University of California, San Diego Medical Center

Report on Audits of Financial Statements
For the Years Ended June 30, 2009 and 2008

University of California, San Diego Medical Center
Index
June 30, 2009 and 2008

Page

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
350 South Grand Avenue
Los Angeles CA 90071
Telephone (213) 356 6000
Facsimile (813) 637 4444

Report of Independent Auditors

The Regents of the University of California
Oakland, California

In our opinion, the accompanying financial statements, as shown on pages 18 through 40, present fairly, in all material respects, the financial position of the University of California, San Diego Medical Center (the "Medical Center"), a division of the University of California ("University"), at June 30, 2009 and 2008, and changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Medical Center's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. These 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the Medical Center are intended to present the financial position, and the changes in financial position and cash flows of only that portion of the University that is attributable to the transactions of the Medical Center. They do not purport to, and do not, present fairly the financial position of the University as of June 30, 2009 and 2008, and its changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 2 through 17 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consist principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

PricewaterhouseCoopers LLP

October 12, 2009

Introduction

The objective of the Management's Discussion and Analysis is to help readers better understand the University of California, San Diego Medical Center's financial position and operating activities for the year ended June 30, 2009, with selected comparative information for the years ended June 30, 2008 and 2007. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes to the financial statements. Unless otherwise indicated, years (2007, 2008, 2009, 2010, etc.) in this discussion refer to the fiscal years ended June 30.

Overview

The University of California, San Diego Medical Center (the "Medical Center") serves as the principal clinical teaching site for the University of California, San Diego ("UCSD") School of Medicine, established by The Regents of the University of California ("The Regents") in 1962. It is San Diego County's only academic medical center encompassing hospital-based and ambulatory patient care services, teaching, and clinical research.

The Medical Center is licensed to provide acute care hospital services at two sites, Hillcrest and La Jolla, and provides psychiatric services for children and adolescents at the 35 bed child and adolescent psychiatric unit located at Alvarado Hospital. The Hillcrest site, located in central San Diego, is licensed to operate 398 beds. As the Medical Center's principal teaching hospital, it is the focal point for UCSD's education and community services missions, and serves as a major tertiary referral center for San Diego and Imperial Counties. It is one of two of the county's Level I Trauma Centers and the only Regional Burn Center.

John M. and Sally B. Thornton Hospital ("Thornton Hospital"), which opened in July 1993, is licensed to operate 119 beds and is located in La Jolla on the UCSD campus. It is a general medical/surgical facility and is also the principal location of the Medical Center's cancer services.

Outpatient services are provided by the UCSD Medical Group, which has a clinical practice of over 340 faculty physicians, primarily at the UCSD Ambulatory Care Center and Lewis Street Center in Hillcrest and at the Perlman Ambulatory Care Center in La Jolla. In addition, the UCSD Cancer Center on the East Campus serves as the primary site for outpatient clinical oncology care encompassing prevention, diagnosis, prognosis, treatment, education, rehabilitation and after-care.

Together, these sites enable the Medical Center to provide the full spectrum of services and attract the volume and diversity of patients necessary to meet its educational, clinical research, and community service missions.

For the fiscal year ended June 30, 2009, the Medical Center reported net income of $96.0 million and generated a total margin of 12.2 percent. Total operating revenues increased by 9.5 percent over the prior year due to increased volumes, improved collections resulting from revenue cycle initiatives, strategic pricing, and contract improvements while operating expenses increased by 5.3 percent due to increased patient volumes, wage increases, and inflationary increases in pharmaceuticals, medical and other supplies.

The Medical Center's cash position remained strong despite using $117.9 million for capital expenditures to renovate, expand, and replace existing facilities and invest in new technology.

The Medical Center's operating revenues reflect increased utilization of outpatient services in key ancillary areas including surgery, radiation oncology, imaging and infusion, and continued focus on maximizing collections through revenue cycle initiatives, contracting and pricing strategies. Labor costs continue to reflect increases in wages for nurses, other healthcare professionals and technical employees, and increased premiums for employee healthcare. Medical and other supply costs reflect the impact of new technologies and inflation.

