hospital and audits by the Medicaid audit contractor. The Hospital is required to pay the federal match for the difference in reimbursement between the Tax Equity and Fiscal Responsibility Act inpatient rate and full cost. For outpatient services, the Hospital is required to pay the federal match for the difference reimbursed between the outpatient prospective rates and full cost. As of June 30, 2013, the Hospital's Medicaid cost reports have been audited by the Medicaid audit contractor through June 30, 2009.

FGP and AHECs

Services rendered to both Medicare and Medicaid program beneficiaries are reimbursed on prospectively determined rates per unit of service.

Laws and regulations governing the Medicare and Medicaid programs are 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 net adjustments to estimated settlements resulted in a decrease to net patient services revenue of \$589,500 for the year ended June 30, 2013 and an increase of \$7,461,000 for the year ended June 30, 2012. Management believes that UAMS is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs.

The Hospital, FGP, and AHECs have agreements with certain commercial insurance carriers and preferred provider organizations, which include prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

3. Net State Appropriations Revenue

State appropriations are reported in the statements of revenues, expenses, and changes in net position as Nonoperating Revenue, net of the Medicaid match payments required under various contracts between UAMS and the DHS.

Net state appropriations revenue for the years ended June 30, 2013 and 2012 is as follows:

<i>(in thousands)</i>	2013	2012
Gross state appropriations revenue	\$ 114,638	\$ 114,777
Less: Medicaid match payments	<u>64,638</u>	<u>72,145</u>
Net state appropriations revenue	<u><u>\$ 50,000</u></u>	<u><u>\$ 42,632</u></u>

4. Cash and Cash Equivalents

All cash deposits of UAMS are carried at cost. The carrying amount of deposits is separately displayed in the statements of net position as cash and cash equivalents. The carrying amount differs from the bank balance shown below due to timing differences of clearing outstanding checks and deposits.

UAMS' deposits at June 30, 2013 and 2012 are categorized below to give an indication of the level of risk assumed by UAMS at each year-end. Category 1 includes deposits that are insured or collateralized with securities held by UAMS or by its agent in UAMS' name. Category 2 includes uninsured deposits collateralized with securities held by the pledging financial institution's trust department or agent in UAMS' name. Category 3 includes uncollateralized deposits or deposits collateralized with securities held by the pledging financial institution, or by its trust department or agent, but not in UAMS' name. Amounts are shown.

<i>(in thousands)</i>	Carrying Amount	Bank Balance	Category		
			1	2	3
Cash at June 30, 2013	\$ 63,030	\$ 80,470	\$ 80,470	\$ -	\$ -
Cash at June 30, 2012	94,714	114,750	114,750	-	-

At June 30, 2013 and 2012, Category 1 is composed of \$1,350,000 and \$1,274,000, respectively, of insured deposits and \$79,120,000 and \$113,476,000, respectively, of securities that are held in custody by the Federal Reserve Bank.

The following schedule reconciles the reported amount of deposits to the statements of net position under GASB Statement No. 3 (GASB 3), *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*:

<i>(in thousands)</i>	2013	2012
Reported amount of deposits under GASB 3 as reported in the statements of net assets	<u>\$ 63,030</u>	<u>\$ 94,714</u>
Cash and cash equivalents	<u><u>\$ 63,030</u></u>	<u><u>\$ 94,714</u></u>

Deposits and funds held in trust as reported in the statements of net position include money market accounts of \$12,414,000. Interest income on cash and cash equivalents as of June 30, 2013 and 2012 was \$1,006,000 and \$1,019,000, respectively.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

5. Investments

UAMS participates in an external investment pool which is sponsored by the University of Arkansas Board of Trustees and the University of Arkansas Foundation Board of Trustees. In January 2010, the University of Arkansas Investment Committee approved an agreement which delegated authority to the UA Foundation to manage University funds held in the Pool. The agreement included delegation of all responsibility for all investment guidelines and performance objectives (the guidelines) for accounts within the Pool. The agreement also delegated to the UA Foundation authority for further delegation of portfolio implementation decisions to one or more investment managers. In January 2010, the UA Foundation entered into such an agreement with Cambridge Associates, LLC.

The following table lists the invested assets of UAMS at June 30:

<i>(in thousands)</i>	Fair Value	
	2013	2012
Investment Type		
Commingled funds:		
U.S. equity	\$ 442	\$ 360
U.S. fixed income	141	146
	<u>583</u>	<u>506</u>
Other investments:		
Escrow accounts	1,231	1,049
External investment pool	183,873	169,383
	<u>185,104</u>	<u>170,432</u>
	<u>\$ 185,687</u>	<u>\$ 170,938</u>

The activities during fiscal year 2013 affecting UAMS' investments are summarized below:

<i>(in thousands)</i>	Total Return Pool	Short/ Intermediate Pool	Other Investments	Total
Balances at June 30, 2012	\$ 102,415	\$ 66,968	\$ 1,555	\$ 170,938
Income	1,258	1,745	13	3,016
Realized gains	2,741	2,210	41	4,992
Unrealized gains (losses)	8,973	(3,240)	10	5,743
Expenses paid	(446)	(77)	(4)	(527)
Purchases, net	1,326	-	199	1,525
Balances at June 30, 2013	<u>\$ 116,267</u>	<u>\$ 67,606</u>	<u>\$ 1,814</u>	<u>\$ 185,687</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

The activities during fiscal year 2012 affecting UAMS' investments are summarized below:

<i>(in thousands)</i>	Total Return Pool	Short/ Intermediate Pool	Other Investments	Total
Balances at June 30, 2011	\$ 90,332	\$ 72,674	\$ 10,149	\$ 173,155
Income	942	1,842	89	2,873
Realized gains	1,071	1,374	10	2,455
Unrealized gains (losses)	(10)	1,138	12	1,140
Expenses paid	(361)	(60)	(4)	(425)
Purchases (sales), net	10,441	(10,000)	(8,701)	(8,260)
Balances at June 30, 2012	<u>\$ 102,415</u>	<u>\$ 66,968</u>	<u>\$ 1,555</u>	<u>\$ 170,938</u>

A substantial portion of the endowment investments is pooled, with participation in or withdrawal from the Pool based on the market value per unit at the beginning of the calendar quarter in which the transaction takes place.

