UNIVERSITY OF VIRGINIA MEDICAL CENTER

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2012

APA
Auditor of
Public Accounts
COMMONWEALTH OF VIRGINIA

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MANAGEMENT'S DISCUSSION AND ANALYSIS
(unaudited)

The following discussion and analysis provides an overview of the financial position and activities of the University of Virginia's Medical Center (Medical Center) for the year ended June 30, 2012, with comparative information for the year ended June 30, 2011. This discussion has been prepared by management and should be read in conjunction with the financial statements, and the notes thereto, which follow this section.

The Medical Center is one of the three operating divisions of the University of Virginia. The Vice President and Chief Executive Officer of the Medical Center provide overall leadership and management of the Medical Center. The Medical Center is an integrated network of primary and specialty care services ranging from wellness programs and routine checkups to the most technologically advanced care. The hub of the Medical Center is a 676 licensed bed hospital with a state designated Level 1 trauma center located on the Charlottesville campus. The Medical Center also has a 40-licensed bed Transitional Care Hospital located west of the Charlottesville campus. In addition, primary and specialty care are provided at clinic locations throughout central Virginia communities.

Financial Highlights

	2012	2011
Operating revenues	$1,215.5	$1,095.2
Operating income	$84.8	$95.6
Net non-operating revenue	0.8	65.9
Net Income	$85.6	$161.5
* in millions		

At the end of fiscal year 2012, the operating income was $84.8 million, compared to fiscal year 2011operating income of $95.6 million. The current fiscal year performance resulted from continued efforts by management and staff in controlling labor and supply expense. Additional contributing factors to operating income were the following: 2.5 percent increase in admissions, 4.5 percent increase in surgeries, and 8.1 percent increase in outpatient visits.

Increased discharges are attributable to the following departments: Cardiology, Neurology, Medicine, and Surgery. Admissions were also supported by fiscal year 2012 being the first full year of operations for the Transitional Care Hospital. The growth in outpatient visits was due to increased demand in the local market for existing services, focused efforts to increase utilization of the University of Virginia Health System services by employees of both the Medical Center and the University, and the acquisition of a large physician oncology group.

In 2010, the IRS made an administrative determination to accept the position that medical residents are exempt from FICA taxes based on the student exception for tax periods ending before April 1, 2005. The IRS subsequently established a process for medical residents and institutions to file claims. In fiscal year 2011, the Medical Center filed for a refund of $11 million. The Medical Center's claim has been perfected by the IRS. The Medical Center has reduced fringe benefit expense by this amount. In 2012, the IRS provided the applicable interest rates for perfected claims. The Medical Center reduced fringe benefit expense by $13 million for the expected interest associated with the claim.

The Medical Center participated in a class action lawsuit against CMS, which alleged that CMS had incorrectly completed changes in payments to hospitals for 2004 through 2011. The lawsuit was settled in favor of the hospitals and the net benefit to the Medical Center in fiscal year 2012 was $8.2 million.

The Medical Center's operating income in fiscal year 2012 includes a $17.3 million reduction of expenses for the settlement of a multi-year dispute with a vendor.

Net non-operating revenue decreased by $65.1 million from fiscal year 2011 to fiscal year 2012. Several factors contributed to the decrease. Investment income (both realized and changes in fair market value) was $18.8 million in fiscal year 2012 or $60.4 million less than the investment income recorded in fiscal year 2011. Also contributing to the decline in net non-operating revenue was gift income decreasing by $10.9 million. In addition, earnings from affiliates, loss on the disposal of assets, and other departmental payments increased by $3.8 million. The gain sharing accrual made to the University of Virginia, School of Medicine was $8.0 million in fiscal year 2012, which is a $10.0 million decrease from fiscal year 2011. The gain sharing accrual is based on the Medical Center exceeding operating margin thresholds.

Financial Statements

The Medical Center's financial report includes three financial statements: the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows. These financial statements are prepared in accordance with the Governmental Accounting Standards Board (GASB) Statement 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*; GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis of Public Colleges and Universities* and with the Financial Accounting Standards Board requirements for Health Care Organizations.

The Statement of Net Assets presents the financial position of the Medical Center at the end of the fiscal year, including all assets and liabilities of the Medical Center. Net assets are the difference between total assets and total liabilities and are one of the indicators used to evaluate the current financial condition of the Medical Center. In contrast, the change in net assets indicates whether the overall financial condition improved or worsened during the year. Shown below is a summary of the Medical Center's Statements of Net Assets.

Statement of Net Assets
As of June 30, 2012 and 2011

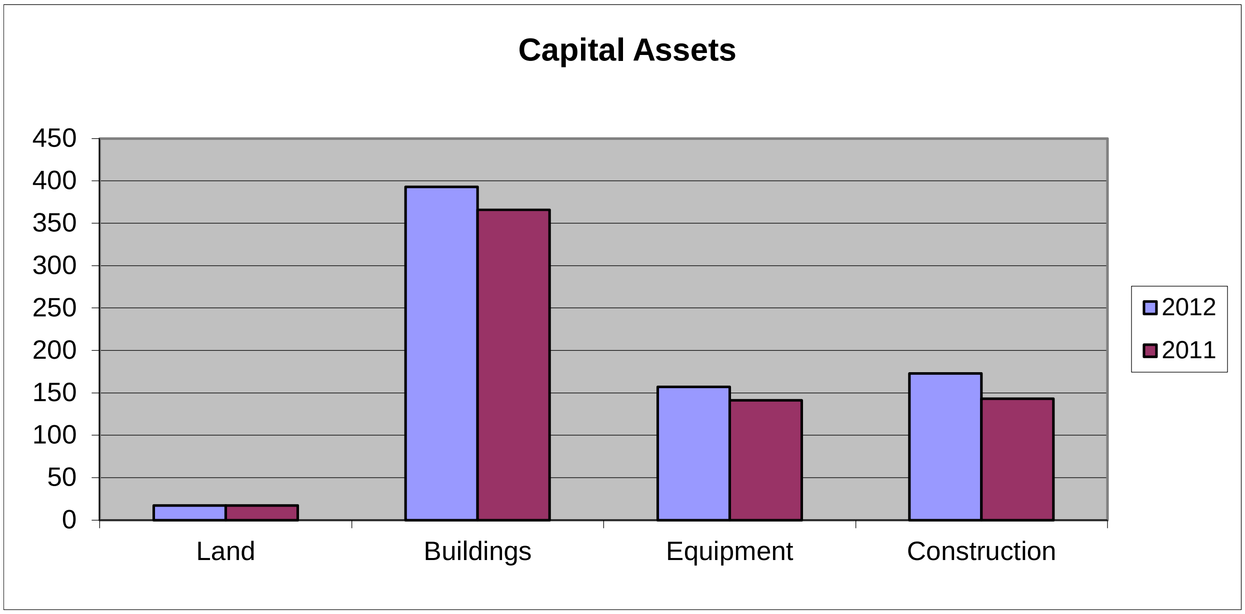
	2012	2011	Increase(Decrease) Amount	Percent
Assets:				
Current assets	$ 348.6	$ 284.8	$ 63.8	22.4%
Capital Assets	731.8	667.5	64.3	9.6%
Other non-current assets	812.7	748.9	63.8	8.5%
Total Assets	1,893.1	1,701.2	191.9	11.3%
Liabilities:				
Current Liabilities	259.8	213.6	46.2	21.6%
Non-current liabilities	433.7	373.5	60.2	16.1%
Total Liabilities	693.5	587.1	106.4	18.1%
Net Assets				
Invested in capital assets, net of related debt	416.1	402.6	13.5	3.4%
Restricted for				
Nonexpendable	53.1	53.1	-	0.0%
Expendable	65.6	62.9	2.7	4.3%
Unrestricted	664.8	595.5	69.3	11.6%
Total net assets	$1,199.6	$1,114.1	$ 85.5	7.7%

* in millions

During fiscal year 2012, the Medical Center's financial position remained positive. Net assets increased $85.5 million, or 7.7 percent, primarily due to strong operating income and the continued increase in the fair market value of the Medical Center's investments.

The value of capital assets net of depreciation increased $64.3 million from the prior fiscal year. Major projects in fiscal year 2012 include significant progress on construction of the Battle Building, completion of the 72-bed expansion, relocation of the heli-pad to the roof of the Hospital, and renovation of multiple patient care units in the Hospital.

Components of the Medical Center's capital assets are shown below:



*in millions

Total liabilities increased $106.4 million. During fiscal year 2012, the Medical Center acquired debt for the Battle Building, $106.0 million.