As part of its overall strategic plan, management continues to focus on its financial goal of generating margins to reinvest in clinical initiatives by optimizing reimbursement, improving efficiency, managing resources and costs, and developing comprehensive capital and development plans to ensure adequate funds are available to support its facilities renovation and expansion needs. Growth of patient volumes and expansion of targeted service lines, including surgery, oncology and cardiovascular services, and expansion of the Medical Center's facilities to create capacity and support growth are also key elements of the overall strategic plan.

- *Optimizing net patient service revenue*
  In the second quarter of 2009, the Medical Center completed its revenue cycle improvement project, which was initiated in the third quarter of 2008. The revenue cycle project redesigned and automated workflow and developed and delivered standard reporting of performance in all areas of the revenue cycle including patient access, care management, charge description master/pricing, and patient financial services.

  The Medical Center also continued strategic pricing initiatives through 2009, working with the same outside consulting group to continue to review and revise pricing to maintain and improve its competitive market position. A key change to the process in 2009 was to adjust the set of hospitals included in the benchmarking group to better align with entities that provide the similar types of services, to similar types of patients, in the southern California area.

  Process redesign and technology enhancements, which included changing the structure of outpatient accounts, allowed for automation, management and reporting of key revenue cycle tasks including eligibility checks, authorization and coverage verification. In addition, these changes promoted better controls on the front end process, which reduced manual billing tasks and improved collections by reducing third party payor denials. Care management and patient financial services workflows were also automated. All these efforts contributed to a reduction in the Medical Center's initial denial rate from approximately 13.2% to approximately 8.3%, which resulted in increased collections in 2009 of approximately $21 million and a decrease in days outstanding in patient accounts receivable of 11 days.

In order to keep up with the change in the market and technology and the recent trends towards reduced lengths of stay and a shift from the inpatient to outpatient setting, contracting efforts focused on targeting outpatient reimbursement, increased inpatient per diems in specific services lines, negotiations of carve outs for pharmaceuticals, and removal of not to exceed caps that are in place for services reimbursed at a percent of charges. In addition, efforts are made to maintain stoploss thresholds by limiting negotiated increases. Throughout 2009 the Medical Center continued to participate with other University of California medical centers in coordinated efforts to ensure successful contract negotiations with key payors.

- *Managing resources and costs*
  During 2009, the Medical Center continued to focus on reducing its premium labor costs. As a result of these efforts, the Medical Center experienced a decrease in the use of nurse travelers and a decrease in staff double time shift expense. This resulted in savings to the Medical Center of $1.1 million compared to 2008. Near the end of 2009 the Medical Center also converted an overflow unit to a permanent 6 bed Intensive Care Unit ("ICU") to eliminate the geographical inefficiencies that were occurring within the Surgical ICU. In addition, the Medical Center is evaluating a progressive care model for medical/surgical and Intermediate Medical Unit patients as a means of gaining further staffing efficiencies while maintain patient care quality and nurse staff ratios. Management expects both of these efforts to result in decreased labor costs during 2010.

  Managing medical and other supply costs is also a priority for Medical Center management.

  During 2009, the Medical Center participated in all eight standardized programs offered to members of the University Healthcare Consortium ("UHC") and began the process of providing all supply purchase history to UHC on a quarterly basis for review and analysis. These efforts resulted in increased vendor rebates and indentified further opportunities for supply chain savings. The Medical Center also revamped its Technology Assessment committee, which resulted in an improvement to the process of evaluating new medical technologies.

  Other actions taken during 2009 include standardization of the receipt and delivery of products at both hospitals, improved management of clinical inventories through the use of par cart functionality within the Medical Center's materials management software, and ongoing education and training of purchasing staff on contract and negotiation skills. Management estimates that these initiatives resulted in supply cost savings of approximately $1.5 million during 2009.

  In 2010 the Medical Center will continue to submit data quarterly to UHC Spendlink and Emergency Care Research Institute ("ECRI") for benchmarking of our prices against other medical centers and will proceed with renegotiating contracts where opportunities have already been identified.

- *Facilities planning*

  At the November 18, 2008 meeting of the University of California Board of Regents the Medical Center received approval to amend the project scope and augment the budget of the Thornton Expansion/Cardiovascular project to replace 100 faculty offices with approximately 26 to 28 new inpatient beds on the fourth floor of the Cardiovascular Center, expand the central plant, and cover budget overage due to cost escalation. Additional beds are needed beyond the number originally proposed in this project due to a significant increase in patient care due primarily to the unexpectedly large increase in demand for cancer care and as recent faculty recruits expand their practices. The total impact to the project budget for these changes was $55.8 million and included approval to increase external financing for the project by $39.9 million to a total of $129.0 million.