The following table summarizes the relationship between the pooled endowed assets and their earnings:

<i>(in thousands, except unit amounts)</i>	2013	2012
Fair value at June 30	\$ 29,496	\$ 27,388
Number of units in Pool at June 30	495,961	495,890
Fair value per unit at June 30	\$ 59.47	\$ 55.23
Realized gains for the year	\$ 700.00	\$ 299.00
Income earned for the year	\$ 231.00	\$ 265.00
Realized gains per unit	\$ 1.41	\$ 0.60
Income earned per unit	<u>\$ 0.47</u>	<u>\$ 0.53</u>
Total income per unit	<u>\$ 1.88</u>	<u>\$ 1.13</u>

The calculation of realized gains and losses is independent of the calculation of the net change in the fair value of investments. Additionally, realized gains and losses on investments held in more than one fiscal year and sold in fiscal years 2013 and 2012 were included as a change in the fair value of investments reported in fiscal years 2013 and 2012.

The following table contains information on the risk disclosure for the Pool, which commingles (pools) the moneys of more than one legally separate entity and invests, on the participants' behalf, in an investment portfolio. The Pool was originally established in 1997 by the University and the University of Arkansas Foundation. During 1998, the Walton Arts Foundation joined the Pool, and during 2003, the Fayetteville Campus Foundation joined the Pool. The participants of the Pool have adopted investment guidelines and performance objectives for the accounts within the Pool. This information is provided in total for the pools, which include the Total Return Pool, the Intermediate Pool, and the Cash Pool. UAMS owned 11.9% of the total of these pools as of June 30, 2013 and 11.7% as of June 30, 2012.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

External Investment Pool
Statement of Invested Assets

<i>(in thousands)</i> Investment Type	Fair Value <i>(includes accrued income)</i>	
	2013	2012
Fixed income:		
Government bonds	\$ 30,331	\$ 31,440
Corporate bonds	84	73
Other fixed income	400,015	401,158
	<u>430,430</u>	<u>432,671</u>
Venture capital and partnerships:		
Partnerships	<u>577,858</u>	<u>565,298</u>
Commodities:		
Funds - Commodity Linked	<u>19,739</u>	<u>-</u>
Equity:		
Common stocks	393,141	331,591
Preferred stocks	30	58
	<u>393,171</u>	<u>331,649</u>
Hedge fund:		
Hedge equity	<u>116,901</u>	<u>74,460</u>
Other	<u>18</u>	<u>73</u>
Cash/cash equivalents:		
Short term investment funds	13,482	66,858
Cash	(514)	(30,289)
Invested cash	1	25
	<u>12,969</u>	<u>36,594</u>
	<u>\$ 1,551,086</u>	<u>\$ 1,440,745</u>

In accordance with the guidelines, the Pool manages its exposure to credit risk by diversifying the portfolio. The Policy prohibits purchase of securities rated less than BBB-. Securities downgraded below BBB should not represent more than 5% of the portfolio at cost or market. The average quality of the portfolio shall be no less than AA. Except for U.S. Treasury and Agency obligations, the portfolio shall contain no more than 5% exposure to any issuer. The following tables present the credit risk associated with the fixed income portfolio and exclude the accrued income included in the Statement of Invested Assets above.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

Credit Risk – S&P Quality Ratings at June 30, 2013

<i>(in thousands)</i> Investment Type	S&P Quality Rating by Fair Value					U.S.	Total Fair Value
	AAA	AA	A	BBB	Not Rated	Government Guaranteed	
Corporate bonds	\$ -	\$ -	\$ -	\$ -	\$ 28,891	\$ -	\$ 28,891
Government bonds	-	-	-	8	-	30,251	30,259
Other fixed income	-	-	-	-	370,848	-	370,848
Hedge event driven	-	-	-	-	24,133	-	24,133
Short term investment funds	-	-	-	-	13,482	-	13,482
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8</u>	<u>\$ 437,354</u>	<u>\$ 30,251</u>	<u>\$ 467,613</u>

<i>(in thousands)</i> Investment Type	Investment Maturities in Years					
	Less Than 1	1 - 5	6 - 10	More Than 10	Maturity not Determined	Total Fair Value
Corporate bonds	\$ -	\$ -	\$ -	\$ 84	\$ 28,807	\$ 28,891
Government bonds	-	-	30,251	8	-	30,259
Other fixed income	-	-	-	-	370,848	370,848
Hedge event driven	-	-	-	-	24,133	24,133
Short term investment funds	-	-	-	-	13,482	13,482
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 30,251</u>	<u>\$ 92</u>	<u>\$ 437,270</u>	<u>\$ 467,613</u>

Credit Risk – S&P Quality Ratings at June 30, 2012

<i>(in thousands)</i> Investment Type	S&P Quality Rating by Fair Value					U.S.	Total Fair Value
	AAA	AA	A	BBB	Not Rated	Government Guaranteed	
Corporate bonds	\$ -	\$ -	\$ -	\$ -	\$ 24,621	\$ -	\$ 24,621
Government bonds	-	-	-	39	-	31,401	31,440
Other fixed income	-	-	-	-	376,191	-	376,191
Hedge event driven	-	-	-	-	-	-	-
Short term investment funds	-	-	-	-	66,857	-	66,857
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 39</u>	<u>\$ 467,669</u>	<u>\$ 31,401</u>	<u>\$ 499,109</u>

<i>(in thousands)</i> Investment Type	Investment Maturities in Years					
	Less Than 1	1 - 5	6 - 10	More Than 10	Maturity not Determined	Total Fair Value
Corporate bonds	\$ -	\$ -	\$ -	\$ 73	\$ 24,548	\$ 24,621
Government bonds	-	31,401	-	39	-	31,440
Other fixed income	-	-	-	-	376,191	376,191
Hedge event driven	-	-	-	-	-	-
Short term investment funds	-	-	-	-	66,857	66,857
	<u>\$ -</u>	<u>\$ 31,401</u>	<u>\$ -</u>	<u>\$ 112</u>	<u>\$ 467,596</u>	<u>\$ 499,109</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

In accordance with the Policy, the Pool manages its exposure to credit risk by diversifying the portfolio, as follows:

<i>(in thousands)</i>		Effective		Effective
Investment Type	2013	Duration	2012	Duration
	Fair Value	(Years)	Fair Value	(Years)
Corporate bonds	\$ 28,891	N/A	\$ 24,621	N/A
Government bonds	30,259	8.92	31,440	1.99
Other fixed income	370,848	N/A	376,191	N/A
Hedge event driven	24,133	N/A	-	N/A
Short term investment funds	13,482	N/A	66,857	N/A
	<u>\$ 467,613</u>		<u>\$ 499,109</u>	

Arkansas Code

The following Arkansas Code sections outline the ability of UAMS to spend any net appreciation in endowment funds:

28-69-604 Rule of construction. Subject to the intent of a donor expressed in the gift instrument, an institution may appropriate for expenditure or accumulate so much of an endowment fund as the institution determines is prudent for the uses, benefits, purposes, and duration for which the endowment fund is established. Unless stated otherwise in the gift instrument, the assets in an endowment fund are donor-restricted assets until appropriated for expenditures by the institution.