Statement of Revenues, Expenses and Changes in Net Assets

Changes in total net assets as presented in the Statements of Net Assets are based on activity shown in the Statements of Revenues, Expenses, and Changes in Net Assets. The purpose of these statements is to present the Medical Center's operating and non-operating revenues and expenses and any other revenues, expenses, gains, and losses. A summarized comparison of revenues, expenses and other changes in net assets for the years ended June 30, 2012 and 2011 is as follows:

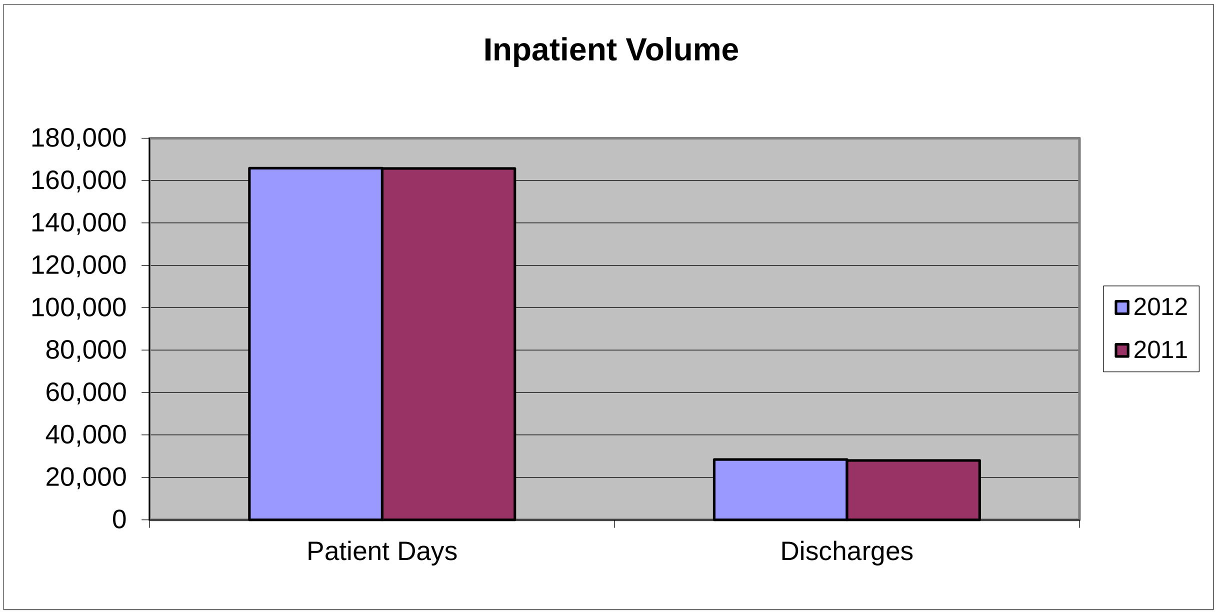
Statement of Revenues, Expenses and Changes in Net Assets
For the years ended June 30, 2012 and 2011

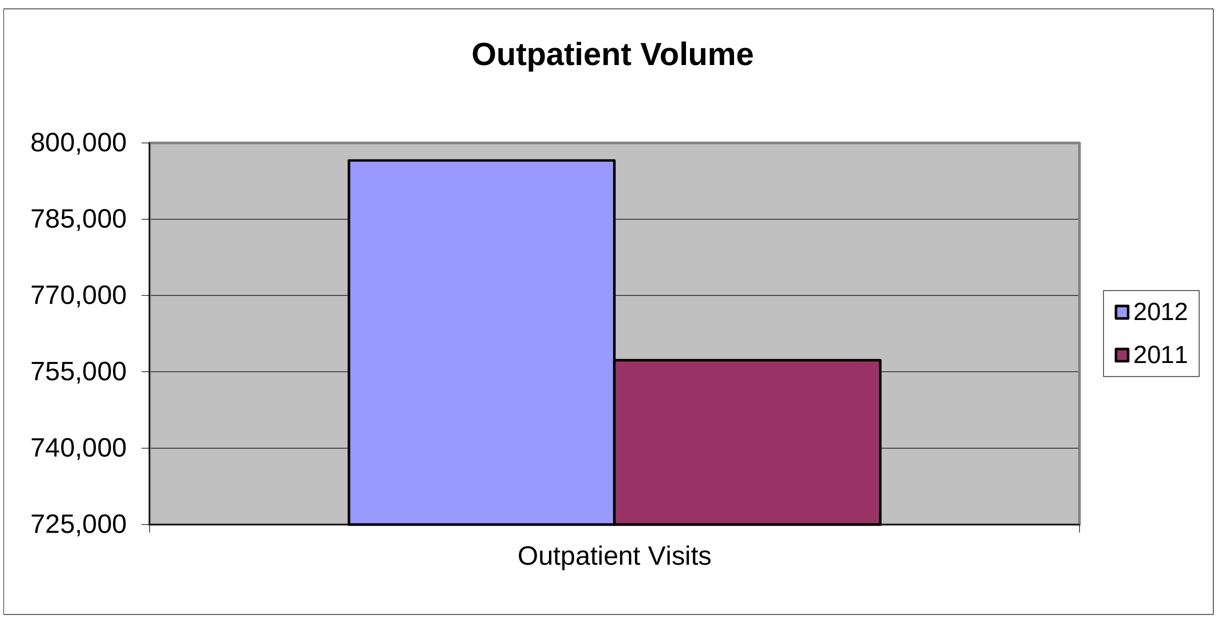
	2012	2011	Increase(Decrease) Amount	Percent
Net patient service revenue	$1,146.8	$1,042.1	$104.7	10.0%
University allocations	24.9	23.3	1.6	6.9%
Other	43.8	29.8	14.0	47.0%
Total operating revenue	1,215.5	1,095.2	120.3	11.0%
Salaries and Benefits	472.6	432.2	40.4	9.3%
Other operating expenses	658.1	567.4	90.7	16.0%
Total operating expenses	1,130.7	999.6	131.1	13.1%
Operating income	84.8	95.6	(10.8)	(11.3)%
Non-operating revenue	0.8	64.6	(63.8)	(98.8)%
Capital Appropriations	-	-	-	
Income before other revenue and transfers	85.6	160.2	(74.6)	(46.6)%
Transfers to UVA/Commonwealth	-	1.3	(1.3)	(100.0)%
Increase in net assets	85.6	161.5	(75.9)	(47.0)%
Net assets-beginning of year	1,114.1	952.6	161.5	17.0%
Net assets-end of year	$1,199.7	$1,114.1	$ 85.6	7.7%

*millions

Operating Revenue

Net patient service revenue for fiscal year 2012 was 10.0 percent above prior year. Net patient service revenue increased as a result of an overall increase in discharges of 2.5 percent and an overall increase of 8.1 percent in outpatient visit volume during the current fiscal year. Besides the factors discussed previously, the increase of the case mix index and negotiated rate increases with managed care payers contributed to the growth in net patient service revenue. A significant factor to the growth was the growth of outpatient cancer services through the acquisition of the HOPE physician group at the beginning of Fiscal Year 2012.

