

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Secondary Market Disclosure Information

December 31, 2015

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Table of Contents

	Page(s)
Balance Sheets	1
Statements of Revenues, Expenses, and Changes in Net Positions	2
Notes to Financial Statements	3-16
Selected Operating Utilization Data	17-23

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)
Balance Sheet
(In thousands)

Assets	Business-Type Activities - UH December 31, 2015	Business-Type Activities - UH June 30, 2015	Increase/(Decrease)
Current assets:			
Cash	\$90,499	\$97,915	(\$7,416)
Restricted investments	302	625	(323)
Patient accounts receivable, net	66,881	65,320	1,561
Due from State of New Jersey	8,146	4,832	3,314
Supplies	18,132	16,268	1,864
Grants receivable	5,179	1,856	3,323
Other current assets	14,087	9,608	4,479
Total current assets	203,226	196,424	6,802
Noncurrent assets:			
Restricted investments, net	127,455	34,876	92,579
Prepaid Bond Insurance	17,610	-	17,610
Capital assets, net	203,722	203,397	325
Total noncurrent assets	348,787	238,273	110,514
Total assets	552,013	434,697	117,316
Deferred Outflows of Resources			
Change in pension plan assumptions and deferred contributions	26,470	28,814	(2,344)
	578,483	463,511	114,972
Liabilities			
Current liabilities:			
Accounts payable and accrued expenses	22,252	27,848	(5,596)
Accrued salaries and related payroll taxes	18,351	19,251	(900)
Accrued vacation and sick pay	12,513	12,293	220
Due to Rutgers University	22,937	26,702	(3,765)
Current portion of accrued claims liability	7,105	7,105	0
Estimated third-party payor settlements, net	5,771	4,864	907
Current portion of long-term debt and capital lease obligation	54	41,830	(41,776)
Other current liabilities	8,252	1,167	7,085
Total current liabilities	97,235	141,060	(43,825)
Noncurrent liabilities:			
Accrued claims liability, net of current portion	21,218	21,205	13
Capital lease obligation, net of current portion	76,727	76,747	(20)
Long-term debt	271,310	108,769	162,541
Pension liability	355,067	346,611	8,456
Total noncurrent liabilities	724,322	553,332	170,990
Total liabilities	821,557	694,392	127,165
Deferred Inflows of Resources			
Net difference between projected and actual earnings on pension plan investments	9,205	10,520	(1,315)
	9,205	10,520	(1,315)
Commitments and contingencies			
Net Position			
Net position:			
Net investment in capital assets	33,065	48,489	(15,424)
Restricted for debt service	2,111	1,723	388
Unrestricted	(287,455)	(291,613)	4,158
Total net position	(252,279)	(241,401)	(10,878)
Total liabilities and net position	\$578,483	\$463,511	\$114,972

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)
Statement of Revenues, Expenses, and Changes in Net Position
(In thousands)

	<u>Business-Type Activities - UH Year ended December 31, 2015</u>	<u>Business-Type Activities - UH Year ended December 31, 2014</u>
Operating revenues:		
Net patient service revenue	\$238,472	\$225,917
Grants revenue	4,159	7,989
Other revenue	7,999	8,445
Total operating revenues	<u>250,630</u>	<u>242,351</u>
Operating expenses:		
Personnel services	120,908	116,762
Contracted physician and resident fees	36,436	36,255
Fringe benefits	47,474	46,789
Pension	9,485	11,691
Supplies and other expenses	102,078	93,277
Depreciation	10,274	9,474
Total operating expenses	<u>326,655</u>	<u>314,248</u>
Operating (loss) income	(76,025)	(71,897)
Nonoperating income (expenses):		
Appropriations from State of New Jersey	68,349	68,769
Interest income	71	34
Interest expense	(5,849)	(5,721)
Forgiveness of long-term debt	-	-
(Loss) income before other changes in net position	<u>(13,454)</u>	<u>(8,815)</u>
Other changes in net position:		
Capital contributions funded by grantors and donors	2,576	-
Total other changes in net position	<u>2,576</u>	<u>-</u>
(Decrease) increase in net position	(10,878)	(8,815)
Net position at beginning of year	(241,401)	80,615
Effect of adoption of GASB 68 and 71	-	(308,245)
Net position at 12/31/15	<u><u>(\$252,279)</u></u>	<u><u>(\$236,445)</u></u>

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

(1) Organization

In accordance with Public Law 2012, c. 45, the New Jersey Medical and Health Sciences Education and Restructuring Act (the Restructuring Act), effective July 1, 2013, University Hospital (the Hospital or UH), a public institution of healthcare and a body politic of the State of New Jersey (the State) was separated from University of Medicine and Dentistry of New Jersey (UMDNJ) as a new stand-alone entity and will continue to be the primary teaching hospital for the Newark-based schools of the Rutgers School of Biomedical and Health Sciences. The Hospital shall maintain its public mission to provide a comprehensive healthcare program and services to the greater Newark community, including outreach and mobile health services as well as services in collaboration with the Newark-based schools of the Rutgers School of Biomedical and Health Sciences. The Hospital is committed to act in accordance with the spirit and intent of the “Agreements Reached between Community and Government Negotiators Regarding New Jersey College of Medicine and Dentistry and Related Matters of April 30, 1968.”