28-69-607 Standard of conduct. In the administration of the powers to expend endowment funds, to make and retain investments, and to delegate investment management of institutional funds, members of a governing board shall exercise ordinary business care and prudence under the facts and circumstances prevailing at the time of the action or decision. In so doing they shall consider long- and short-term needs of the institution in carrying out its educational, religious, charitable, or other eleemosynary purposes, its present and anticipated financial requirements, expected total return on its investments, price-level trends, and general economic conditions, and the aggregate value of all endowment funds held by the institution.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

6. Notes and Student Loans Receivable

The net unpaid balances of notes and student loans receivable on June 30, 2013 and 2012, net of allowances of \$4,756,000 and \$4,198,000, respectively, are as follows:

<i>(in thousands)</i>	2013	2012
Perkins loans	\$ 1,293	\$ 1,442
Health professional loans	4,744	5,073
Institutional funds loans	2,979	3,330
University of Arkansas at Fayetteville	773	893
Arkansas State Hospital note receivable	5,874	6,403
Arkansas Department of Health note receivable	1,200	1,461
Miscellaneous	-	10
Total notes and student loans receivable, net	<u>16,863</u>	<u>18,612</u>
Less: Current portion	<u>(2,387)</u>	<u>(2,698)</u>
Notes and student loans receivable, noncurrent, net	<u>\$ 14,476</u>	<u>\$ 15,914</u>

7. Capital Assets

Capital assets of UAMS at June 30 were as follows:

<i>(in thousands)</i>	June 30, 2012	Additions	Transfers	Dispositions	June 30, 2013
Nondepreciable					
Land	\$ 12,570	\$ -	\$ -	\$ -	\$ 12,570
Construction in progress	20,708	40,268	(16,254)	-	44,722
Depreciable					
Buildings and fixtures	933,990	23,591	16,329	(16)	973,894
Improvements other than buildings	2,453	-	-	-	2,453
Equipment	228,209	22,872	1,745	(11,611)	241,215
Leased property	26,151	10,726	(1,820)	(957)	34,100
Other	29,867	208	-	-	30,075
Total capital assets	<u>1,253,948</u>	<u>97,665</u>	<u>-</u>	<u>(12,584)</u>	<u>1,339,029</u>
Less: Accumulated depreciation and amortization					
Buildings and fixtures	267,811	31,470	4	(7)	299,278
Improvements other than buildings	2,441	6	-	-	2,447
Equipment	159,074	19,699	1,694	(11,231)	169,236
Leased property	13,903	4,841	(1,698)	(412)	16,634
Other	18,911	1,031	-	-	19,942
Total accumulated depreciation and amortization	<u>462,140</u>	<u>57,047</u>	<u>-</u>	<u>(11,650)</u>	<u>507,537</u>
Capital assets, net	<u>\$ 791,808</u>	<u>\$ 40,618</u>	<u>\$ -</u>	<u>\$ (934)</u>	<u>\$ 831,492</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

<i>(in thousands)</i>	June 30, 2011	Additions	Transfers	Dispositions	June 30, 2012
Nondepreciable					
Land	\$ 10,797	\$ 1,773	\$ -	\$ -	\$ 12,570
Construction in progress	13,911	18,459	(11,662)	-	20,708
Depreciable					
Buildings and fixtures	881,231	42,723	10,046	(10)	933,990
Improvements other than buildings	2,453	-	-	-	2,453
Equipment	202,420	29,167	2,304	(5,682)	228,209
Leased property	25,478	2,704	(1,836)	(195)	26,151
Other	18,981	9,738	1,148	-	29,867
Total capital assets	<u>1,155,271</u>	<u>104,564</u>	<u>-</u>	<u>(5,887)</u>	<u>1,253,948</u>
Less: Accumulated depreciation and amortization					
Buildings and fixtures	239,295	28,422	-	94	267,811
Improvements other than buildings	2,411	30	-	-	2,441
Equipment	145,811	17,010	1,617	(5,364)	159,074
Leased property	11,016	4,675	(1,617)	(171)	13,903
Other	18,506	405	-	-	18,911
Total accumulated depreciation and amortization	<u>417,039</u>	<u>50,542</u>	<u>-</u>	<u>(5,441)</u>	<u>462,140</u>
Capital assets, net	<u>\$ 738,232</u>	<u>\$ 54,022</u>	<u>\$ -</u>	<u>\$ (446)</u>	<u>\$ 791,808</u>

In addition to the leased property noted, the buildings and fixtures above include \$24,252,000 and \$24,449,000 of net assets under capital leases at June 30, 2013 and 2012, respectively.

Bond interest of \$3,183,000, net of interest income of \$9,000, was capitalized. The interest was from the 2010A and 2010B Series Various Facilities Revenue Bonds, and included \$712,000 interest from fiscal year 2013, and \$1,410,000 interest from fiscal year 2012. In addition, loan interest of \$279,000 was capitalized.

Library holdings comprise books and periodicals, including old and rare books, held by UAMS. The estimated value of the holdings at June 30, 2013 and 2012 was \$1,308,000 and \$1,366,000, respectively. UAMS has not reported library holdings in the accompanying statements of net position.

8. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities consist of the following at year-end:

<i>(in thousands)</i>	2013	2012
Trade payables	\$ 20,197	\$ 12,921
Accrued wages	41,260	39,884
Miscellaneous payables	15,043	14,182
Total accounts payable and accrued liabilities	<u>\$ 76,500</u>	<u>\$ 66,987</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

9. Long-Term Obligations

Changes in long-term obligations during fiscal year 2013 were as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Bonds payable	\$ 292,166	\$ 125,206	\$ 134,445	\$ 282,927
Notes payable	14,984	70,886	17,423	68,447
Capital leases	33,433	14,880	9,309	39,004
Total debt	340,583	210,972	161,177	390,378
Compensated absences	52,484	3,570	9,023	47,031
Other postemployment benefits	22,225	2,704	120	24,809
Total obligations	<u>\$ 415,292</u>	<u>\$ 217,246</u>	<u>\$ 170,320</u>	<u>\$ 462,218</u>

The current and long-term portions of the categories noted above were as follows at June 30, 2013:

	Current	Long Term	Total
Bonds payable	\$ 7,255	\$ 275,672	\$ 282,927
Notes payable	12,977	55,470	68,447
Capital leases	8,121	30,883	39,004
Total debt	28,353	362,025	390,378
Compensated absences	2,881	44,150	47,031
Other postemployment benefits	-	24,809	24,809
Total obligations	<u>\$ 31,234</u>	<u>\$ 430,984</u>	<u>\$ 462,218</u>

Changes in long-term obligations during fiscal year 2012 were as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Bonds payable	\$ 301,704	\$ 8,341	\$ 17,879	\$ 292,166
Notes payable	7,363	9,570	1,949	14,984
Capital leases	35,698	5,377	7,642	33,433
Total debt	344,765	23,288	27,470	340,583
Compensated absences	43,634	8,850	-	52,484
Other postemployment benefits	19,273	2,952	-	22,225
Total obligations	<u>\$ 407,672</u>	<u>\$ 35,090</u>	<u>\$ 27,470</u>	<u>\$ 415,292</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

The current and long-term portions of the categories noted above were as follows at June 30, 2012:

	Current	Long Term	Total
Bonds payable	\$ 9,300	\$ 282,866	\$ 292,166
Notes payable	1,896	13,088	14,984
Capital leases	<u>7,522</u>	<u>25,911</u>	<u>33,433</u>
Total debt	18,718	321,865	340,583
Compensated absences	2,859	49,625	52,484
Other postemployment benefits	<u>-</u>	<u>22,225</u>	<u>22,225</u>
Total obligations	<u>\$ 21,577</u>	<u>\$ 393,715</u>	<u>\$ 415,292</u>

UAMS has bonds outstanding for the Patient Bed Tower, Radiation Oncology Center Building, Residence Hall, Psychiatry Building, power plant, the East Parking Deck and land and capital improvements. The income from the revenue-producing facilities, along with a portion of tuition and fees, is pledged to meet the principal and interest payments of certain bonds. Separate accounting is not required for these facilities under the provisions of the debt instruments; accordingly, segment reporting is not required for financial reporting purposes.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

A summary of the principal amount of outstanding debt is as follows at June 30, 2013 and 2012:

<i>(in thousands)</i>		2013	2012
Bonds Payable			
Various Facility Revenue Bonds, Series 2006, \$107,500,000 original amount, plus a premium of \$5,048,000, due annually to 2036 with \$35,305,000 in term bonds due 2036, various fixed interest rates of 3.40% to 5.00% collateralized by pledged revenue.	PAR	\$ 93,820	\$ 95,985
	Premium	3,827	3,996
Parking System Revenue Refunding Bonds, Series 2010, \$7,605,000 original amount plus a premium of \$560,000, due annually to 2019, various fixed interest rates of 2.0% to 4.5% over the life of the issue, collateralized by a pledge of gross revenue derived from all parking facilities owned by UAMS.	PAR	6,130	6,885
	Premium	371	433
Various Facility Revenue Bonds, Series 2010A, \$42,680,000 original amount plus a premium of \$2,876,000 due annually to 2030, various fixed interest rates of 2.00% to 5.00%, collateralized by pledged revenue.	PAR	41,905	42,295
	Premium	2,512	2,656
Various Facility Revenue Bonds, Series 2010B (taxable), \$3,680,000 original amount, due annually to 2013, various fixed interest rates of 1.20% to 1.93% over the life of the issue, collateralized by pledged revenue.	PAR	1,250	2,475
Parking System Revenue Refunding Bonds, Series 2011, \$8,995,000 original amount, due annually to 2034. Used to advance refund the Series 2004 Parking System Revenue Construction Bonds. Various fixed interest rates of 2.00% to 4.25% over the life of the issue, collateralized by a pledge of gross revenue derived from all parking facilities owned by UAMS.	PAR	8,580	8,985
	Discount	(51)	(53)
Various Facility Revenue Bonds, Series 2013, \$112,665,000 original amount, \$16,667,000 premium due annually to 2034. Used to advance refund the Series 2004A and 2004B Various Facility Bonds. Various fixed interest rates of 1.0% to 5.0% over the life of the issue, collateralized by pledged revenue.	PAR	112,665	N/A
	Premium	16,567	
Various Facility Revenue Refunding Bonds, Series 2004A, \$54,085,000 original amount plus a premium of \$4,797,000, due annually to 2018, various fixed interest rates of 4.00% to 5.00% collateralized by pledged revenue.	PAR	-	30,320
	Premium	-	2,187
Various Facility Revenue Construction Bonds, Series 2004B, \$95,915,000 original amount, plus a premium of \$3,412,000, due annually to 2034, various fixed interest rates of 2.0% to 5.0% over the life of the issue, collateralized by pledged revenue.	PAR	-	94,030
	Premium	-	2,545
	Deferred Loss Amortization	<u>(4,649)</u>	<u>(573)</u>
	Total Bonds Payable	<u>\$ 282,927</u>	<u>\$ 292,166</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

Scheduled maturities of bonds and notes payable are as follows. Interest on variable rate debt is calculated based on the rate in effect at June 30, 2013:

<i>(in thousands)</i>	Bonds Payable				Notes Payable		
	Principal	Interest	Premium Amortized	Total	Principal	Interest	Total
2014	\$ 7,255	\$ 11,982	\$ 1,148	\$ 20,385	\$ 12,976	\$ 988	\$ 13,964
2015	8,045	11,753	1,148	20,946	9,809	828	10,637
2016	8,315	11,490	1,148	20,953	9,874	668	10,542
2017	8,610	11,188	1,148	20,946	14,968	506	15,474
2018	8,945	10,830	1,148	20,923	9,197	255	9,452
2019–2023	51,530	47,502	5,496	104,528	9,345	110	9,455
2024–2028	63,165	33,809	5,435	102,409	1,828	-	1,828
2029–2033	72,690	16,818	5,060	94,568	300	-	300
2034–2037	35,795	2,608	1,495	39,898	150	-	150
	<u>\$ 264,350</u>	<u>\$ 157,980</u>	<u>\$ 23,226</u>	<u>\$ 445,556</u>	<u>\$ 68,447</u>	<u>\$ 3,355</u>	<u>\$ 71,802</u>