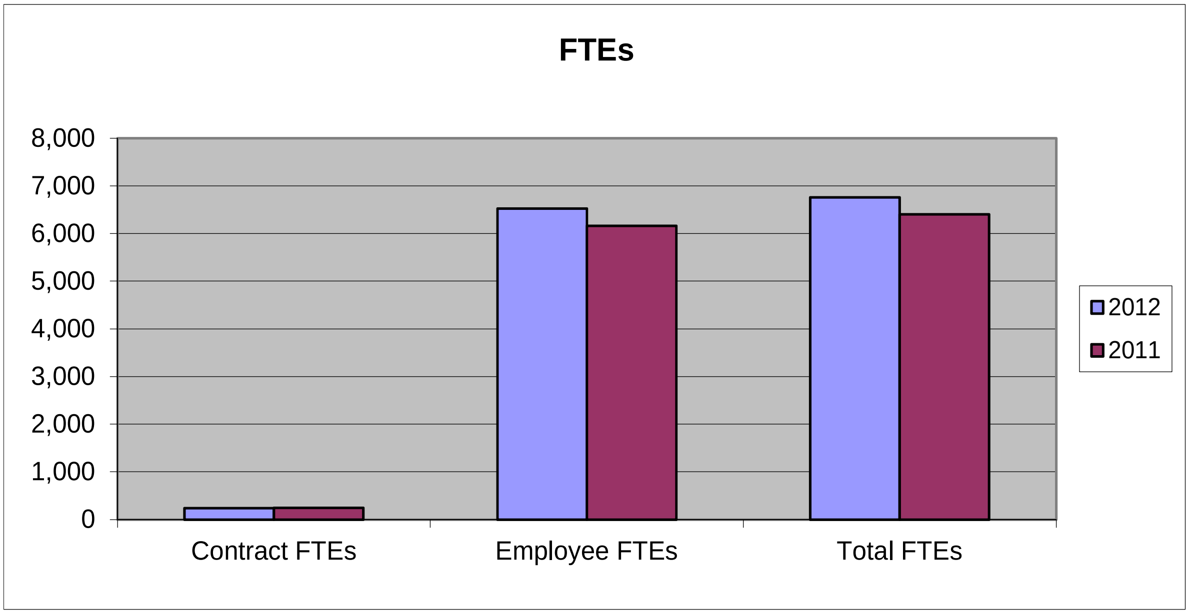


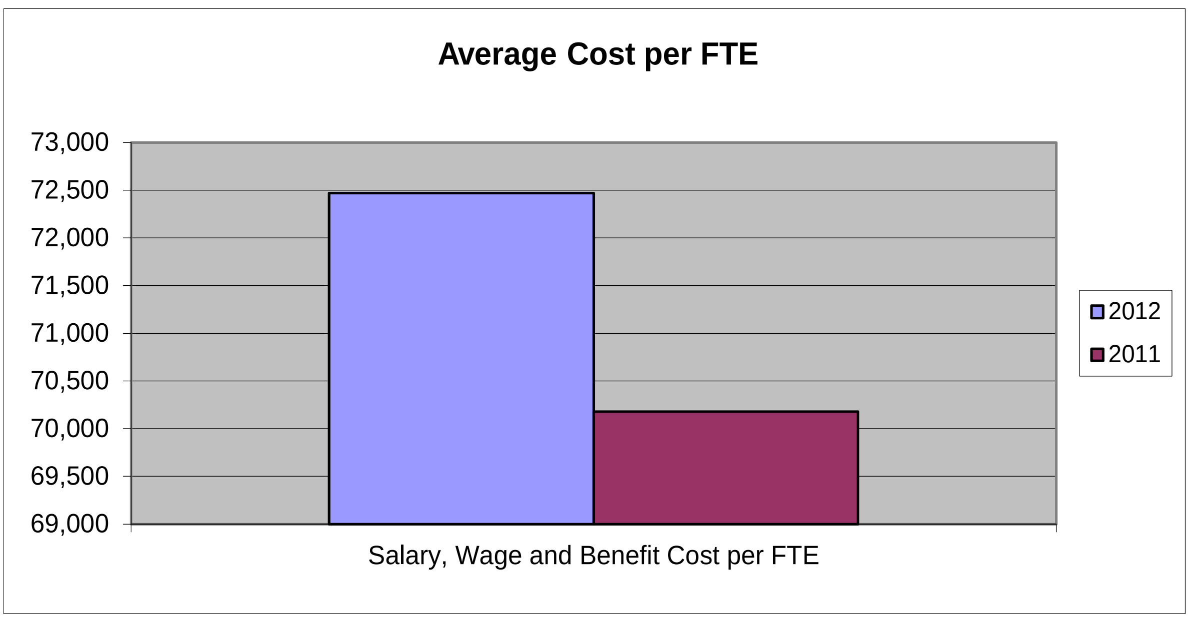


Operating Expenses

Total operating expenses for fiscal year 2012 were 13.1 percent above the prior year. Total labor expenses (including salaries and wages, fringe benefits and contract labor) grew 8.2 percent from the prior year, due to market adjustments, volume growth, first full year of operations for the Transitional Care Hospital, and the acquisition of a large physician oncology group. Employee FTEs increased compared to fiscal year 2011, from 6,159 to 6,521. Conversely, contract labor FTEs decreased from 243 to 236 during fiscal year 2012. Total FTEs increased from 6,402 in fiscal 2011, to 6,757 in fiscal 2012, as a result of increased volume. The average salary, wage and benefit cost per FTE increased from $70,178 in the prior fiscal year, to $72,471 in fiscal year 2012, a 3.3 percent increase.

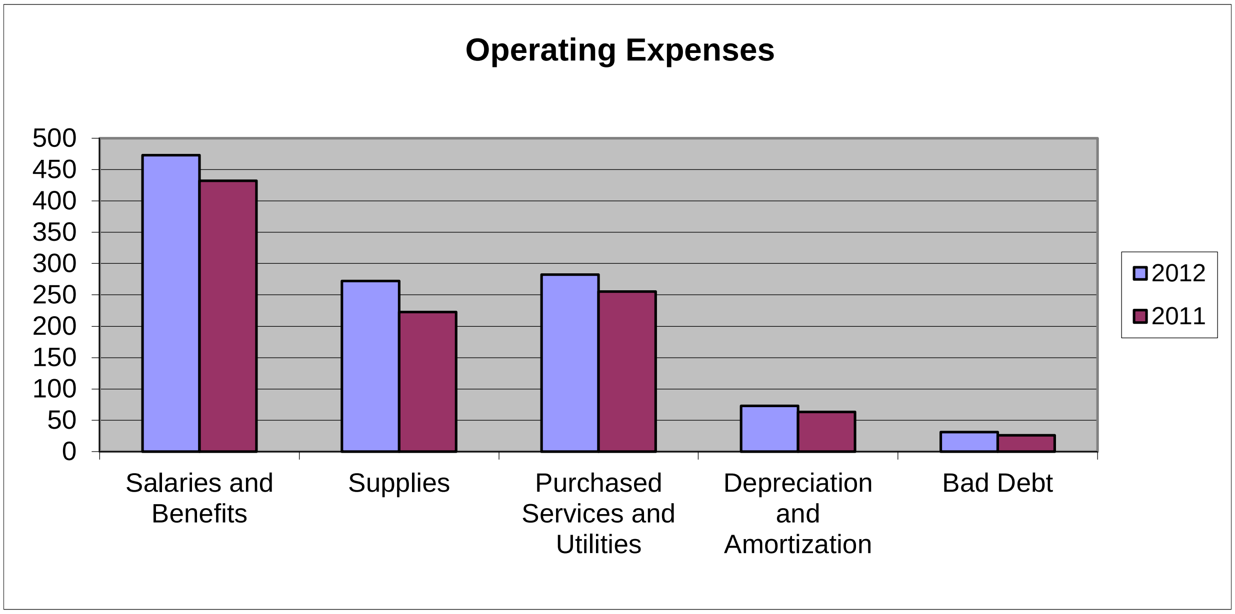
Total paid employees, including contracted employees, are summarized below:





Other operating expenses rose 16 percent from the prior year, primarily due to an increase in purchased services, pharmaceuticals, medical supplies, depreciation and utilities. In addition, overall inflation contributed to the increase in other operating expense. The increase in pharmaceutical expense was due to the growth of outpatient cancer services through the acquisition of the HOPE physician group at the beginning of Fiscal Year 2012. The growth in expenses was offset by revenues.

It has been widely reported that due to the current high unemployment rates indigent care has been increasing across the nation. For fiscal year 2012, indigent care has totaled $207.5 million, which is 6.5 percent of gross revenue. Unlike most other hospitals, the Medical Center receives cost-based payments from a combination of State and Federal dollars to pay the Medical Center and its Faculty. However, the trend in indigent care and issues with the State budget and healthcare reform are reasons for concern as we look to future years.



* in millions

Statement of Cash Flows

The Statement of Cash Flows provides additional information about the Medical Center's financial results by reporting the major sources and uses of cash. A comparative summary of the statement of cash flows for the years ended June 30, 2012 and 2011 is as follows:

Statements of Cash Flows For the years ended June 30, 2012 and 2011			Increase(Decrease)	
	2012	2011	Amount	Percent
Cash flows from operating activities	$102.6	$139.7	-$37.1	-26.6%
Cash flows from non-capital financing activities	4.4	14.1	-9.7	68.8%
Cash flows from capital and related financing activities	(61.1)	(201.5)	140.4	-69.7%
Cash flows from investing activities	(52.6)	34.8	(87.4)	251.3%
Net increase(decrease) in cash and cash equivalents	(6.7)	(12.9)	6.2	-47.8%
Cash and cash equivalents-beginning of the year	155.2	168.1	(13.0)	-7.7%
Cash and cash equivalents-end of the year	$148.4	$155.2	(6.7)	-4.3%
*-millions				

The cash generated from operating activities decreased by 26.6 percent from fiscal year 2011 to fiscal year 2012 because of changes in patient accounts receivable, settlements from governmental third parties, and working capital needs.

Cash flows from non-capital financing activities decreased $9.7 million from fiscal year 2011. During fiscal year 2012, the Medical Center received $10.9 million less gift funds.

Cash flows from capital and related financing activities decreased 69.7 percent or $140.4 million in fiscal 2012. The primary reason for the decrease is the Medical Center spent $47.4 million less for the purchase of capital assets. In addition, the Medical Center acquired 106 million of debt to build the Battle Building.

Cash provided from investing activities decreased $87.4 million from fiscal year 2012 due to lower realized investment income and unrealized changes in the fair market value investments. The change was also impacted by investments in affiliates including the acquisition of physician practices.

Economic Factors Affecting the Future

Since 1996, Medicare has implemented several initiatives to prevent improper payments to health care providers. The latest such initiative is Recovery Audit Contractors. The overall goal is to reduce payments due to billing errors. Recovery Audit Contractors are private companies with whom Medicare has contracted to perform audits. The Recovery Audit Contractor has recently begun work with Virginia providers including the Medical Center. To prepare for the Recovery Audit initiative a multidisciplinary team consisting of Audit, Compliance, Medical Records, Revenue Cycle and Finance leaders in the Medical Center have built tools and workflows to support this process.

The Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 were signed into law in March 2010. The two Acts provide for a number of changes that will affect the health care industry over the next decade. The regulations to implement the Acts are beginning to take effect; however, the substantive portions of the Acts are deferred until 2014. The impact on the Medical Center cannot be known at this time but rather will emerge over the next three years.

Another factor is the ability of Federal legislators to reach agreements on raising the debt ceiling and balancing the Federal Budget. If agreement is not reached, the Medical Center will be subject to “Sequestration” resulting in automatic cuts in payments from Federal sources.

FINANCIAL STATEMENTS

UNIVERSITY OF VIRGINIA MEDICAL CENTER - All Business Units
STATEMENT OF NET ASSETS
As of June 30, 2012
With Comparative Amounts as of June 30, 2011

	2012	2011
A S S E T S		
Current assets:		
Cash and cash equivalents (Note 2)	$107,809,223	$117,339,923
Accounts receivable, net of estimated uncollectibles of $331,186,785 at June 30, 2012 and $267,422,561 at June 30, 2011	206,436,546	142,279,029
Due from University of Virginia	204,074	109,830
Inventories and prepaid expenses	34,125,491	25,051,167
Notes receivable	7,042	8,320
Total current assets	348,582,376	284,788,269
Noncurrent assets:		
Cash and cash equivalents restricted (Note 2)	40,576,818	37,814,352
Due from the University of Virginia - non current	21,658,262	22,725,140
Investments in pooled endowment funds (Note2)	418,193,522	404,834,685
Goodwill (Note 3)	11,445,473	11,938,447
Investments (Note 2)	138,598,332	138,524,567
Investments in affiliated companies (Note 4)	70,030,783	55,785,864
Land (Note 5)	17,392,966	17,392,967
Construction in Progress (Note 5)	173,281,346	143,160,458
Depreciable land improvements, buildings, and equipment, less accumulated depreciation of $607,679,335 at June 30, 2012 and $556,783,693 at June 30, 2011 (Note 5)	541,081,682	506,986,293
Deferred bond discount and issue costs, net of amortization of $232,174 at June 30, 2012	5,759,433	4,011,607
Assets whose use is limited:		
Cash and cash equivalents (Note 6)	-	-
Investments (Note 2)	106,482,768	73,270,113
Total noncurrent assets	1,544,501,385	1,416,444,492
Total assets	$1,893,083,761	$1,701,232,761

The accompanying notes to financial statements are an integral part of this statement.

UNIVERSITY OF VIRGINIA MEDICAL CENTER - All Business Units
STATEMENT OF NET ASSETS
As of June 30, 2012
With Comparative Amounts as of June 30, 2011

	2012	2011
L I A B I L I T I E S A N D N E T A S S E T S		
Current liabilities:		
Accounts payable and accrued expenses (Note 7)	$158,431,865	$129,569,989
Deferred Revenue	16,575,328	16,935,937
Due to third-party payers	14,442,809	8,090,679
Current installments of long-term debt (Note 8)	23,356,566	22,840,591
Grants payable - current portion	8,722,091	6,057,316
Due to Culpeper Regional Hospital-current (Note 8)	38,137,417	30,000,000
Bond premium - current amortization	99,615	109,847
Total current liabilities	259,765,691	213,604,358
Long-term liabilities:		
Long-term debt (Note 8)	426,343,357	341,912,494
Grants payable - noncurrent portion	4,999,999	5,625,001
Other Long-term liabilities	-	17,900,000
Due to Culpeper Regional Hospital-noncurrent	-	7,693,344
Bond Premium ,net of amortization of $99,215 at June 30, 2012	-	99,615
Noncontrolling Interest in Subsidiary	2,328,871	260,300
Total long-term liabilities	433,672,227	373,490,754
Total liabilities	693,437,918	587,095,112
NET ASSETS		
Invested in capital assets, net of related debt	416,112,665	402,643,692
Restricted for:		
Nonexpendable	53,099,192	53,099,192
Expendable	65,631,100	62,868,634
Unrestricted	664,802,886	595,526,131
Total net assets	1,199,645,843	1,114,137,650
Total liabilities and net assets	$1,893,083,761	$1,701,232,761

The accompanying notes to financial statements are an integral part of this statement.

UNIVERSITY OF VIRGINIA MEDICAL CENTER - All Business Units

STATEMENTS OF REVENUES AND EXPENSES AND CHANGES IN NET ASSETS

As of June 30, 2012

With Comparative Amounts as of June 30, 2011

	2012	2011
Operating revenue:		
Net patient service revenue (Note 10)	$1,146,772,903	$1,042,100,331
University allocations (Note 11)	24,917,663	23,316,240
Other	43,789,793	29,751,071
Total operating revenue	1,215,480,359	1,095,167,642
Operating Expenses:		
Salaries and wages	389,019,562	351,766,385
Fringe benefits	83,564,583	80,457,335
Supplies	271,889,199	222,608,003
Purchased services and other expenses	258,843,165	235,020,467
Utilities	23,528,964	20,494,465
Provision for depreciation and amortization	72,937,492	63,428,344
Provision for bad debts	30,942,354	25,837,665
Total operating expenses	1,130,725,319	999,612,663
Income from operations	84,755,040	95,554,979
Nonoperating revenue (expenses):		
Gifts	2,360,231	13,262,360
Investment income	5,407,826	(1,077,465)
Net increase (decrease) in the fair value of investments	13,402,011	80,250,258
Net gain (loss) from investments in affiliated companies (Note 4)	2,828,747	3,177,423
Noncontrolling Interest in Subsidiary Income	(1,612,235)	(1,894,045)
Interest expense	(7,103,475)	(7,724,616)
Loss on disposal of fixed assets	(286,094)	717,386
Gain Sharing School of Medicine (Note 12)	(8,038,526)	(18,044,078)
Other	(6,205,332)	(4,078,405)
Net nonoperating revenues	753,153	64,588,818
Income before other revenues, expenses, gains or losses	85,508,193	160,143,797
Transfers	-	1,338,706
Increase (decrease) in net assets	85,508,193	161,482,503
NET ASSETS		
Net assets - beginning of year	1,114,137,650	952,655,147
Net assets - end of year	$1,199,645,843	$1,114,137,650

The accompanying notes to financial statements are an integral part of this statement.

UNIVERSITY OF VIRGINIA MEDICAL CENTER - All Business Units

STATEMENT OF CASH FLOWS

As of June 30 2012

With Comparative Amounts as of June 30 2011	2012	2011
Cash flows from operating activities:		
Receipts from patients and third-parties	$1,092,603,350	$999,329,325
Receipts from other revenue	33,545,808	25,050,190
Payments to employees	(474,727,381)	(440,688,665)
Payments to suppliers	(525,313,541)	(423,560,434)
Payment for utilities	(23,528,964)	(20,455,071)
Net cash provided by operating activities	102,579,272	139,675,344
Cash flows from non-capital financing activities:		
Payments on grants	2,039,773	847,089
Gifts	2,360,231	13,262,360
Net cash provided (used) by non-capital financing activities	4,400,004	14,109,449
Cash flows from capital and related financing activities:		
State appropriation for construction		
Purchase of capital assets	(136,422,943)	(183,852,809)
Principal paid on capital debt	(22,237,242)	(18,638,680)
Principal paid on capital leases	(616,881)	-
Interest paid on capital debt	(7,294,746)	(7,764,684)
Proceeds from incurring loan from the University	103,271,216	8,446,435
Proceeds (increase) to capital leases	1,600,000	-
Proceeds from sale of capital assets	586,595	281,151
Net cash used by capital and related financing activities	(61,114,001)	(201,528,587)
Cash flows from investing activities:		
Interest on investments	7,877,235	7,941,491
Purchase of investments	(33,212,655)	41,910,266
Transfer to endowment	(2,500,000)	-
Other	(13,838,249)	(11,877,796)
Transfer to affiliate	501,828	(1,777,467)
Payment affiliate	(11,461,667)	(1,413,454)
Net cash provided by investing activities	(52,633,508)	34,783,040
Net increase in cash and cash equivalents	(6,768,233)	(12,960,754)
Cash and cash equivalents - beginning of the year	155,154,274	168,115,027
Cash and cash equivalents - end of the year	$ 148,386,041	$ 155,154,274
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	84,755,040	95,554,979
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	72,937,492	63,428,344
Change in assets and liabilities		
Accounts receivables	(56,697,465)	(40,152,648)
Inventories and prepaid expenses	(9,208,333)	2,064,270
Accounts payable and accrued expenses	10,792,538	18,780,399
Net cash provided by operating activities	$ 102,579,272	$ 139,675,344

The accompanying notes to financial statements are an integral part of this statement.