The Hospital is a component unit of the State of New Jersey, and accordingly, its financial statements are included in the State of New Jersey’s Comprehensive Annual Financial Report.

(2) Summary of Significant Accounting Policies

The Hospital’s significant accounting policies are as follows:

(a) Basis of Presentation

The financial statements have been prepared on the accrual basis using the economic resources measurement focus.

(b) Cash

Cash represent operating cash that is unrestricted with original maturities of three months or less at the date of purchase.

(c) Restricted Investments

Restricted investment primarily include assets held by a trustee, TD Bank, National Association under bond resolution. Amounts required to meet current liabilities of the Hospital have been classified as current assets in the statement of net position. Interest income earned on restricted investments is included in nonoperating income (loss).

Restricted investments at June 30, 2015 are invested in the State of New Jersey Cash Management Fund (Cash Management Fund). Amounts contributed in to Cash Management Fund are recorded at amortized cost, which approximately fair value. Restricted investments at December 31, 2015 are invested in U.S. Treasury Obligations and are recorded at fair value based on quoted market prices.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

(d) *Charity Care*

The Hospital provides care to patients who meet certain criteria under its charity care policy at amounts less than its charges or established rates. The Hospital does not pursue collection of amounts determined to qualify as charity care, and they are not reported as revenue.

(e) *Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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 may differ from those estimates.

(f) *Classifications of Revenues and Expenses*

All transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are considered to be operating activities and are reported as operating revenues and operating expenses. Appropriations from State of New Jersey, interest income, and interest expense are reported as nonoperating income and expenses. Other changes in net position, which are excluded from income before other changes in net position, consist of grants for capital assets.

(g) *Patient Accounts Receivable and Net Patient Service Revenue*

The Hospital has agreements with certain third-party payers that provide for payments at amounts different from its charges or established rates. Payment arrangements include prospectively determined rates, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated third-party payer settlements resulting from audits, reviews, and investigations. These estimated third-party payer settlements are accrued in the period the related services are rendered and adjusted in future periods as revised information becomes known or as years are no longer subject to such audits, reviews, and investigations. For the six months ended, December 31, net patient service revenue is reported net of the provision for bad debts of \$98.7 million in 2015 and \$89.6 million in 2014.

The allowance for doubtful patient accounts is the Hospital's estimate of the amount of probable credit losses in its patient accounts receivable. The Hospital determines the allowance based on collection studies and historical write-off experience. Past-due balances are reviewed individually for collectability. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The allowance for estimated doubtful accounts at December 31, 2015 is \$212.5 million and at June 30, 2015 is \$172.5 million.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

(h) Appropriations from State of New Jersey

State appropriation revenues are recognized in the fiscal year during which the State appropriates the funds for the Hospital. The Hospital is fiscally dependent upon these appropriations. Funds appropriated from the State are payments, either directly or indirectly, for services rendered by the Hospital. The Hospital classifies them as non-operating revenues.

The Hospital records both revenues and expenses in an amount equal to expenditures made on its behalf by the State, that is, fringe benefits of the Hospital's employees.

The State pays on behalf of the Hospital for fringe benefits of employees, medical malpractice settlements, negligence, and other torts. In 2015 and 2014 for the six months ended December 31, the fringe benefits of employees paid by the State were \$46.4 million and \$46.8 million. The State also paid the Hospital appropriations of \$21.9 million for each of the six month periods ending December 31, 2015 and 2014 to support the operations of the Hospital.

(i) Government and Private Grants and Contracts

Grants and contracts revenues comprise mainly funds received from grants and contracts from federal, state, other governments and private sources and are recognized when all eligibility requirements for revenue recognition are met, which is generally the period in which the related expenses are incurred.

(j) Capital Assets and Depreciation

Capital assets are recorded at cost or in the case of donated assets at fair value at the date of acquisition. Major renewals and improvements are capitalized while maintaining repairs are expensed when incurred.

The State retains legal title to the land, buildings and improvements as of July 1, 2013 and thereafter and subleases them to the Hospital for \$1 until June 30, 2089. The Hospital is sole beneficiary as to the use of the capital assets and is responsible for their control and maintenance. Accordingly, the capital assets have been capitalized in the accompanying statement of net position.

Depreciation is computed on a straight-line basis using estimated useful lives in accordance with American Hospital Association guidelines:

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

Land improvements	2 to 25 years
Buildings and leasehold improvements	5 to 40 years
Equipment	3 to 25 years

Capital assets under capital lease obligations are depreciated over either the lease term or the estimated useful life.

(k) Supplies

Supplies are stated at the lower of cost (first-in, first-out method) or market (net realizable value).

(l) Income Taxes

The Hospital qualifies as a governmental entity not subject to federal income tax, by reason of the organization being a state or political subdivision thereof, or an integral part of a state or political subdivision thereof; or, an entity all of whose income is excluded from gross income for federal income tax purposes under section 115 of the Internal Revenue Code of 1986. Accordingly, no provision for income taxes has been made in the accompanying financial statements.