On May 14, 2013, UAMS issued revenue refunding bonds of \$112,665,000 (par value) with an interest rate of 1% to 5% to advance refund Various Facility Revenue Refunding Bonds Series 2004A with an interest rate of 5%, and Various Facility Revenue Construction Bonds Series 2004B bonds with an interest rate of 3.25% to 5%, with a combined par value of \$150,000,000. The 2004A bonds mature on November 1, 2018, and the 2004B bonds mature on November 1, 2034 and are callable on November 1, 2014. The revenue refunding bonds were issued at a premium of \$16,667,000 and, after paying issuance costs of \$210,000 and underwriter's discount of \$653,000, the net proceeds were \$128,469,000, net of accrued interest of \$175,000. The net proceeds from the issuance of the revenue refunding bonds were used to purchase U.S. government securities and provide debt service payments until the term bonds are called on November 1, 2014. The advance refunding met the requirements of an in-substance debt defeasance and the 2004A and 2004B Series bonds were removed from UAMS financial statements. As a result of the advance refunding, the UAMS reduced its total debt service requirements by \$14,429,000, which resulted in an economic gain (difference between the present value of the debt service payments on the old and new debt) of \$13,600,000. All defeased debt in prior years has been refunded, leaving only \$124,352,000 from the defeasance of the 2004 A and B series as the outstanding defeased balance as of June 30, 2013.

The Parking System Revenue Refunding Bonds, Series 2011, were issued in November 2011. The 2011 issue provided \$8,995,000 necessary to advance refund the UA Board's Parking System Revenue Construction Bonds, Series 2004. The bonds bear interest at various fixed interest rates from 2.00% to 4.125%. Principal payments are made annually until July 2034. Interest payments are made semiannually. The refunding reduced cash flows by \$668,000. There was a deferred refunding loss on the transaction of \$589,000 which will be amortized as a component of interest expense until July 2034.

The Various Facility Revenue Bonds, Series 2010A and 2010B, were issued in December 2010. The 2010A issue provided \$42,680,000 for Patient Tower Building Improvements, Winthrop P. Rockefeller Cancer Institute Improvements, Central Energy Improvements, Operating Room and Surgical Suite Improvements, and various other acquisitions and improvements. The bonds bear interest at various fixed interest rates from 2.0% to 5.0% and principal payments are due annually with interest payments due semiannually until the year 2030. The 2010B (Taxable) issue provided \$3,680,000 for acquiring land and properties for expansion and other University

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

related purposes. The bonds bear interest at various fixed interest rates from 1.20% to 1.93% and principal payments are due annually with interest payments due semiannually until fiscal year 2014.

The Parking System Revenue Refunding Bonds, Series 2010, were issued in June 2010. The 2010 Bonds were issued to refund the Parking System Revenue Construction and Refunding Bonds, Series 1998. The \$7,605,000 issue enabled UAMS to take advantage of lower rates, with the 2010 Bonds bearing interest at various fixed rates from 2.0% to 4.5%. Principal payments are due annually, with interest payments due semiannually until the year 2019. The refunding resulted in a net present value benefit of \$770,000 and a deferred refunding loss of \$230,000, which will be amortized as a component of interest expense until June 30, 2020. For current and advance refunding resulting in defeasance of debt, the difference between the reacquisition price and the net carrying amount of the refunded debt is deferred and amortized as a component of interest expense until July 1, 2019.

The Various Facility Revenue Bonds, Series 2006, were issued in March 2006. The 2006 issue provided an additional \$107,500,000 for the recent expansion of the UAMS Hospital to include a new Patient Bed Tower, new Residence Hall, new Psychiatry Building, and a new power plant. The bonds bear interest at various fixed interest rates from 3.4% to 5.0%, and principal payments are due annually with interest payments due semiannually until the year 2036.

10. Commitments

Capital Leases

Scheduled maturities of capital lease commitments outstanding as of June 30, 2013 are as follows:

<i>(in thousands)</i>	Principal	Interest	Total
2014	\$ 8,121	\$ 1,458	\$ 9,579
2015	7,069	1,178	8,247
2016	6,764	896	7,660
2017	5,034	641	5,675
2018	3,452	486	3,938
2019–2022	8,564	948	9,512
	<u>\$ 39,004</u>	<u>\$ 5,607</u>	<u>\$ 44,611</u>

Operating Leases

The following is a schedule by years of future minimum rental payments required under operating leases that have initial or remaining noncancelable lease terms in excess of one year as of June 30, 2013:

<i>(in thousands)</i>	
2014	\$ 5,816
2015	3,769
2016	1,709
2017	747
2018	92
2019–2022	-
Total minimum payments required	<u>\$ 12,133</u>

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

Rental expense for operating leases for the years ended June 30, 2013 and 2012 was approximately \$8,976,000 and \$9,456,000 respectively, and is included in supplies and other services in the accompanying statements of revenues, expenses, and changes in net position.

Construction Projects

Construction in progress at June 30, 2013 included the Surgical Services renovation and the technology upgrade for the parking decks and surface lots. At June 30, 2013, construction contracts outstanding were approximately \$7,473,000.

Outstanding Commitments

At June 30, 2013 and 2012, UAMS had outstanding purchase orders for normal operating supplies and equipment amounting to approximately \$66,195,000 and \$155,796,000, respectively.

11. Retirement Benefits

All active employees of UAMS who work 20 or more hours a week participate in the Arkansas Teacher Retirement System (ARTRS), Arkansas Public Employee Retirement System (APERS), or the University of Arkansas Optional Retirement Plan (UAORP), which is funded through the Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA-CREF) and Fidelity Investments. ARTRS was established as an actuarial reserve system, with a financial base derived from employer and employee contributions and income from investments to pay future benefits. It pays retirement benefits based on length of service and an average of the three highest fiscal years' earnings. Benefit provisions are established and amended by State of Arkansas Statute (A.C.A. 266). UAMS' required contribution rate has been 14% since 2007. ARTRS issues a publicly available financial report, which may be obtained by writing or calling: ARTRS, 1400 West Third Street, Little Rock, Arkansas 72201, 501-682-1517. The gross payroll amount for UAMS employees covered by ARTRS for the years ended June 30, 2013 and 2012 was \$280,700 and \$439,800, respectively. UAMS' total salaries were \$666,263,000 and \$649,819,000 for fiscal years 2013 and 2012, respectively. Total employer contributions to ARTRS in fiscal years 2013, 2012, and 2011 were \$39,300, \$61,500, and \$77,000, respectively. Employee contributions to ARTRS in fiscal years 2013 and 2012 were \$12,400 and \$19,300, respectively.