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Mission

The Medical Center is a division of the University of Virginia. The Medical Center's mission is to provide excellence, innovation, and superlative quality in the care of patients, the training of health professionals, and the creation and sharing of health knowledge within a culture that promotes equity, diversity and inclusiveness. Only those activities directly associated with the furtherance of this mission are considered to be operating activities. Other activities that result in gains or losses unrelated to the Medical Center's primary mission are considered to be non-operating.

A separate report is prepared for the Commonwealth that includes all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority. The University is a component unit of the Commonwealth and is included in the basic financial statements of the Commonwealth.

B. Basis of Accounting

The Medical Center has adopted the accrual basis of accounting in accordance with Generally Accepted Accounting Principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB) and the Financial Accounting Standards Board (FASB) for providers of healthcare services.

Pursuant to GASB Statement 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Medical Center has elected to apply the provisions of all relevant pronouncements of FASB, including those issued after November 30, 1989.

The financial statements have been prepared in accordance with GASB Statement 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis of Public College and Universities.*

C. Use of Estimates

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

D. Subsidiary and Affiliated Companies

The consolidated financial statements include the accounts of controlled subsidiary companies where ownership is greater than 50 percent. Investments in affiliates in which the Medical Center has a substantial interest (approximately 20 to 50 percent) or for which the Medical Center exercises significant influence, but not control, over policy decisions are accounted for by the equity method.

E. Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered. Net patient service revenue also includes funds from the Commonwealth's Department of Medical Assistance Services for disproportionate share and indirect medical education payments and funds from third-party payers for estimated retroactive adjustments under reimbursement agreements. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

F. Indigent Care

The Medical Center accepts all patients regardless of their ability to pay. A patient is classified as indigent by reference to established Commonwealth policies. The criteria for identifying indigent patients are based on asset and income guidelines that are updated annually in accordance with the federal poverty income guidelines as provided by the federal Office of Management and Budget. Because the Medical Center does not pursue collection of amounts determined to qualify as indigent care, they are not reported as revenue.

G. Receivables From Third Parties and Contractual Adjustments

A significant portion of the Medical Center's services is rendered to patients covered by Medicare, Medicaid, or other third-party payers. The Medical Center entered into contractual agreements with these third parties to accept payment for services in amounts less than scheduled charges.

Certain annual settlements of amounts due for patient services covered by third parties are determined through cost reports that are subject to audit and retroactive adjustment by the third parties. Provisions for possible adjustments of cost reports have been estimated and reflected in the accompanying financial statements. Since the determination of cost reimbursement settlements of amounts earned in prior years has been based on reasonable estimation, the difference in any year between the originally estimated amount and the final determination is reported in the year of determination.

H. Cash, Cash Equivalents, and Investments

Cash and cash equivalents include cash and all highly liquid investments with maturity of three months or less when purchased.

Donated investments are reported at the fair market value at the date of receipt. The major portion of the investments of the Medical Center's endowment funds is pooled under the University of Virginia Growth and Income Fund, the general endowment pool for the University. Annually, endowment earnings on the consolidated endowment pool are distributed to the participating funds based on the participating share of each fund in the pool.

Investments are carried at fair value as determined by quoted market prices. Unrealized appreciation or depreciation of investments is included in the current period net of earnings. All investment income, including changes in the fair value of investments (unrealized gains and losses), is reported as non-operating revenue in the Statement of Revenues, Expenses, and Changes in Net Assets.

I. Inventories

Inventories are valued at the lower of cost, generally determined on the weighted average method, or market and consist primarily of expendable supplies held for consumption.

J. Property, Plant, and Equipment

Property, plant, and equipment are stated at cost, or if donated, at fair market value at the date of donation. The Medical Center capitalizes expenditures for equipment costing $2,000 or more and having a useful life of two years or greater in accordance with the *Medicare Reimbursement Manual*.

Depreciation on property, plant, and equipment, excluding land and construction-in-progress, is computed over the estimated useful lives of the assets using the straight-line method. The general range of estimated useful lives is 10 to 40 years for buildings and fixtures and 3 to 20 years for equipment.

The Medical Center utilizes the half-year convention for recognizing depreciation expense related to equipment, both fixed and moveable. A half-year of depreciation is recognized on all equipment in the fiscal year of acquisition. Likewise, a half-year of depreciation is recognized in the fiscal year at the end of the equipment's useful life. Depreciation on buildings is recognized from the date that the asset is placed in service to the date on which it is retired.

K. Deferred Bond Issue Costs

Deferred bond issue costs are amortized over the remaining life of the bonds.

L. Accrued Leave

The amount of leave earned, but not taken by salaried employees is recorded as a liability on the Statement of Net Assets. The amount reflects, as of June 30, all earned leave not taken and the amount payable under the catastrophic leave pay-out policy upon termination, which is the lesser of 25 percent of sick leave not taken or $5,000 per employee with five or more years of service. The liability is based on the probability that an employee with less than five years of service will eventually become vested and has a right to receive payment for sick leave benefits. The applicable share of employer-related taxes payable on the eventual termination payments is also included.

M. Comparative Data

The Medical Center presents its financial information on a comparative basis. The basic financial statements include certain prior year summarized comparative information, in total, but not at the level of detail required for a presentation in conformity with generally accepted accounting principles. Accordingly, the prior year information should be read in conjunction with the Medical Center's financial statements for the year ended June 30, 2011, from which the summarized information is derived.

N. Reclassifications

Certain amounts from prior year financial statements needed to be reclassified to conform to current year presentation.

2. CREDIT RISK UNDERLYING CASH, CASH EQUIVALENTS AND INVESTMENTS

Cash, Cash Equivalents and Investments:

The following risk disclosures are required by GASB Statement Number 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreement), and Reverse Repurchase Agreements* as amended by GASB Statement 40, *Deposit and Investment Risk Disclosures*:

Custodial Credit Risk (Category 3 deposits and investments) - The custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The Medical Center has no category 3 deposits or investments for 2012.

Credit risk - The risk that an issuer or other counterparty to an investment will not fulfill its obligations. GASB Statement 40 requires the disclosure of the credit quality rating on any investments subject to credit risk. The Medical Center does not have any credit risk.

Concentration of credit risk - The risk of loss attributed to the magnitude of a governments investment in a single issuer. GASB Statement 40 requires disclosure of any issuer with more than five percent of the Medical Center investments are in the University of Virginia Growth and Income Fund. The Medical Center investments are 100 percent invested in the University of Virginia Growth and Income Fund.

Interest rate risk - The risk that changes in interest rates will adversely affect the fair value of an investment. GASB Statement 40 requires disclosure of maturities for any investments subject to interest rate risk. The Medical Center does not have an interest rate risk policy.

Foreign currency risk - The risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The Medical Center has no foreign investments or deposits for 2012.

The following information is provided with respect to the risks associated with the Medical Center's cash, cash equivalents, and investments at June 30, 2012.

Cash and Cash Equivalents

Pursuant to Section 2.2-1800, et seq., Code of Virginia, all state funds of the Medical Center are maintained by the Treasurer of Virginia who is responsible for the collection, disbursement, custody, and investment of state funds. Cash deposits held by the Medical Center are maintained in accounts collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400, et seq., Code of Virginia. The Virginia Security for Public Deposits Act eliminates any custodial credit risk for Medical Center's deposits. Cash and Cash Equivalents represent cash with the treasurer, cash on hand, certificates of deposit, and temporary investments with original maturities of 90 days or less, and cash equivalents with the Virginia State Non-Arbitrage Program (SNAP). SNAP is an open-end management investment company registered with the Securities and Exchange Commission (SEC). Cash and Cash Equivalents reporting requirements are defined by GASB Statement 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting*.

Additional disclosures required for cash equivalents under GASB Statement Number 40 are presented with the investments in the following tables.

Investments

The investment policy of the Medical Center is established by the Board of Visitors and monitored by the Board's Finance and Audit Committee. Authorized investments are set forth in the "Investment of Public Funds Act", Sections 2.2-4500 through 2.2-4516, Code of Virginia. Authorized investments include U.S. Treasury and agency securities; corporate debt securities of domestic corporations, asset-backed securities, mortgage-backed securities, AAA rated obligations of foreign governments, bankers' acceptances and bank notes, negotiable certificates of deposit, repurchase agreements, and money market funds.

Investments fall into two groups: short and long-term. Short-term investments have an original maturity of over 90 days but less than or equal to one year. Long-term investments have an original maturity greater than one year.

Credit and Concentration of Credit Risks

Type of Investment	Fair Value	Credit Rating	Concentration Risk
CASH EQUIVALENTS:			
Total Cash Equivalents	-		
INVESTMENTS:			
University of Virginia Long Term Pool	418,193,522		100%
Total Investments	418,193,522		
Total Cash Equivalents and Investments	418,193,522		

Interest Rate Risk – Maturities

Type of Investment	<1 year	1-5 years	6-10 years	Total
University of Virginia Long Term Pool	418,193,522			418,193,522
Total Investments	418,193,522	0.00		418,193,522

3. GOODWILL

In July 2004, the Medical Center purchased Virginia Ambulatory Surgery Center, (VASI), now known as the University of Virginia Outpatient Surgery Center. As a result of the purchase, the Medical Center recorded $6,980,198 of goodwill to be amortized over a period of 40 years.