(m) Due from State of New Jersey

Due from State of New Jersey represents reimbursements due for fringe benefits paid by the Hospital for employees covered by the State of New Jersey benefit plans.

(n) Grants Receivable

Grants receivable relate to various healthcare provision programs under contract with the State and other grantors. Grants receivable, which are reimbursed to the Hospital for providing such services, relate to Urban Security Initiative, North Star, and School Based Youth Service grants.

(o) Net Position

Net positions of the Hospital are classified in various components. *Net investment in capital assets* consist of capital assets net of accumulated depreciation and reduced by outstanding borrowings used to finance the purchase or construction of those assets. *Restricted expendable net position* are noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or donors external to the Hospital, including amounts deposited with trustee as required by bond indentures, discussed in note 6. *Unrestricted net position* is remaining net position that does not meet

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

the definition of *Net investment in capital assets or restricted*. The Hospital first applies restricted resources when unrestricted resources are available for the same purpose.

(p) *Compensated Absences*

The Hospital's employees earn vacation and holiday days at varying rates depending on years of service and title. Generally, vacation and holiday time may accumulate up to specified maximums, depending on title. Upon resignation or retirement, employees are paid for unused vacation and holiday days, most at the current rate. Employees accrue sick leave at a fixed rate and there is no accumulation limit on sick leave. Upon retirement employees can opt for partial payment of accumulated sick leave.

(q) *Retirement Plans*

Under GASB 68, *Accounting and Financial Reporting for Pensions*, the Hospital recorded pension expense, pension liability, deferred outflows of resources and deferred inflows of resources related to cost sharing multi-employer pension plan for its proportionate share of collective pension expense, collective pension liability, and collective deferred outflows of resources and deferred inflows of resources.

(r) *Accrued Claims Liability*

Accrued claims liability represents estimated amounts payable related to workers compensation claims.

(3) *Cash*

Custodial credit risk is the risk that, in the event of a bank failure, the Hospital's deposits may not be returned to it. At December 31, 2015, the actual amount of cash and cash equivalents in the Hospital's bank accounts was \$92.5 million (with \$2.0 million in outstanding checks). As of May 29, 2015 a Tri-Party collateral agreement was established between the Hospital, the Bank of America, N.A. and the Bank of New York Mellon to collateralize the Hospital's cash.

(4) *Charity Care*

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services furnished under its charity care policy and the estimated

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

cost of those services. The following information measures the level of charity care provided during the six month period ended:

	December 31, 2015		December 31, 2014	
Charges foregone, based upon established rates	22,501	33.6%	24,674	37.8%
Estimated cost incurred to provide charity care	5,337	8.0%	7,185	11.0%

The Hospital only includes charges for patient services in this category for individuals who complied with the New Jersey Department of Health’s criteria for qualification into the Charity Care Subsidy formula. These criteria require a patient’s cooperation and documentation to participate. The Hospital believes that a large number of its patient accounts that default to bad debts are in fact charity care cases, but due to a patients’ unwillingness or inability to provide the documentation such cases do not qualify.

The Hospital received \$26.7 million and \$38.1 million from the State’s Charity Care Subsidy Fund for the six months ended December 31, 2015 and 2014, respectively, of reimbursement associated with cost of bad debt and charity care.

(5) Patient Accounts Receivable, net and Net Patient Service Revenues

Most of the Hospital’s net patient service revenue is from funds received on behalf of patients under governmental health insurance plans. Revenue from these governmental plans is based upon relevant reimbursement principles and is subject to audit by the applicable payers. Certain payers have performed audits and have proposed various disallowances, which other payers may similarly assert.

Included in net patient service revenue are adjustments to prior year estimated third-party payer settlements that were originally recorded in the period the related services were rendered. The adjustments to prior year estimates and other third-party reimbursement receipts or recoveries that relate to prior years resulted in an increases to net patient service revenues.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

Net patient service revenue for the six months ended December 31 are as follows:

	December 31, 2015	December 31, 2014
Medicaid and Medicaid HMO	81,642	72,120
Medicare	44,061	48,161
Other third-party payers	75,765	59,277
Self-Pay	3,652	3,323
	<u>205,120</u>	<u>182,881</u>
Health Care Subsidy Revenues	33,352	43,036
	<u>238,472</u>	<u>225,917</u>

The Hospital provides services to its patients, most of who are insured under third-party payer agreements. Patient accounts receivable, net were as follows:

	December 31, 2015		June 30, 2015	
Medicaid and Medicaid HMO	22,501	33.6%	24,674	37.8%
Medicare	5,337	8.0%	7,185	11.0%
Other third-party payers	33,152	49.6%	28,385	43.4%
Self-Pay	5,891	8.8%	5,076	7.8%
	<u>66,881</u>	<u>100.0%</u>	<u>65,320</u>	<u>100.0%</u>

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

(6) Restricted Investments

Restricted investments consist of the following:

	December 31, 2015	June 30, 2015
Working Capital funds	584	8
Capital reserve funds	107,800	18,770
Debt service reserve funds	17,262	15,000
Debt service funds	2,111	1,723
	<hr/>	<hr/>
	127,757	35,501
Less: Current portion of restricted investments	302	625
	<hr/>	<hr/>
	127,455	34,876