APERS is a cost-sharing multiple-employer defined benefit plan administered by the State of Arkansas, which pays retirement benefits based on length of service and an average of the five highest fiscal years' earnings. Vesting is effective after 10 years of participation in the plan. Benefit provisions are established and amended by State of Arkansas Statute (A.C.A. 24). UAMS' required contribution rate was 14.24% in 2013 and 13.47% in 2012. APERS issues a publicly available financial report, which may be obtained by writing or calling: APERS, One Union National Plaza, 124 W. Capitol, 5th Floor, Little Rock, Arkansas 72201, 501-682-7855. The gross payroll amount for UAMS employees covered by APERS for the years ended June 30, 2013 and 2012 was \$7,566,000 and \$6,582,000, respectively. Total employer contributions to APERS in fiscal years 2013, 2012, and 2011 were \$1,078,000, \$960,900, and \$788,200, respectively. Employee contributions to APERS in fiscal years 2013 and 2012 were \$238,500 and \$210,500, respectively.

The UAORP was established by the Board of Trustees of the University of Arkansas System. These funds represent a defined contribution plan as set forth in Sections 403(b) and 457(b) of the Internal Revenue Code. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings.

UAMS automatically contributes 5% of an employee's regular salary to a TIAA-CREF or Fidelity Fund retirement account, allocated between the two funds according to the employee's choice. In addition, employees may make voluntary contributions of any amount up to the individual maximum allowance.

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

For any contributions an employee makes in excess of 5% of regular salary, UAMS makes an equal contribution up to a maximum total UAMS contribution of 10% of regular salary up to a maximum of \$25,500 per employee, which is the IRS maximum for tax year 2013. All contributions for faculty members and nonclassified employees are vested immediately. For classified employees, UAMS contributions will be vested when one of the following occurs: three years of service is completed; when the participant reaches the age of 70; or the participant contributes at least 5% of regular salary for at least six months. The eligible salary earnings for UAMS employees covered by UAORP for the years ended June 30, 2013 and 2012 was \$602,270,000 and \$587,024,000, respectively. Total employer contributions during fiscal years 2013 and 2012 to TIAA-CREF and Fidelity were \$46,745,000 and \$52,423,000, respectively. Employee contributions to TIAA-CREF and the Fidelity Fund in the fiscal years 2013 and 2012 were \$52,423,000 and \$50,359,000, respectively.

In addition to providing retirement benefits, UAMS arranges health, dental, and life insurance for retired and disabled employees and their families. Substantially, all of UAMS' employees may become eligible for those benefits if they meet normal retirement requirements while still working for UAMS. The number of enrolled retirees was 764 and 688 as of June 30, 2013 and 2012, respectively. The participants of this program incur the total premium for this insurance. There is no direct expense for these services incurred by UAMS.

12. Other Postemployment Benefits (OPEB)

The University offers postemployment health (including prescription drugs) and dental benefits along with life insurance (\$10,000 available coverage) to eligible retirees. Health and dental benefits are provided in the University's self-funded plan sponsored by the Board of Trustees of the University of Arkansas System for current and retired employees of Fayetteville (UAF), Little Rock (UALR), Medical Sciences (UAMS), Monticello (UAM), Pine Bluff (UAPB), Phillips (PCCUA) and Batesville (UACCB) campuses, the Cooperative Extension Service of the Division of Agriculture (CES), the Arkansas School for Mathematics, Sciences, and the Arts (ASMSA), and the University of Arkansas System Administration (SYSTEM). The plan is considered a single-employer defined benefit plan. The System Administration manages and administers the plan. Although benefits are also provided under the University's plan for the University of Arkansas Foundation, Inc. (the Foundation) and the University of Arkansas Winthrop Rockefeller Institute, no postemployment benefit is accrued by the University for these private entities. Financial activities of the plan are reported in the University's consolidated financial report.

Governmental entities recognize and match other postretirement benefit costs with related services received and also provide information regarding the actuarially calculated liability and funding level of the benefits associated with past services. Accordingly, UAMS accrued \$2,828,000 and \$2,952,000 in retiree healthcare expense during the fiscal years ended June 30, 2013 and 2012, respectively.

For those campuses in the University's self-funded plan, retirees qualify for postretirement benefits as follows:

Participation: Employees who retire with a combination of age and years of service of at least 70 years with at least 10 years of coverage under the plan are eligible to participate. Retirees may cover spouses and eligible dependent children. Surviving spouses can continue coverage after retiree's death. Retirees can continue coverage past Medicare eligibility age (age 65 or disabled) with the University plan paying secondary to Medicare.

Benefit Provided: Retirees participate in the plan at the same premium rate as an active employee.

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

Required Contribution Ratio: Retirees pay 100% of premium. The pre-65 premium is based upon blended active and pre-65 retiree claims experience. The valuation accounts for the implicit subsidy that arises as a result. Employer costs are funded on a pay-as-you-go basis.

Summary of Key Actuarial Methods and Assumptions

University Self-Funded Plan

Valuation date	July 1, 2012 valuation for the fiscal year ended June 30, 2013
Valuation year	Census data was collected as of November 1, 2012. Liabilities were measured as of November 1, 2012 and rolled backward to the July 1, 2012 valuation date.
Actuarial cost method	Projected unit credit
Amortization method	30 years open, level percentage of payroll
Asset valuation method	N/A
Discount rate	4.50%
Projected payroll growth rate	4.00%
Medical trend rate	Initial rate of 8.0% unchanged for 3 years, with a 0.5% decrease each year afterwards to an ultimate rate of 5.0%.
Dental trend rate	Dental benefits were excluded from the valuation since expected retiree contributions are sufficient to fully cover expected costs.

General Overview of the Valuation Methodology

The process of determining the liability for retiree medical benefits is based on many assumptions about future events. Future increases in healthcare costs are affected by many factors, including: medical inflation; change in utilization patterns; technological advances; cost shifting; cost leveraging; and changes to government medical programs, such as Medicare.