In November 2004, the Medical Center purchased Amherst and Lynchburg renal facilities. As a result of the purchase, the Medical Center recorded goodwill of $3,476,068 and $4,017,321, respectively, for the Amherst and Lynchburg facilities. The goodwill is to be amortized over a period of 20 years.

4. AFFILIATED COMPANIES

Culpeper Regional Hospital

On December 31, 2008, the University of Virginia Medical Center and Culpeper Regional Hospital entered into a partnership agreement, whereby the Medical Center obtained a 49 percent interest in Culpeper Regional Hospital, with a $41.2M investment. The Medical Center uses the equity method of consolidation in order to reflect the Medical Center's investment in Culpeper Regional Hospital.

University of Virginia Imaging, LLC

On March 26, 2002, the Medical Center entered into an agreement with Outpatient Imaging Affiliates of Virginia, LLC to establish University of Virginia Imaging, LLC (UVI). The limited liability corporation was formed to operate an outpatient diagnostic imaging center to help respond to the need for radiology services in the Charlottesville area.

The Medical Center currently operates an outpatient imaging department offering MRI, plain film radiography, fluoroscopy, and ultrasound in office space at the Fontaine Research Park and at the Transitional Care Hospital. UVI provides services to outpatients from the Medical Center's primary and secondary service areas.

Since the Medical Center owns 80 percent of UVI, its financial activity is presented under the consolidation method.

Community Medicine, LLC

On November 14, 2000, the University established the Community Medicine University of Virginia, LLC (Community Medicine). Community Medicine was established as a limited liability corporation (LLC) under the laws of the Commonwealth to house physician practices. This model gives physicians an organizational structure that allows them the opportunity to practice independently in a virtual private practice environment with all the risks and gains associated with an independent model. As an LLC, which is a wholly owned subsidiary of the University, Community Medicine is considered a disregarded entity for tax purposes and its financial activity is accounted for under the consolidation method.

Community Medicine commenced operations on July 1, 2001 and the Medical Center's investment totaled $1,810,000.

Central Virginia Health Network, Inc.

In May 1995, the Medical Center joined the Central Virginia Health Network, Inc. (CVHN), a partnership of eight Richmond area hospitals. CVHN was formed to provide an efficient and coordinated continuum of care, with services ranging from acute hospital treatment to primary physician care and home health services.

The Medical Center originally paid $100 for 10,000 shares of common stock and $109,900 as additional paid-in capital. In addition, the Medical Center is obligated for monthly dues to CVHN of $15,913. Complete financial statements can be obtained from the registered agent: Steven D. Gravely, Esq., Mezzullo and McCandlish, Post Office Box 796, Richmond, Virginia 23206.

University of Virginia / HEALTHSOUTH, LLC

The Medical Center entered into a joint venture with HEALTHSOUTH Corporation to establish an acute rehabilitation facility located at the Fontaine Research Park to provide patient services to the region. The Medical Center made a capital contribution of $2,230,000 to the joint venture in May 1996, which represents a 50 percent interest. Complete financial statements can be obtained from the managing member: HEALTHSOUTH Corporation, 7700 East Parham Road, Richmond, Virginia 23294.

Valiance Health, LLC

In November 1997, the Medical Center became a participant with Rockingham Memorial Hospital and Augusta Health Care, Inc., in Valiance Health, LLC (Valiance), a joint venture integrating and coordinating the delivery of healthcare services in central and western Virginia. The Medical Center contributed $100,000 in initial capital, which entitles it to a pro-rata distribution of any profits and losses of Valiance. In October 2003, the Medical Center contributed an additional $400,000 in capital to Valiance, bringing the Medical Center's total investment to $500,000.

University Health System Consortium (UHC)

In December 1986, the Medical Center became a member of the University Health System Consortium (UHC). Founded in 1984, UHC is an alliance of the clinical enterprises of academic health centers. While focusing on the clinical mission, UHC is mindful of and supports the research and education missions. The mission of the UHC is to advance knowledge, foster collaboration, and promote change to help members compete in their respective healthcare markets. In keeping with this mission, UHC helps members pool resources, create economies of scale, improve clinical and operating efficiencies, and influence the direction and delivery of healthcare. Accordingly, UHC is organized and operated on a cooperative basis for the benefit of its member health systems as patrons.

UHC is a not-for-profit organization. It is incorporated as a nonstock corporation and designated as a nonexempt cooperative, which is taxable under Subchapter T, section 1382-1388, of the Internal Revenue Code. As such, UHC's bylaws provide for distributions of patronage dividends to its patrons. This allocation is based on the value of business done with or for each patron by UHC. The Medical Center records the portion of the patronage dividends that were held by UHC as patronage equity.

Hematology Oncology Patient Enterprises, Inc.

The Medical Center purchased Hematology Oncology Patient Enterprises, Inc. (HOPE) on July 15, 2012 for $15,000,000. HOPE is wholly owned by the Medical Center, and is comprised of the following clinics: Pantops, Farmville, Culpeper, and Augusta. The purchase was the cornerstone of forming UVA HOPE Cancer Care, which is a network of doctors and nurses who deliver high quality cancer treatment throughout the region. The physicians at HOPE explore all treatment with a patient focused approach using the latest medical, surgical, and radiological therapies along with support therapies, massage, nutrition, mind and body medicine, naturopathy and spiritual wellness.

PACE

In March 2012, the Medical Center contributed $245,000 for a 24.5 percent investment in Charlottesville PACE (Program of All Inclusive Care for the Elderly). The Charlottesville PACE financial transactions will be recorded using the equity method of accounting. The program delivers various medical and support services to senior residents in Charlottesville and surrounding counties. Patients in the program have an alternative to residential nursing home care providing daily access to doctors and physical therapists, home health care, and personal care.

As of June 30, 2012

	Common Stock and Equity Contribution	Share of accumulated income (loss)	Net investment
UVA Imaging, LLC	687,019	7,124,591	7,811,610
Community Medicine, LLC	1,810,000	(5,156,929)	(3,346,929)
Central Virginia Health Network, Inc.	232,500	(41,026)	191,474
Healthsouth, LLC	-	9,870,818	9,870,818
Valiance, LLC	-	1,694,631	1,694,631
University Health System Consortium	-	551,839	551,839
Culpeper Regional Hospital	41,248,100	5,013,046	46,261,146
PACE Equity	245,000	-	245,000
HOPE Equity	11,216,667	-	11,216,667

HealthCare Partners, Inc.

In May 1995, HealthCare Partners, Inc., a non-stock, non-profit corporation, was established to support networking, external business relationships with neighboring hospitals and physicians groups, and expansion of primary care activities. The Medical Center and the University Physicians' Group are the primary contributors to the funding of the corporation. Healthcare Partners, Inc. is governed by a board of directors composed of the following members: Medical Center Operating Board Chairman, the Chief Executive Officer and Chief Financial Officer of the Medical Center, University Physicians Group representatives, community members, and President appointees.

5. PROPERTY, PLANT, AND EQUIPMENT

A summary of the property, plant, and equipment accounts and the related accumulated depreciation as of June 30, 2012, is presented as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Land	17,392,966	-	-	17,392,966
Construction in Progress	143,160,458	100,229,892	70,109,005	173,281,345
Depreciable Capital Assets				
Land improvements	8,935,476	224,986		9,160,462
Buildings	680,487,221	62,509,584	5,946,153	737,050,652
Equipment-Fixed	22,160,476	183,385	63,918	22,279,943
Equipment-Movable	304,891,421	44,264,110	11,161,259	337,994,272
Total depreciable capital assets	1,016,474,604	107,182,066	17,171,330	1,106,485,340
Less accumulated depreciation				
Land improvements	7,486,903	199,069	-	7,685,972
Buildings	316,022,960	29,927,337	820,978	345,129,320
Equipment-fixed	17,378,390	605,503	57,549	17,926,344
Equipment-movable	215,895,440	28,708,771	7,666,514	236,937,698
Total accumulated depreciation	556,783,694	59,440,681	8,545,040	607,679,335
Depreciable land improvements, buildings and equipment, net	459,690,911	47,741,385	8,626,290	498,806,006
Depreciable Intangible Assets	88,451,254	5,093,263	16,500	93,528,016
Less accumulated amortization: Intangible Assets	41,155,871	10,112,958	16,500	51,252,329
Depreciable intangible assets	47,295,382	(5,019,696)	-	42,275,686
Total depreciable capital and intangible assets(net)	$506,986,293	$ 42,721,689	$ 8,626,290	$541,081,692

6. ASSETS HELD BY TRUSTEES

Assets held by trustees consist of assets whose use is limited under indenture agreements. The Series 1998B, 1999A, 2003A, 2003B, 2006, 2008, 2009, 2010, 2011 and 2012 bond resolutions require deposits be made in a specific order to various accounts and funds held by the University of Virginia Internal Loan Program as follows:

A. to the credit of the Interest Account on a monthly basis, the amount of interest due and payable on the first day of the succeeding month with respect to the bonds of each series then outstanding;

B. to the credit of the Principal Account on a monthly basis, the amount sufficient to pay maturing principal of all bonds on the next principal payment date;

C. to the credit of the Sinking Fund Account, the amount sufficient to retire all bonds to be called by mandatory redemption on the next ensuing mandatory redemption date;

D. to the credit of any other fund or account created pursuant to an applicable Series Resolution.

Funds held by the Treasurer and restricted by bond agreements consist of the following as of June 30, 2012:

Bond Sinking Fund-2008	2,516,117
Bond Sinking Fund-2009A	9,244,412
Bond Sinking Fund-2009B	496,908
Bond Sinking Fund-2009C	1,218,517
Bond Sinking Fund-2009D	1,213,017
Bond Sinking Fund-2010A	2,466,527
Bond Sinking Fund-2010B	7,456,981
Bond Sinking Fund-2010C	4,126,401
Bond Sinking Fund-2010D	2,500,000
Bond Sinking Fund-2010E	174,075
Bond Sinking Fund-2011A	2,087,500
Bond Sinking Fund-2012A	72,982,313

*The Medical Center also participates in the Commonwealth's Public Higher Education Financing Program, Series 1999A ("Pooled Bond Program"). The indenture of the series specifies the Bank of New York as trustee and the Medical Center is required to make debt service payments to the trustee in the amount billed by the trustee semi-annually.

7. ACCOUNTS PAYABLE

As of June 30, 2012, the components of accounts payable and accrued expenses consist of the following:

Vendor Accounts Payable	$ 24,229,283
Due to the University	16,710,708
Accrued Leave	30,540,697
Accrued Allotments	25,493,479
Other Accounts Payable	14,552,685
Accrued Payroll	7,492,485
Due to Employees-FICA	17,653,921
Other Accrued Expenses	21,758,607
	$158,431,865

8. LONG-TERM DEBT

*In thousands

Description	Interest Rate	Maturity	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Bonds Payable:							
Series 1998B Refinance	4.5-6.00	2018	3,054	-	376	2,678	395
Series 1999A	4.5-5.25	2013	13,021	-	6391	6,630	6630
Series 1999A Pooled	4.5-5.25	2019	-	-	-	-	-
Series 1999A Pooled Refinance	4.5-5.25	2019	2,655	-	240	2,415	255
Series 2003A Pooled	4.5-6.00	2015	17,315	-	220	17,095	245
Series 2003B Pooled	4.7-6.00	2023	25,563	-	1592	23,971	1671
UVA Pooled Debt	4.7-6.00	2024	12,207	-	880	11,327	736
Series 2006 Pooled	4.5-6.00	2027	31,924	-	1385	30,539	1451
Series 2007 Pooled	4.5-6.00	2014	5,640	-	1881	3,759	1,971
Series 2008 Pooled	4.5-6.00	2028	78,358	-	2719	75,639	3,259
Series 2009 Pooled (1)	4.75	2029	3,458	-	132	3,326	138
Series 2009 Pooled (2)	4.75	2029	2,441	-	674	1,767	707
Series 2009 Pooled (3)	4.75	2029	3,889	-	142	3,747	149
Series 2009 Pooled (4)	4.75	2029	21,930	-	859	21,071	901
Series 2009 Pooled (5)	4.75	2029	14,846	-	582	14,264	610
Series 2009 Pooled (6)	4.75	2029	14,796	-	529	14,267	555
Series 2010 Pooled (1)	4.75	2030	6,763	-	244	6,519	256
Series 2010 Pooled (2)	4.75	2030	25,996	-	704	25,292	1,098
Series 2010 Pooled (3)	4.75	2030	4,094	-	164	3,930	172
Series 2010 Pooled (4)	4.75	2030	8,253	-	204	8,049	318
Series 2010 Pooled (5)	4.75	2030	5,006	-	184	4,822	193
Series 2010 Pooled (6)	4.75	2030	20,404	-	692	19,712	725
Series 2010 Pooled (7)	4.75	2030	5,496	-	184	5,312	193
Series 2011 Pooled	4.75	2031	7,007	-	19	6,988	238
Series 2012 Pooled	4.75	2032	-	106,244	-	106,244	-
Total bonds payable			334,116	106,244	20,997	419,363	22,866
Notes Payable:							
UVA Imaging			3,950	35	1,321	2,664	491
Total Notes Payable			3,950	35	1,321	2,664	491
Capitalized Leases:							
Kirtley			7,121	-	223	6,898	219
Transitional Care Hospital			19,569	1,600	394	20,775	397
Total Capitalized Leases:			26,690	1,600	617	27,673	616
Total Long-term debt			364,756	107,879	22,935	449,700	23,973

Future Debt Requirements

Fiscal Year	Principal	Interest	Total
2013	$ 23,973,015	$ 15,705,861	$ 39,678,876
2014	29,483,785	16,654,934	46,138,719
2015	28,283,680	18,248,278	46,531,958
2016	20,243,537	16,924,946	37,168,483
2017	21,206,461	15,971,560	37,178,021
2018-2022	119,141,318	64,132,126	183,273,444
2023-2027	131,318,317	34,573,831	165,892,148
2028-2032	64,307,808	9,068,677	73,376,485
2033-2037	5,692,699	3,251,687	8,944,386
2038-2042	4,274,161	2,648,823	6,922,984
2043-2047	622,393	2,923,010	3,545,403
2048	1,152,754	5,062,460	6,215,214
	$449,699,928	$205,166,193	$654,866,121

9. FINANCING OF MAJOR CONSTRUCTION AND RENOVATION PROJECTS

The Clinical Office Building at Fontaine Research Park was purchased in April 2004. The Medical Center borrowed $17.6 million from the University's Pooled Bond Program to buy the building and complete its construction. In 2009, the University, through its Pooled Debt Loan Program, issued $4,078,517 to complete construction and fit-out of the 3rd floor of the Fontaine building. The purpose of this building is to expand the outpatient clinic services for the Medical Center.

The Medical Center began the Hospital Bed Expansion Project in fiscal year 2008. The Medical Center will add 72 beds over a period of three years. The expected cost of the project is $80.2 million funded using bonds issued under the University of Virginia Pooled Debt Program in May 2008. The Bed Expansion will include 6 12-bed units on floors 3 through 8 of the Hospital. The expected completion is fiscal year 2013. As part of the Bed Expansion Project, the Elevator Banks and Fire Alarm system are to be updated at an expected cost of $8.2 million, using bonds issued under the University of Virginia Pooled Debt program.

During fiscal year 2011, the Medical Center began construction of the new Helipad on the roof of the Medical Center. The projected cost of the Helipad project is $6.8 million funded through the University of Virginia Pooled Debt Program. The expected completion date is 2012.

At the end of fiscal year 2011, the Medical Center broke ground for the Battle Building. Once completed, the Battle Building will contain the University of Virginia Children's Hospital and replace the current University of Virginia Outpatient Surgery Center. During fiscal year 2012, $99 million debt was issued through the Pooled Debt Loan Program. The project is expected to cost $141 million with expected completion in fiscal year 2014.

10. NET PATIENT SERVICE REVENUE

The Medical Center's patient service revenue is as follows for the year ended June 30, 2012:

Gross Patient Service Revenue:	
Inpatient	
Routine	$ 386,277,731
Ancillary	1,357,689,371
Outpatient Services	
Ancillary	1,463,444,586
Clinics	5,643,203
Total Gross Patient Revenue	3,213,054,891
Allowances for indigent care and contractual adjustments	(2,066,281,988)
Net Patient Service Revenue	$1,146,772,903

The Medical Center received $73,899,067 in fiscal year 2012 from the Commonwealth's Department of Medical Assistance Services. These payments are included in net patient service revenue as an adjustment to allowances for indigent care and contractual adjustments.

Of the payment received for disproportionate share, relating to the care provided to indigent patients, $21,500,00 was transferred to Health Services Foundation (currently known as the University Physicians Group) for related physician services and is included in the purchased services expense.

11. UNIVERSITY ALLOCATIONS

The School of Medicine faculty assists the Medical Center in its mission of providing healthcare and medical education. A survey is conducted annually to determine the value of this effort. An allocation is made on the Statement of Revenues, Expenses, and Changes in Net Assets to reflect the value of this effort as income. This allocation is offset in the operating expenses by an equal amount in purchased services. The amount of this allocation for fiscal year 2012 was $22,698,484.

Likewise, the University provides the Medical Center with various general and administrative support services. An analysis is prepared annually to determine the cost of providing these services. The same type of allocation as above is made to the Statement of Revenues, Expenses, and Changes in Net Assets to reflect the difference between the direct charge to the Medical Center and the actual cost of these services. The amount of this allocation for fiscal year 2012 was $ 2,219,180.