Restricted investments under the terms of the bond resolutions are to provide for debt service requirements and the acquisition of capital assets. Terms of the bond resolutions provide that assets be maintained in separate funds held by the trustee, TD Bank, National Association.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

(7) Long-Term Debt and Capital Lease Obligations

Long-term debt consists of the following:

	December 31, 2015	June 30, 2015
Bonds payable:		
New Jersey Health Care Facilities Financing Authority (NJHCFFA) Series A Bond, bearing interest at fixed rates to be paid semi-annually; with principal payments to be paid annually and set to commence on July 1, 2021 (a)	\$ 254,975	-
NJHCFFA Series A Bond Net Premium and amortized over the 30 year life of the bond (a)	15,826	-
NJHCFFA Revenue Bond Anticipation Notes (BAN), series 2013, bearing interest at a variable rate set daily with principal payments commencing February 1, 2016 and maturing over the following 18 months (b)	-	150,000
New Jersey Educational Facilities Authority (NJEFA) Higher Education Capital Improvement Fund, Series 2000 annual principal payments (c)	471	506
Capital lease obligations (d)	76,819	76,840
	348,091	227,346
Less current installments	54	41,830
Total	\$ 348,037	185,516

- (a) On December 22, 2015 University Hospital issued \$255 million of New Jersey Healthcare Facilities Financing Authority Series 2015A Bonds. Total proceeds from the sale were \$295.8 million and included a net premium of \$15.8 million as well as \$25.0 million from trustee-held debt service and reserve funds. Proceeds from the sale were used for the purpose of: (i) the defeasance of \$150 million of BAN debt (ii) funding current debt service reserve requirements of \$17.3 million; (iii) funding capital projects including \$20 million for IS&T capital, \$10 million for HVAC improvements, \$15 million for operating room renovations, \$10 million for Cancer Center expansion as well as \$52.8 million to address routine and emergency capital needs; (iv) funding bond insurance costs of \$17.6 million, to be amortized over the life of the bond; (v) and paying bond issuance costs of \$2.7 million. The Series 2015A Notes were issued under and secured by a Trust Agreement (the Trust Agreement) by and between the Authority and TD Bank, National Association, as Trustee. The Hospital entered into a Loan Agreement (the Loan Agreement) with the Authority relating to the Series 2015A bond.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

A security feature for this obligation is provided by a lock box arrangement with the Trustee, TD Bank, N.A. Debt service requirements will be funded by unrestricted state appropriations including state charity pools, Delivery System Reform Incentive Payments (DSRIP), Graduate Medical Education (GME) and individual state supplemental appropriations that will flow through the lock box. Any excess funds will then be released to the Hospital for operations.

Principal payments on the bonds will be due annually and are not set to commence until July 1, 2021. Interest will be paid semi-annually on July 1 and January 1, with the first payment due July 1, 2016. The bonds are set at fixed interest rates and are as follows: (i) \$65,250,000 in serial bonds at 5.000%; (ii) \$78,220,000 in term bonds at 4.125% and (iii) \$111,505,000 in term bonds at 5.000%.

- (b) On July 1, 2013, the Hospital issued \$150 million of New Jersey Health Care Facilities Financing Authority (the Authority), Revenue Bond Anticipation Notes, University Hospital Issue, Series 2013A (the Series 2013A Notes) and its Revenue Bond Anticipation Notes, University Hospital Issue, Series 2013B (Federally Taxable) (the Series 2013B Notes) and together with the Series 2013A Notes, the (Series 2013 Notes) for the purpose of (a) the defeasance of the Hospital's allocable share of certain bonds issued by or for the benefit of UMDNJ in the amount of \$77.9 million; (b) financing capital assets in the Hospital's budget (the Series 2013 Project) in the amount of \$23.0 million; (c) funding the debt service reserve requirements of the Series 2013 Notes in the amount of \$15 million; (d) funding working capital in the amount of \$38.2 million; and (e) paying the costs of issuance of the Series 2013 Notes. If the bonds were not refinanced by February 1, 2016 the principal payments were due over the following 18 months. No principal payments are due until February 1, 2016. The Series 2013 Notes were issued under and secured by a Trust Agreement by and between the Authority and The Bank of New York Mellon, as Trustee. The Hospital entered into a Loan Agreement with the Authority relating to the Series 2013 Notes. The Hospital's obligations under the Loan Agreements were evidenced by Promissory Notes. The Hospital's obligations under the Loan Agreements were secured by a pledge of the Hospital's revenues.

The interest rate for the Series 2013 Notes from July 1, 2013 through and including December 31, 2015 is SIFMA rate plus 5.0% (5.07% at June 30, 2015). The interest rate on the Series 2013 Notes from January 1, 2016 and thereafter until the bonds are paid in full is SIFMA rate plus 6.5%. The BANs were fully defeased with proceeds from Series 2015A bonds.