The required frequency of valuations per GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, depends on the number of members in the plan. Even though the University's self-funded plan only requires it every two years, a full actuarial valuation is performed every other year and a roll forward valuation is performed in the interim years. No decision has been made at this time as to whether annual or biennial valuations will be made in the future.

Actuarial calculations reflect a long-term perspective. Actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

Calculations are based on the types of benefits provided under the terms of each plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the University and plan members in the future.

Changes in Actuarial Assumptions and Methods

For fiscal year 2012, the mortality rates were changed to the RP-2000 Fully Generational Combined Healthy Mortality Table projected by scale AA to better reflect anticipated future mortality improvements. For fiscal year 2013, the healthcare trend rate assumption was changed to better reflect anticipated future experience.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

Medical Coverage – Retirees Not Eligible for Medicare

Claim experience for the period January 1, 2011 through December 31, 2012 was used to develop the claims cost for non-Medicare-eligible retirees. The paid claims data was converted to an incurred basis using a completion factor approach. This experience includes 612 life years of exposure and was deemed to be 80% credible. The experience was combined with the active claims experience adjusted for demographic differences to produce the per capita claims costs used in the valuation. Adjustment factors were then applied to develop expected claims by age to be used in the valuation. Expected retiree premiums were developed to represent the expected cost sharing level anticipated by the University. Retiree premiums were also age-adjusted for use in the valuation.

Medical Coverage – Retirees Eligible for Medicare

Medical and prescription drug claims for the period January 1, 2011 through December 31, 2012 was used to develop per capita claims cost for Medicare-eligible retirees. This experience includes 3,000 life years of exposure and was deemed to be fully credible. Based on this analysis, it was concluded that the retiree contributions are sufficient to fully cover the expected claims costs as intended. As such, the cost for Medicare eligible retirees was excluded from this valuation.

Determination of Annual Required Contribution (ARC) and End-of-Year Accrual

	July 1	
	2012	2011
Unfunded actuarial accrued liability	\$ 26,463	\$ 28,120
Annual Required Contribution (ARC)		
Normal cost	2,008	2,102
Amortization of the unfunded actuarial accrued liability over 30 years using level percentage of payroll amortization	945	1,004
Interest	132	140
Annual Required Contribution (ARC)	3,085	3,246
Annual OPEB Cost		
Interest on net OPEB obligation	1,000	867
ARC amortization adjustment	(829)	(719)
Annual OPEB Cost	3,256	3,394
Less: Expected employer contributions	(672)	(442)
End-of-year accrual	2,584	2,952
Beginning of year liability	22,225	19,273
End of year of year liability	\$ 24,809	\$ 22,225

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

Schedule of Employer Contributions

	Annual Contributions	Expected Contributions	Percentage Contributed
Fiscal Years Ended			
June 30, 2013	\$ 3,256	\$ 672	20.64 %
June 30, 2012	3,394	442	13.02 %
June 30, 2011	3,071	449	14.62 %

Since there is no funding, the expected contributions are the expected implicit subsidy payments. The implicit rate subsidy is the difference between the true cost of medical benefits and the cost-sharing premiums paid by the retiree.

Schedule of Funding Progress (Unaudited)

	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as Percentage of Covered Payroll
Fiscal Years Ended						
June 30, 2013	\$ -	\$ 26,463	\$ 26,463	\$ -	\$ 610,117	4 %
June 30, 2012	-	28,120	28,120	-	594,046	5 %
June 30, 2011	-	25,114	25,114	-	552,717	5 %

13. Affiliated Entities

The UA Foundation operates as a nonprofit benevolent corporation for charitable educational purposes. It was established to benefit the University, or its students, faculty, and staff. The Board of Directors of the Foundation includes four members who are also members, or former members, of the University Of Arkansas System Board Of Trustees. Support, by the Foundation on behalf of UAMS, was \$27,374,000 and \$33,908,000 for the years ended June 30, 2013 and 2012, respectively.

Based on information provided by the Foundation, during the years ended June 30, 2013 and 2012, respectively, revenue of \$42,916,000 and \$27,870,000 was received by the Foundation for the benefit of UAMS. These revenue amounts are provided by the Foundation and are unaudited.

14. Related-Party Transactions

Notes receivable from related parties at June 30 are as follows:

<i>(in thousands)</i>	2013	2012
University of Arkansas at Fayetteville	\$ 773	\$ 893
Arkansas State Hospital	5,874	6,403
Arkansas Department of Health	1,200	1,461
Total included in notes and student loans receivable (Note 6)	<u>\$ 7,847</u>	<u>\$ 8,757</u>

In addition to the above transactions, UAMS conducts various activities with University of Arkansas System campuses and the State of Arkansas. These activities take place in the normal course of business and are on an arm's-length basis.

University of Arkansas for Medical Sciences

Notes to Financial Statements

June 30, 2013 and 2012

15. Contingencies

Amounts received and expended by UAMS under various federal and state programs are subject to audit by governmental agencies. Management believes that adjustments, if any, which might result from such audits would not have a significant impact on the financial position of UAMS. Immunity provisions in Arkansas law prohibit suits naming the Board of Trustees of the University of Arkansas System or UAMS as a defendant in Arkansas State courts. Employees of UAMS acting in good faith in the course and scope of their employment may be sued in state courts, but only to the extent of maintained insurance coverage. UAMS maintains malpractice insurance for certain employees under a claims-made policy. Premiums are accrued based on a retrospective rating plan. UAMS incurred costs of \$4,000,000 and \$3,469,000 for this insurance during the years ended June 30, 2013 and 2012, respectively. A party may bring an action against UAMS through the Arkansas State Claims Commission (the Claims Commission). The Claims Commission may award a claim of up to \$7,500 without further review or appropriation. Awards that the Claims Commission approves in excess of \$7,500 must be approved and appropriated by the Arkansas State Legislature. Appropriations of this type, if any, reduce appropriations from the state to UAMS in the period in which the claim is appropriated.

UAMS is involved in litigation and regulatory investigations arising in the normal course of business. Management and counsel believe that these matters will be resolved without material adverse effect on UAMS' financial statements.