  Construction is expected to be complete in the December 2010 with occupancy expected in the spring of 2011.

  At the May 15, 2007 meeting of the University of California Board of Regents Building and Grounds Committee, the Medical Center received approval to proceed with preliminary plans for the UCSD Medical Center East Campus Bed Tower. This proposed project would build a new bed tower containing approximately 125-150 inpatient beds as an extension of the Thornton Hospital on the East Campus in La Jolla.

  The project will create additional inpatient capacity within the Medical Center's two-hospital system. During 2009 the Medical Center engaged a well-known healthcare architect and further refined its plans to construct a major addition to Thornton Hospital, including new ICU and medical/surgical beds, new operating and procedure rooms, a major expansion of imaging, and new inpatient perinatal services. In 2010 the Medical Center plans to submit to the University of California Board of Regents a request for project and financing approval. Preliminary project costs are approximately $600 million and the project will be funded through a combination of hospital reserves, gifts, external financing, and state funds. Management estimates the project will be complete in 2016.

  During 2009, the Medical Center spent $93.7 million on facilities renovation and improvement projects, which included $38.0 million funded with hospital cash reserves with the remaining $55.7 million funded with state lease revenue bonds under The Hospital Facilities Seismic Safety Act ("SB1953"), appropriations from the State of California for infrastructure improvements at the Hillcrest site, interim financing from the University for the Thornton Expansion/Cardiovascular project, and donated funds. An additional $25.1 million was spent for equipment, information systems and new technology, which included $24.1 million funded with hospital cash reserves and $1.0 million acquired under capital lease obligations.

  At June 30, 2009, the Medical Center's financial statements include capital assets of $450.8 million.

- *Information Technology Initiatives*
  Adopting new technologies to support operational, clinical and research excellence is also a strategic priority for the Medical Center.

  During 2009, the Medical Center upgraded thousands of clinical and administrative computer workstations and associated software to support its employees and provide them with up to date tools. The Medical Center also deployed very high bandwidth networks to ensure fast and reliable communication among our hospitals, clinics and off-site locations. To support our clinical providers, the Medical Center implemented a sophisticated electronic medical record ("EMR") system across our ambulatory clinics, enabling providers to have on line and up to date access to clinical information for their patients. The Medical Center is in the process of a multi-year implementation of EMR in the inpatient setting. Other clinical systems implemented include an integrated oncology system at our Moores Cancer Center to assist in managing the complex care process typical to cancer centers and voice recognition technology to enable providers to more conveniently perform needed documentation with real time, on line availability.

  To provide more convenience and improved access to our patients, a secure patient portal called MyUCSDchart was implemented. This enables patients to have secure access to their clinical information and to electronically communicate with their physicians and the care teams.

  Our demonstrative efforts to ensure excellence in information technology tools have earned the Medical Center important and highly visible national recognition including awards for achieving HIMSS Stage 6 EMR adoption at both hospital sites, placing us in the top 0.5% of hospitals in the country. In addition, the Medical Center has once again been named a winner of the nationally recognized "Most Wired" award by the Hospitals and Health Network publication and has been recognized as one of the top 25 more wireless hospitals. Management believes that our health information technology deployment is very much aligned with the goals defined in the American Reinvestment and Recovery Act ("ARRA") Health Information Technology ("HIT") act and that our HIT systems meet the requirement of being "certified" and can demonstrate "meaningful use".

Operating Statistics

The following table presents utilization statistics for the Medical Center for 2009, 2008 and 2007:

Statistics	2009	2008	2007
Admissions	23,339	28,194	21,694
Average daily census	367	374	363
Discharges	23,219	23,057	21,635
Average length of stay	5.9	5.9	6.1
Patient days:			
Medicare (non-risk)	33,229	31,822	31,526
Medi-Cal (non-risk)	36,892	37,613	39,356
Contracts – Commercial	48,518	50,596	46,015
County/Uninsured	15,232	16,712	15,622
Total patient days	133,871	136,743	132,519
Ambulatory visits:			
Clinic visits	520,491	473,284	464,804
Emergency room visits	60,551	60,392	60,023
Total ambulatory visits	581,042	533,676	524,827

Admissions increased by 0.6 percent in 2009 compared to 2008 while discharges similarly increased by 0.7 percent in 2009 compared to 2008 while average length of stay remained at 5.9.