- (c) In addition on July 1, 2013, the Hospital assumed a portion of the UMDNJ obligation of the New Jersey Educational Authority's, Higher Education Capital Improvement fund, Series 2000A (as revised) in the amount of \$0.7 million. The debt bears interest at a fixed rate of 5.0% and requires principal payments until August 2020.
- (d) On July 1, 2013, the Hospital entered into five capital lease agreements with Rutgers, the State University of New Jersey for space in various locations on its Newark campus. The agreements are

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

for 76 years and require monthly rent payments in advance. The Hospital has capitalized the present value of the lease payments using a discount factor of 5.1%, based on Hospital's incremental borrowing rate, and will amortize the asset over the estimated useful life of each of the buildings.

(8) Employee Benefits

Retirement Plans

The Hospital has primarily two retirement plans available to its employees, the State of New Jersey Public Employees Retirement System, a defined benefit plan, and the Alternate Benefit Program, a defined contribution plan. Under these plans, participants make annual contributions, and the State of New Jersey, in accordance with State statutes, makes employer contributions on behalf of the Hospital for these plans. The Hospital is charged for contributions on behalf of employees through a fringe benefits charge assessed by the State which is included within fringe benefits in the accompanying statement of revenues, expenses, and changes in net position. Summary information regarding these plans is provided below.

Postemployment Benefits Other Than Pension

In addition to providing pension benefits, the State provides certain health care and life insurance benefits for the Hospital's retired employees, in accordance with State statutes. Full health coverage is provided to eligible employees retiring with 25 years of service credited on or before June 30, 1997 in one of the State of New Jersey's mandatory pension plans. Employees retiring with 25 years of service credited after June 30, 1997 may share in the cost of the health care provided under the State Plan according to the terms specified in the appropriate bargaining unit agreement in effect at the time the employee reaches 25 years of credited service. The rules governing the contribution rate are the same as that for active employees. Since the costs of these programs are the responsibility of the State and the retired employees, the amounts are not available to the Hospital and no expenses or liabilities for these benefits are reflected in the Hospital's financial statements.

(9) Commitments and Contingencies

(a) Reimbursement

The Hospital derives significant third-party revenues from the Medicare and Medicaid programs. Medicare reimburses most inpatient acute services on a prospectively determined rate per discharge, based on diagnosis-related groups (DRGs) of illnesses, i.e., the Prospective Payment System (PPS). For outpatient services, Medicare payments are based on service groups called ambulatory payment classifications (APCs).

Medicare adjusts the reimbursement rates for capital, medical education, costs related to treating a disproportionate share of indigent patients, and some physician services are reimbursed on a cost basis.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

Due to these adjustments and other factors, final determination of the reimbursement settlement for a given year is not known until Medicare performs its annual audit. The Hospital's costs reports have been settled by the Medicare fiscal intermediary through June 30, 2012, except for years 2005, 2006 and 2010. The Hospital's Medicaid cost report have been audited and settled with the Medicaid fiscal intermediary through June 30, 2013.

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

Revenues received under the various reimbursement systems and agreements are subject to audit and adjustment. Accordingly, provisions for estimated adjustments resulting from audit, final settlement, and changes in estimates have been recorded. Differences between the provisions and the amounts settled are recorded in the year of settlement. The Hospital did not recognize an increase in net patient service revenues for the six months ended December 31, 2015. However \$5.3 million in additional revenue was recognized during the six months ended December 31, 2014 as the result of a favorable decision involving a hospital appeal of prior year Medicare reimbursement.

The Hospital is in varying stages of appeals relating to third-party payers' reimbursement rates. Management routinely provides for the effects of all determinable prior year appeals, settlements, and audit adjustments and records estimates based upon existing regulations, past experience, and discussions with third-party payers. However, since the ultimate outcomes for various appeals are not presently determinable, no provision has been made in the accompanying financial statements for such issues.

The Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (collectively, Health Reform Law), which was signed into law on March 23, 2010, will change how healthcare services are covered, delivered and reimbursed through expanded coverage of uninsured individuals, reduced growth in Medicare program spending, reduction in Medicaid Disproportionate Share Hospital payments, overall reduction and significant redistribution of Medicare Disproportionate Share Hospital payments, and the establishment of programs in which reimbursement is tied to quality and integration. In addition, Health Reform Law reforms certain aspects of health insurance, expands existing efforts to tie Medicare and Medicaid payments to performance and quality, and contains provisions intended to strengthen fraud and abuse enforcement.

There are various proposals at the federal and state levels that could, among other things, reduce reimbursement rates, modify reimbursement methods, or increase managed care penetration, including Medicare and Medicaid. The ultimate outcome of these proposals and other market changes cannot presently be determined.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

Laws and regulations governing Medicaid and Medicare 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 Hospital believes that it is in compliance with all applicable regulations and that any pending or possible investigations involving allegations of potential wrongdoing will not materially impact the accompanying financial statements. While certain regulatory inquiries have been made, compliance with the regulations can be subject to future government review and interpretation as well as significant regulatory action, i.e., fines, penalties, and possible exclusion from Medicaid and Medicare, in the event of noncompliance. In accordance with recent trends in healthcare financial operations, the Hospital has established a Corporate Compliance Committee and appointed a Corporate Compliance Officer to monitor adherence to laws and regulations.