Although these allocations have no direct effect on operating income, they do affect the Medical Center's reimbursement from third-party payers by increasing allowable costs.

12. GAIN SHARING WITH THE SCHOOL OF MEDICINE

Beginning with fiscal year 2003, the Medical Center and the School of Medicine entered into a Memorandum of Understanding for gain sharing. The amount of gain sharing with the School of Medicine is a tiered arrangement based on the Medical Center's income in excess of minimum requirements established by the Board of Visitors. As a result of the Medical Center exceeding the minimum requirements established by the Board of Visitors, for fiscal year 2012, the gain-sharing amount is $8,038,526.

13. COMMITMENTS

Future minimum lease payments by year and in the aggregate under operating leases are:

Year Ending June 30,	Operating Leases
2013	7,508,406
2014	5,414,860
2015	4,419,901
2016	2,298,917
2017	1,791,837
2018-2022	6,907,888
2023-2027	4,808,292
2028-2032	823,200
2033-2037	823,200
2038-2042	823,200
2043-2047	823,200
2048-2050	329,280
Total	$36,772,181

The total rental expense for operating leases for the year ended June 30, 2012, was $8,660,214.

The Medical Center was party to construction contracts and commitments for the year ended June 30, 2012 totaling $329,141,252 of which $309,328,728 was incurred as of June 30, 2012.

14. UNIVERSITY OF VIRGINIA PHYSICIANS GROUP

The University of Virginia Physicians Group (UPG), a nonprofit educational, scientific, and charitable organization, began operating with the approval of the Board of Visitors as of June 30, 1980, to assist the University in providing hospital and medical care services, medical education programs, and programs of public charity at the University. Prior to August 1, 2011, UPG was formerly known as the University of Virginia Health Services Foundation (HSF).

On August 1, 2000, management of 63 outpatient clinics operated by HSF since July 1, 1994, transferred to the Medical Center. At that time, the Medical Center filed for provider-based status with the federal government and became responsible for all costs associated with the operations of these provider-based clinics except for physicians' costs. As of the end of fiscal year 2012, there were 74 outpatient clinics. On August 1, 2000, the Medical Center entered into leased employment agreements with HSF for limited personnel who remained HSF employees, but were performing Medical Center duties.

The Medical Center recorded $22,553,875 as expense payable to the Physicians Group for the provision of supervisory and administrative services, $29,677,411 for other services, and $3,894,186 for rental of space for the year ended June 30, 2012. In addition, the Medical Center recorded non-operating expenses of $5,773,816 payable to the Physicians Group. Prior to fiscal year 2008, this expense had been recorded as supervisory and administrative services.

The Medical Center recorded income from the Physicians Group of $17,077,578 for clinic facility fees and other services, and $862,179 for the rental of space for clinics for the year ended June 30, 2012.

15. RISK MANAGEMENT AND SELF-INSURANCE

The Medical Center is a participant in the Commonwealth's self-insurance program administered by the Department of Treasury, Division of Risk Management. Participation in this program provides the Medical Center with medical malpractice insurance on an occurrence basis with no aggregate limitation and with such limits of coverage equal to the statutory malpractice recovery limits as specified in Section 8.01-581.15 of the Code of Virginia. In the opinion of management, such coverage is adequate to provide for the ultimate liability, if any, which might result from the settlement of claims currently asserted against the Medical Center, as well as the potential liability for medical incidents of which the Medical Center has knowledge, but for which claims have not yet been asserted against the Medical Center. Accordingly, no provision is included in the financial statements for such potential liabilities.

Sufficient information has not been developed by the Medical Center to provide a reasonable basis for estimation of the potential liability for incurred medical incidents, which have not been reported to the Medical Center; however, in the opinion of management, any potential liability for unreported medical incidents is not expected to have a material effect on the financial position of the Medical Center.

The University sponsors a self-funded, comprehensive program of health care benefits. The program covers all employees of the University and the Medical Center. Fringe benefit expenses include estimates for claims that have been incurred, but not reported. Additional information regarding the medical benefits program is available for the entire University only in the University's annual President's Report.

University employees are covered by a self-insured workers' compensation benefits program administered by the Commonwealth's Department of Human Resources. Information regarding this plan is available at the statewide level only in the Commonwealth's Comprehensive Annual Financial Report (CAFR).

Other risk management insurance plans are administered by the Commonwealth's Department of Treasury, Division of Risk Management. Risk management insurance includes property, boiler and machinery, crime, employee dishonesty bond, general (tort) liability, professional liability, aviation and watercraft, and automobile liability. Detailed information relating to this policy is available at the statewide level only in the CAFR

The University is self-insured for the first $100,000 of each property and boiler and machinery loss, and for the first $20,000 of each vehicle physical damage loss. The University also maintains excess crime/employee dishonesty insurance and insurance for vehicle physical damage insurance on vehicles valued in excess of $20,000.

16. RETIREMENT PLANS

Employees of the Medical Center are employees of the Commonwealth. Approximately 10 percent of all full-time classified salaried employees participate in a defined benefit pension plan administered by the Virginia Retirement System (VRS) for the Medical Center. Information relating to this plan is available at the statewide level only in the CAFR. The Commonwealth, not the Medical Center, has overall responsibility for contributions to this plan.

Substantially, all full-time faculty, including certain administrative staff and health care professionals, participate in Faculty Optional Retirement Plans. These are fixed-contribution plans where the retirement benefits received are based upon the employer and employee contributions (all of which are paid by the Medical Center), and the interest and dividends. Individual contracts issued under the plans for full-time faculty, including certain administrative staff, provide for full and immediate vesting of both the Medical Center’s and the participant’s contributions. Health Care Professional’s employer contributions fully vest after one year of employment.

Total pension costs under the plans were $12,850,372 for the year ended June 30, 2012. Contributions to the Optional Retirement Plans were calculated using base salaries of $240,684,634 for the year ended June 30, 2012. The contribution percentage amounted to five percent for the year ended June 30, 2012.

17. POST-EMPLOYMENT BENEFITS OTHER THAN PENSION BENEFITS

The Commonwealth participates in the VRS-administered statewide group life insurance program that provides post-employment life insurance benefits to eligible retired and terminated employees. The Medical Center also provides retiree life insurance to certain retirees.

The Commonwealth provides healthcare credits against the monthly health insurance premiums of its retirees who have at least 15 years of state service and participate in the Commonwealth’s health plan. Additionally, some employees receive healthcare credits for participation in the University of Virginia Health Plan. Information related to these plans is available at the statewide level in the CAFR.

18. CONTINGENCIES

In October 2010, the Medical Center was informed that the federal government’s Center for Medicare Services (CMS) issued notices to Virginia’s Department of Medical Assistance Services (DMAS) disallowing $34,089,804 in Disproportionate Share Hospital adjustment payments to DMAS for fiscal years 2006 through 2009. Based on the receipt of final settlements in the years in question, the Medical Center’s portion of the loss would be $17,921,094 for the federal portion and DMAS could elect to recoup the state portion of another $17,921,094. CMS contends that DMAS inappropriately applied payments against subsequent year allotments. DMAS has appealed this disallowance and any repayment is deferred, pending the appeals resolution. The appeal has not progressed sufficiently to determine whether DMAS will be required to return any payments to the federal program and, if so, whether DMAS will require any providers, including the Medical Center, to return any payments to DMAS. The financial impact of the final resolution of this case on the Medical Center is not known at this time; therefore, no liability has been recorded in the financial statements.

Commonwealth of Virginia

Auditor of Public Accounts

Walter J. Kucharski
Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

November 19, 2012

The Honorable Robert F. McDonnell
Governor of Virginia

The Honorable John M. O'Bannon, III
Chairman, Joint Legislative Audit
And Review Commission

Board of Visitors
University of Virginia

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the **University of Virginia Medical Center**, a division of the University of Virginia, as of and for the year ended June 30, 2012, which collectively comprise the University of Virginia Medical Center's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the University of Virginia Medical Center's management. Our responsibility is to express opinions on these financial statements based on our audit. The prior year summarized comparative information has been derived from the University of Virginia Medical Center's 2011 financial statements, and in our report dated October 31, 2011, we expressed an unqualified opinion on the respective financial statements of the University of Virginia Medical Center.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The basic financial statements of the University of Virginia Medical Center are intended to present the financial position and the changes in financial position and cash flows of only that portion of the business-type activities of the University of Virginia that are attributable to the transactions of the University of Virginia Medical Center. They do not purport to, and do not, present fairly the University of Virginia's overall financial position as of June 30, 2012, and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to previously present fairly, in all material respects, the respective financial position of the University of Virginia Medical Center as of June 30, 2012, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 1 through 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the 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 audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

In accordance with Government Auditing Standards, we have also issued our report dated November 19, 2012 on our consideration of the University of Virginia's internal control over financial reporting, which also includes the University of Virginia Medical Center, and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Walter J. Kucharski

AUDITOR OF PUBLIC ACCOUNTS

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