Discharges increased by approximately 0.7 percent in 2009 compared to 2008 with increased cases in the cancer and cardiovascular service lines of 6.8 percent and 9.5 percent, respectively. These increases were partially offset by a 11.3 percent decrease in discharges in the women and infants service line due primarily to a decrease in the county-wide birth rate. In 2008, discharges increased by approximately 6.6 percent compared to 2007 as a result of increased admissions in nearly every major service line, with increases of 9.8 and 7.9 percent in the surgery and medicine service lines, respectively.

Total patient days decreased by 2.1 percent in 2009 compared to 2008 due a reduction in average length of stay. Total patient days increased in 2008 by 3.2 percent over 2007 due to an increase in admissions, which was partially offset by a decrease in length of stay in 2008 from 2007.

The increase in patient days in 2009 for Medicare is due primarily in an increase in admissions, which is partially offset by a 4.4 percent decrease in length of stay. In 2008, patient days increased by 1.0 percent over 2007 as a result of an increase in admissions, that was offset, in part, by a slight decrease in length of stay.

In 2009, the decrease in patient days for Medi-Cal is due to both a decrease in admissions and a decrease in length of stay. In 2008, the decrease in patient days for Medi-Cal is due to a decrease in admissions and a 1.7 percent decrease in length of stay. Over half of the decrease in patient days for 2008 for Medi-Cal was experienced at the child and adolescent psychiatry program at Alvarado Hospital. The decrease in patient days for Contracts – Commercial in 2009 is due to a decrease in admissions, which is partially offset by a 2.6 percent increase in length of stay. In 2008, the increase in patient days for Contracts – Commercial is due to an increase in admissions as length of stay remained the same as in 2007.

The decrease in patient days for County/Uninsured in 2009 is due primarily to an 11.2 percent decrease in admissions. In 2008, the increase in patient days for County/Uninsured is due to increased admissions, which were partially offset by a decrease in length of stay in 2008 from 2007.

Ambulatory clinic visits increased by 10.0 percent in 2009 from 2008. This increase is due primarily to a 19.9 percent increase in visits at the UCSD Cancer Center, partially offset by the transfer of a University staff midwife comprehensive health center to a community provider. Emergency room visits increased by 0.3 percent from 2008. Ambulatory clinic visits for 2008 increased by 1.8 percent from 2007 due primarily to an increase in visits at the UCSD Cancer Center, which opened in 2006, while emergency room visits for 2008 increased by 0.6 percent from 2007.

Statements of Revenues, Expenses and Changes in Net Assets

This statement shows the revenues, expenses and changes in net assets for the Medical Center for 2009 compared to the prior two years.

The following table summarizes the operating results for the Medical Center for fiscal years 2009, 2008 and 2007 (dollars in thousands):

	2009	2008	2007
Net patient service revenue	$ 770,679	$ 702,279	$ 628,420
Other operating revenue	13,778	14,330	14,689
Total operating revenue	784,457	716,609	643,109
Total operating expenses	690,121	655,509	575,542
Income from operations	94,336	61,100	67,567
Total non-operating expenses	1,653	173	(332)
Income before other changes in net assets	$ 95,989	$ 61,273	$ 67,235
Margin	12.2 percent	8.6 percent	10.5 percent
Other changes in net assets	(13,037)	(4,851)	(29,729)
Net assets – beginning of year	485,940	429,518	392,012
Net assets – end of year	$ 568,892	$ 485,940	$ 429,518

Revenues

Total operating revenues for the year ended June 30, 2009 were $784.5 million, an increase of $67.8 million, or 9.5 percent, over 2008. Total operating revenues for 2008 of $716.6 million increased by $73.5 million, or 11.4 percent, over 2007.

Net patient service revenue for 2009 increased by $68.4 million, or 9.7 percent, over 2008. The increase in 2009 over 2008 was due to increased outpatient volumes, improved collections, an increase in the Medicare case mix index, and additional Medi-Cal funds made available under the American Recovery and Reinvestment Act. Net patient service revenue in 2008 increased by $73.9 million, or 11.8 percent, over 2007 due to increased inpatient volumes at both hospital sites, increased outpatient volumes in key ancillary areas including surgery, radiation, oncology, imaging and infusion and improved collections due to ongoing strategic pricing and contracting efforts.