(b) Legal Matters

There are outstanding legal claims against the Hospital for alleged negligence, medical malpractice, and other torts, and for alleged breach of contract. Pursuant to the Agreement, the Hospital is indemnified by the State for such costs. The Hospital records these costs when settled by the State as appropriations from the State and as other than personal services expenses in the accompanying financial statements. Accordingly, no provision has been made in the accompanying financial statements for unsettled claims, whether asserted or not.

In connection with the settlement of two cases that initially resulted in a Deferred Prosecution Agreement with the United States Attorney for the District of New Jersey, UMDNJ, which included the Hospital, entered into a five-year Corporate Integrity Agreement (CIA) with the Office of Inspector General of the Federal Department of Health and Human Services in September 2009. Under the terms of the CIA, UMDNJ agreed to adhere to requirements that will ensure regulatory and legal compliance with all federal healthcare programs. The Hospital remained subject to the CIA upon its separation from UMDNJ. The Hospital received a letter dated March 23, 2015 from Department of Health and Human Services Office of Inspector General, which indicated that the Hospital has completed its CIA requirements and other obligations under the Settlement Agreement.

(c) Accrued Claims Liability

The Hospital is self-insured for workers' compensation benefits. At December 31, 2015 and June 30, 2015, the accrual for estimated workers' compensation claims, based on an independent actuary's estimate, includes undiscounted estimate of ultimate costs for both reported claims and claims incurred but not reported totaled approximately \$28.3 million and \$28.3 million, respectively, and is included in accrued claims liability in the accompanying statement of net position. In addition, the Hospital maintains an excess Workers Compensation Policy with a commercial insurance company.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Notes to Financial Statements

December 31, 2015

(Information Pertaining to the Six Months ended December 31, 2015 and 2014
is Unaudited)

(In thousands)

(d) *Operating Leases*

The Hospital leases equipment, off-site clinic space, and office space under various operating leases. Total rental expense for operating leases was approximately \$1.4 million and \$1.5 million for the six months ended December 31, 2015 and 2014, respectively.

(e) *Rutgers University and the State*

The Hospital entered into a master affiliation agreement, various real estate agreements, transition service agreement, continuing service agreement, various operational agreements with Rutgers University and the State. The agreements include various real estate leases, information technology services, clinical services, research affiliation, medical education, and other services.

(10) *Subsequent Event*

Management evaluated all events and transactions that occurred after December 31, 2015 and through February 15, 2016. The Hospital did not have any known material recognizable subsequent events during the period.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

Table 6-A University Hospital Percent (%) of ED Cases by Payer

Payer Class	2010	2011	2012	2013	2014	2015	Qtr Ending Sept 30, 2015	Qtr Ending Dec 31, 2015
Medicare	5.5%	5.8%	5.1%	5.2%	6.0%	6.0%	6.1%	5.4%
Medicaid	6.9%	5.8%	3.9%	3.8%	7.4%	7.2%	6.0%	5.2%
NJBC	4.3%	4.2%	4.1%	4.0%	4.2%	4.1%	4.1%	3.9%
Other BC	0.5%	0.5%	0.5%	0.4%	0.5%	0.5%	0.5%	0.5%
Commercial	1.9%	1.9%	1.7%	1.8%	2.1%	2.5%	2.6%	2.6%
HMO-Medicare	1.2%	1.5%	1.9%	2.3%	1.7%	1.8%	2.3%	2.4%
HMO-Medicaid	28.1%	29.1%	31.1%	32.7%	40.4%	43.8%	43.2%	45.1%
HMO-Comm.	3.4%	3.3%	3.2%	2.8%	2.6%	2.7%	2.4%	2.6%
Other (WC)	1.2%	1.1%	1.1%	1.0%	1.2%	1.1%	1.2%	0.9%
Other (NF)	2.3%	1.7%	1.7%	1.6%	1.9%	1.8%	2.0%	2.0%
Self-pay	28.8%	29.3%	31.1%	30.8%	25.0%	23.0%	23.6%	24.8%
Charity Care	15.5%	15.4%	14.2%	13.3%	6.7%	5.2%	5.7%	4.3%
Champus	0.1%	0.1%	0.1%	0.0%	0.1%	0.1%	0.1%	0.1%
Other	0.3%	0.3%	0.3%	0.3%	0.2%	0.2%	0.2%	0.2%
<u>Total</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Table 6-B University Hospital Percent (%) of Inpatient Cases by Payer

Payer Class	2010	2011	2012	2013	2014	2015	Qtr Ending Sept 30, 2015	Qtr Ending Dec 31, 2015
Medicare	17.5%	18.5%	18.0%	17.3%	17.1%	17.0%	15.2%	16.3%
Medicaid	19.2%	17.7%	15.7%	14.7%	17.8%	16.8%	18.5%	18.8%
Managed Care *	28.9%	30.3%	33.0%	34.5%	38.4%	42.5%	48.7%	45.5%
Other Third Party Payers	12.6%	12.9%	12.7%	12.6%	13.4%	11.8%	8.4%	10.1%
Self-pay & Charity	21.8%	20.6%	20.6%	20.9%	13.3%	11.9%	9.2%	9.3%
<u>Total</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