UAMS employees and their eligible dependents may participate in the University of Arkansas System sponsored self-funded health plan, which is administered by third parties who are responsible for the processing of claims and administration of cost containment. The monthly premiums are established by the University of Arkansas System at a level sufficient to cover claims expected in the plan. UAMS and the employees share the cost of the monthly insurance premium with the total premium and the portion paid by UAMS varying depending on the insurance coverage chosen by the employee. The employee's portion and UAMS' portion of the premium are remitted the following month to the University of Arkansas System with UAMS recognizing as expense its portion of the premiums in the month to which it relates. UAMS has not recorded any other amounts in the financial statements related to the health plan.

In fiscal year 2006, the Arkansas Development Finance Authority (the Authority) issued \$36,775,000 in Tobacco Settlement Revenue Bonds. The Authority has made the proceeds of the bonds available to the UA Board to fund an expansion to the Arkansas Cancer Research Center. The bonds have an approximate yield to maturity of 4.77% to 5.10% and principal and accumulated interest are payable beginning in 2021 through 2031 for \$22,158,000 of serial bonds and beginning in 2036 through 2046 for \$14,617,000 of term bonds.

Funds received from the Arkansas Tobacco Settlement Funds Act of 2000 are pledged for debt service (Debt Service Revenues) and are the primary source of payment for the bonds. In accordance with a Loan Agreement dated June 1, 2006 between the UA Board and the Authority, the UA Board will be required to make debt service payments on the Series 2006 Bond issue in the event of a shortfall in tobacco settlement revenues. However, no such payments will be made unless the Debt Service Revenues are insufficient to make such payments. Management believes the Debt Service Revenues will be sufficient to service the entire principal and interest due. The *Global Insights USA, Inc.* report, prepared in August 2006, on the *Forecast of U.S. Cigarette Consumption (2004-2046)* indicates that tobacco consumption in 2046 is expected to decline by 54% from the 2003 level. For fiscal year 2003, Arkansas received \$60,067,000 from the Tobacco Settlement Fund. Using the 54% decline from above, Arkansas should receive approximately \$27,600,000 in 2046 with the first \$5,000,000 dedicated to pay the debt service on the above bond issue.

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

If Debt Service Revenues would have been considered insufficient at June 30, 2013, UAMS would have incurred a liability of \$51,942,000 related to issue. This amount includes drawdown of funds related to the project, issuance costs, discounts, accreted interest, and other expenses related to the issue.

The revenues pledged by UAMS to secure the Loan Agreement consist of inpatient service fees and fees collected from other ancillary, therapeutic, and diagnostic services provided within the walls of the Hospital but exclude (a) physician-generated revenues, (b) State appropriations, and (c) revenues restricted for other purposes.

16. Functional Classification of Expenses

For financial reporting purposes, UAMS classifies its operating expenses by their natural classification. The tables below summarize these expenses by their functional classification:

<i>(in thousands)</i>	Year Ended June 30, 2013				
	Compensation and Benefits	Supplies and Other Services	Scholarships and Fellowships	Depreciation and Amortization	Total
Patient care	\$ 449,945	\$ 231,183	\$ -	\$ -	\$ 681,128
Instruction	124,460	11,292	-	-	135,752
Research	83,458	39,361	-	-	122,819
Public services	18,277	21,629	-	-	39,906
Academic support	18,074	5,149	-	-	23,223
Student services	1,994	1,624	-	-	3,618
Institutional support	85,843	14,401	-	-	100,244
Operation and maintenance of plant	31,392	16,803	-	-	48,195
Scholarships and awards	-	-	242	-	242
Auxiliary	4,253	3,012	-	-	7,265
Depreciation and amortization	-	-	-	57,047	57,047
Other	1,225	9,311	-	-	10,536
	<u>\$ 818,921</u>	<u>\$ 353,765</u>	<u>\$ 242</u>	<u>\$ 57,047</u>	<u>\$ 1,229,975</u>

<i>(in thousands)</i>	Year Ended June 30, 2012				
	Compensation and Benefits	Supplies and Other Services	Scholarships and Fellowships	Depreciation and Amortization	Total
Patient care	\$ 421,463	\$ 236,475	\$ -	\$ -	\$ 657,938
Instruction	118,569	10,372	-	-	128,941
Research	79,351	38,301	-	-	117,652
Public services	19,517	65,868	-	-	85,385
Academic support	17,001	4,733	-	-	21,734
Student services	2,025	1,764	-	-	3,789
Institutional support	107,191	7,510	-	-	114,701
Operation and maintenance of plant	31,486	10,919	-	-	42,405
Scholarships and awards	-	-	342	-	342
Auxiliary	3,943	3,081	-	-	7,024
Depreciation and amortization	-	-	-	50,542	50,542
Other	784	13,049	-	-	13,833
	<u>\$ 801,330</u>	<u>\$ 392,072</u>	<u>\$ 342</u>	<u>\$ 50,542</u>	<u>\$ 1,244,286</u>

University of Arkansas for Medical Sciences
Notes to Financial Statements
June 30, 2013 and 2012

17. Out-of-Period Adjustments

During fiscal year 2013, UAMS recorded an out-of-period adjustment which increased Other operating revenue and the Increase in net position by \$13,551,000. The adjustment related to the recognition in 2013 of a refund from the Internal Revenue Service (IRS) of Federal Insurance Contribution Act (FICA) taxes paid by UAMS on wages earned for services performed by medical residents for calendar years 1996 through 1999. The wages of medical residents during this period were deemed by the IRS to be exempt from FICA taxes based on the student exception. On April 1, 2005, new IRS regulations went into effect whereby the earnings of medical residents became subject to FICA taxes. Appropriately, UAMS did not pay FICA taxes on medical resident earnings after calendar 1999 until the new regulations went into effect. The majority of the refund and related interest should have been recognized prior to fiscal year 2012, when the IRS announced they would honor the appropriate claims for refund of FICA taxes. UAMS evaluated the out-of-period adjustment, in relation to the current period, as well as the period in which it originated, and concluded the adjustment is not material to the impacted periods.

During fiscal year 2013, UAMS recorded an out-of-period adjustment to capitalize interest on capital projects previously expensed in the amount of \$1,061,000 and \$1,410,000 in fiscal years 2011 and 2012, respectively. UAMS evaluated the out-of-period adjustment, in relation to the current period, as well as the periods in which it originated, and concluded the adjustment is not material to the impacted periods.

18. Subsequent Events

UAMS evaluated subsequent events through October 2, 2013, which is the date the financial statements were issued, and determined there were no matters that required adjustment to or disclosure in the financial statements.