Net patient service revenue is reported net of estimated allowances under contractual arrangements with Medicare, Medi-Cal, the County of San Diego, and other third-party payors and has been estimated based on the principles of reimbursements and terms of the contracts currently in effect.

Other operating revenue consists primarily of Clinical Teaching Support ("CTS") funds, joint venture income accounted for under the equity method, and other non-patient services such as cafeteria and gift shop operations. The decrease in 2009 in other operating revenue was due primarily to reduced state funding for Clinical Teaching Support. The decrease in 2008 in other operating revenue was due to a decrease in joint venture income.

The following table summarizes net patient service revenue for 2009, 2008 and 2007 (dollars in thousands):

Payor	2009	2008	2007
Medicare (non-risk)	$ 159,861	$ 147,494	$ 132,219
Medi-Cal (non-risk)	185,605	158,636	155,232
Contracts – commercial	395,361	366,016	314,027
County/Uninsured	29,852	30,133	26,942
Total	$ 770,679	$ 702,279	$ 628,420

Net revenues for Medicare represent payments for services provided to patients under Title XVIII of the Social Security Act. Payments for inpatient services provided to Medicare beneficiaries are paid on a per discharge basis at rates set at the national level with adjustments for prevailing area labor costs. The Medical Center also receives additional payments for direct and indirect costs for graduate medical education, disproportionate share of indigent patients, capital reimbursement, and outlier payments on cases with unusually high costs of care. Hospital outpatient care is reimbursed under a prospective payment system.

Net revenue for Medicare patients increased in 2009 by $12.4 million from 2008. Inpatient net revenue for 2009 increased by $6.7 million, or 6.4 percent, over 2008 due primarily to a 7.0 percent increase in discharges and a 6.5% increase in case mix index. Medicare outpatient net revenue for 2009 increased by $5.5 million or 13.4 percent over 2008 due to an increase in patient activity. Net revenue also includes reimbursement for prior year settlements and other adjustments of $0.7 million in 2009 compared to $9.6 million in 2008 and $10.2 million in 2007.

Net revenue for Medicare patients increased in 2008 by $15.3 million from 2007. Inpatient net revenue for 2008 increased by $9.2 million or 9.6 percent over 2007 due primarily to a 6.5 percent increase in discharges and a 5.9 percent increase in the base payment rate per discharge reflecting the annual PPS update factor and wage index adjustment. Medicare outpatient net revenue for 2008 increased by $6.1 million over 2007 due primarily to an increase in patient activity.

In 2006, the State implemented a new Medicaid fee-for-service inpatient payment system. Under SB1100, the legislation enacting the new federal Medicaid hospital financing waiver in California, payments for inpatient services include a combination of fee-for-service payments, Disproportionate Share ("DSH") payments and Safety Net Care Pool ("SNCP") payments.

Total Medi-Cal net revenue for 2009 increased by $27.0 million over 2008 due primarily to an increase in funds made available through the Medicaid hospital waiver and an increase in outpatient supplemental payments. In 2008, total Medi-Cal net revenue increased by $3.4 million over 2007 due primarily to increased utilization of outpatient ancillary services.

Inpatient net revenue for 2009 increased by $20.7 million from 2008 due primarily to an increase in federal matching funds made available under the American Recovery and Reinvestment Act and prior year adjustments to revenue. In 2008, inpatient net revenue for 2008 decreased by $1.1 million from 2007 due primarily to prior year adjustments to revenue available to the Medical Center under the new federal Medicaid hospital financing waiver.

In 2009, outpatient Medi-Cal net revenue increased by $6.3 million from 2008 due to recognition of $6.3 million more supplemental payments under Assembly Bill 915, *the Public Hospital Outpatient Services Supplemental Reimbursement Program*, in 2009 compared to 2008. In 2008, outpatient Medi-Cal net revenue increased by $4.5 million from 2007 due to increased patient volumes and a $1.1 million increase in supplemental funds.