* includes Managed Medicare/ Medicaid

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

Table 6-C All New Jersey Hospitals Percent (%) of Inpatient Cases by Payer

Payer Class	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
Medicare	35.3%	35.5%	34.6%	34.3%	34.9%
Medicaid	5.3%	5.2%	4.6%	4.7%	6.9%
Managed Care *	29.1%	29.4%	30.8%	30.8%	31.9%
Other Third Party Payers	20.7%	20.2%	20.1%	20.2%	20.0%
Self-pay & Charity	9.6%	9.7%	9.9%	10.0%	6.3%
<u>Total</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Source: UH HealthQuest Records, Prepared by Oconco Healthcare Consultants. State Hospital data not available at this time. 2015 Data will be updated for next quarterly filing.

Sources of Hospital Revenue

Hospital revenue other than state subsidy arising from inpatient admissions is sourced as follows:

Source	Fiscal Year 2014 (July 1, 2013 - June 30, 2014)		Fiscal Year 2015 (July 1, 2014 - June 30, 2015)		Fiscal Year 2016- 1st Qtr. (July 1, 2015 -Sept 30, 2015)		Fiscal Year 2016- 2nd Qtr. (Oct 1, 2015 -Dec 31, 2015)	
	Discharges	Percentage	Discharges	Percentage	Discharges	Percentage	Discharges	Percentage
Medicare and Medicare HMO	3,163	20.2%	3,426	20.7%	845	19.6%	871	20.3%
Medicaid and Medicaid HMO	7,543	48.2%	8,755	53.0%	2,416	56.1%	2,343	54.6%
Other Third-Party Payers	2,526	16.2%	2,634	16.0%	650	15.1%	678	15.8%
Self-pay & Charity Care	2,404	15.4%	1,708	10.3%	396	9.2%	399	9.3%
Totals	15,636	100.0%	16,523	100.0%	4,307	100.0%	4,291	100.0%

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

State Appropriations

Historical Unrestricted State Aid to University Hospital

	Actual 2009	Actual 2010	Actual 2011	Actual 2012	Actual 2013	Actual 2014	Actual 2015	Budget 2016	Actual PE 9/30/15	Actual PE 12/31/15	
Charity Care	98,962.3	92,041.7	99,298.2	101,012.1	100,664.9	99,003.2	76,230.6	53,483.6	13,370.9	13,370.9	
DSRIP/HRSF	15,055.1	14,979.4	19,049.0	13,715.2	13,715.2	13,715.2	13,000.5	2 13,516.9	3,463.6	2,787.8	
Mental Health	718.1	718.1	718.1	718.1	718.1	718.1	718.1	718.1	179.2	179.7	
GME (Medicaid)	9,292.0	9,367.0	5,298.0	14,804.1	14,804.1	16,459.3	16,083.6	19,224.5	4,806.1	4,806.1	
University Hospital (Specific line Item)	-	25,000.0	3 -	-	-	-	18,841.0	43,841.0	43,841.0	10,960.3	10,960.3
Health Care Stabilization Fund	-	-	-	-	1,000.0	4,900.0	-	-	-	-	
Total	124,027.5	142,106.2	124,363.3	130,249.5	130,902.3	153,636.8	149,873.8	130,784.1	32,780.1	32,104.8	

Notes:

1. All State aid to the Hospital is Subject to and dependant upon appropriations being made for such purpose by the New Jersey State Legislature (the "State Legislature"). The State Legislature has no legal obligation to make any such appropriations.
2. Of the total amount of DSRIP funding recorded in Fiscal Year 2015 (\$13,000,512) University Hospital received \$3,876,636 in August 2015.
3. Appropriated to UMDNJ and provided by UMDNJ to University Hospital

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

Utilization Data

The following table sets forth selected historical utilization statistics for the Hospital's 2013, 2014 and 2015 fiscal years, and the six months ended December 31, 2015 and 2014.

	<u>Years ended June 30</u>			<u>Six months ended Dec 31</u>	
	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2014</u>	<u>2015</u>
Inpatient Discharges:					
Adult (Non-ICU)	11,017	10,212	10,936	5,476	5,641
Pediatrics	1,120	1,095	1,357	718	715
ICU	1,082	789	874	436	433
Maternity	1,646	1,819	1,704	867	918
Newborn Nursery	1,210	1,307	1,190	622	657
NICU	340	414	462	216	234
	<u>16,415</u>	<u>15,636</u>	<u>16,523</u>	<u>8,335</u>	<u>8,598</u>
Patient Days	95,414	93,696	102,472	51,088	52,726
Average Length of Stay	5.8	6.0	6.2	6.1	6.1
Average Daily Census	261.4	256.7	280.7	277.7	286.6
Occupancy Percentage	74.3	72.9	79.7	78.9	81.4
Maintained Beds	352	352	352	352	352
Medicare Case Mix Index	1.835	1.874	1.870	1.865	1.887
All Payer Case Mix Index	1.664	1.641	1.666	1.649	1.661
Emergency Department visits	96,070	91,026	89,978	45,367	45,345
Clinic Visits	170,248	171,909	160,466	77,013	85,456
Outpatient Same Day Surgeries	8,450	8,502	9,050	4,543	4,704
Inpatient Surgeries	3,865	3,918	4,180	2,098	2,384
Liver Transplants	30	33	42	20	22

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

FISCAL YEAR 2016 OPERATING BUDGET

The Hospital's operating budget for its 2016 fiscal year, and underlying revenue and expense assumptions are set forth below.

Revenue:

Net Patient Revenue	\$	381,079,688
Charity Care and HRSF Subsidy		<u>67,756,346</u>
Total Net Patient Service Revenue		448,836,034
Other Income		
Fringe Benefits Reimbursement		92,350,000
State Appropriation		43,841,000
Miscellaneous Income		<u>15,521,778</u>
Total Other Income		151,712,778
Total Revenue		600,548,812

Expense:

Salaries & Wages		236,708,318
Contracted MDs		55,026,984
Contracted Residents		18,445,682
Fringe Benefits*		95,150,000
Supplies and Others		156,575,094
Interest Expense		11,596,015
Facilities Service Agreements		18,559,332
Depreciation		<u>21,000,000</u>
Total Expense		613,061,425
Net Gain (Loss) from operations before Performance Improvement Initiatives		(12,512,614)
Performance Improvement Initiatives in Budget**		<u>2,700,000</u>
Total Net Gain (Loss) from operations after Performance Improvement Initiatives	\$	<u>(9,812,614)</u>

* The Hospital's operating budget and Fiscal Year 2016 Expense Budget Assumptions do not contain any adjustment for the adoption of GASB

** University Hospital personnel are working to plan, approve and implement performance improvement initiatives in addition to those included which may improve the Net Gain (Loss) from Operations for University Hospital in fiscal year 2016.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

Fiscal Year 2016 Revenue Budget Assumptions

- Inpatient volume is projected to remain unchanged from the fiscal year 2015 year-end projection. Outpatient volume is anticipated to remain at the same levels as in the fiscal year 2015 projection, except for the observation unit which is being expanded.
- Case mix, patient type, and payer mix ratios are also anticipated to remain consistent with those experienced in fiscal year 2015.
- A 4% increase in charges is proposed to be implemented July 1, 2015*, which will enable University Hospital's charges to remain in the 75th to 80th percentile of the State's Major Teaching Hospitals and which will increase net revenues by \$1.5 million.
- A small increase of less than 1% is assumed for payment rates from governmental and non-governmental payers, increasing net revenues in fiscal year 2016 by \$2.1 million.
- It is projected that the Hospital's Charity Care subsidy will decrease by \$22.8 million in fiscal year 2016, which will be partially offset by a \$3.1 million increase in Medicaid GME payments.
- Meaningful use incentive payments, totaling \$10.5 million over several years, are forecasted to be on target at \$1.8 million in fiscal year 2016, which is \$2.0 million less than the \$3.8 million received in fiscal year 2015.
- It is assumed that the Hospital will receive \$3.9 million in fiscal year 2016 as a result of the Community Benefit impact for Wage Index reclassification, a \$1.0 million increase from fiscal year 2015.
- The proposed fiscal year 2016 budget also assumes a \$1.0 million reduction in revenue from the EMS contract with the City.

Fiscal Year 2016 Expense Budget Assumptions

- The proposed fiscal year 2016 budget includes a provision for 2.0% salary increases in fiscal year 2016, in addition to a provision for salary increases of 2.0% in fiscal year 2015, accrued in the fiscal year 2015 financial statements. This is still an open item and the forecasted 2% increases are estimates, pending finalization of the union contracts currently being negotiated.
- The Clinical Service Agreements and GME agreements with Rutgers are assumed to remain at the approximately the same levels in fiscal year 2016 as in fiscal year 2015 (\$55.0 million for the Clinical Services Agreement, the GME agreement and the seconded employee agreement, excluding \$17.7 million for residents and fellows). This is still an open item, because negotiations between University Hospital and Rutgers are still underway.
- Expenses for residents and fellows salaries will increase by \$716,000 to \$18.4 million due to raises that were recently negotiated by the State.
- The Continuing Services Agreement and Transition Services Agreement with RBHS are assumed to increase by 0.1% to \$11.6 million in fiscal year 2016.

* The 4% increase in charges was implemented on July 1, 2015.

UNIVERSITY HOSPITAL
(A Component Unit of the State of New Jersey)

Operating Utilization Data

December 31, 2015

- The proposed budget for fiscal year 2016 assumes that the Series 2013A Notes will be re-financed in fiscal year 2016, with no principal payments due in fiscal year 2016. Interest expenses on University Hospital's debt are anticipated to remain at the same rates in fiscal year 2016 as those experienced in fiscal year 2015.

Depreciation expense is projected to be \$21 million in fiscal year 2016, which is \$2.7 million greater than the \$18.3 million depreciation expense in fiscal year 2015, due to the impact of recent and anticipated capital expenditures, including IT capital purchases, that are only partially offset by retiring **assets**.