Net revenue for contracts – commercial increased by $29.3 million over 2008 due primarily to an increase in outpatient activity and the impact of the Medical Center's ongoing revenue cycle initiatives, contracting efforts and strategic pricing. The $51.0 million increase in 2008 over 2007 is due primarily to an increase in patient activity and similar contracting and pricing strategies.

County/Uninsured patient service revenues includes payments from the County of San Diego under the Medical Center's contract to provide emergency medical services to the county's indigent population and emergency and non-emergency medical services to County custodial patients. Net revenue for County/Uninsured decreased by $0.3 million from 2008 due primarily to a reduction in patient days. The $3.2 million increase in 2008 over 2007 is due primarily to an increase in patient days and an increase in reimbursement for non-emergency services provided to custodial patients.

Operating Expenses

The following table summarizes the operating expenses for the Medical Center for fiscal years 2009, 2008 and 2007 (dollars in thousands):

	2009	2008	2007
Salaries and wages	$ 278,809	$ 261,726	$ 225,768
Employee benefits	86,204	77,045	69,487
Professional services	30,054	26,170	23,581
Medical supplies	164,592	152,732	131,051
Other supplies and purchased services	95,139	105,432	94,198
Depreciation and amortization	29,763	27,598	26,148
Insurance	5,560	4,806	5,309
Total operating expenses	$ 690,121	$ 655,509	$ 575,542

Total operating expenses for 2009 of $690.1 million increased by $34.6 million, or 5.3 percent, over 2008 due primarily to increased outpatient volumes, the impact of inflation, and increased depreciation expense. Total operating expenses for 2008 increased by $80.0 million, or 13.9 percent, over 2007 due primarily to similar patient volume and inflationary increases.

Salary and wage expenses include wages paid to hospital employees and holiday and sick pay. Amounts paid for nurse registry and other contract labor is included in other expenses. The total paid for salaries and wages in 2009 increased by $17.1 million, or 5.6 percent, over 2008 due primarily to increases in wages and a 5.4 percent increase in full time equivalent employees ("FTEs") In 2008, salaries and wages increased by $36.0 million due to similar inflationary increases and a 4.8 percent increase in FTEs resulting from increased patient activity and the provision of services previously provided by outside contractors.

In 2009, employee benefits expense increased by $9.2 million, or 11.9 percent, over 2008 due the increase in FTEs and an increase in employee healthcare premiums. Employee benefits expense increased by $7.6 million, or 10.9 percent, in 2008 over 2007 due to the similar increases. Employee benefit expense for 2009, 2008 and 2007 also include a retrospective rebate of workers compensation premiums from the University of $5.8 million, $7.1 million and $6.3 million, respectively.

Payments for professional services increased by $3.9 million, or 14.8 percent, in 2009 compared to 2008 and $2.6 million, or 11.0 percent, in 2008 compared to 2007 due to the provision of new services.

In 2009, medical supply expense increased by $11.9 million, or 7.8 percent, over 2008 due to increased patient volumes and the impact of inflation. Surgical supplies and implant costs increased by $5.1 million or 11.7 percent over 2008 due in part to a 3.0 percent increase in surgical cases. Pharmaceuticals increased by $5.0 million or 7.5 percent over 2008 due to inflation and increased patient volumes. This includes a $1.8 million increase in the cost of drugs provided to patients at the UCSD Cancer Center, a $1.0 million increase in the cost of infusion drugs provided to pharmacy home infusion patients, and a $0.5 million increase in the cost of drugs for hemodialysis patients. The remaining $1.8 million increase in medical supply expense in 2009 was in blood bank and other supply costs. Medical supply expense for 2008 increased by $31.7 million, or 16.5 percent, over 2007 with increases in pharmaceutical costs of $10.9 million and implants, surgical and all other supply of $10.8 million. These increases in 2008 were the result of an increase in patient volumes and the impact of inflation.

Other supplies and purchased services expense decreased in 2009 by $10.3 million, or 9.8 percent, over 2008 due to a decrease in outside consulting expense related to the revenue cycle initiative and decreased expenditures for facilities equipment maintenance and improvements. Other supplies and purchased services expense for 2008 increased by $11.3 million, or 12.0 percent, over 2007 due to the one-time consulting expense related to the revenue cycle initiative and the additional facilities and equipment maintenance costs incurred in 2008.

Depreciation and amortization increased by $2.2 million, or 7.8 percent, in 2009 compared to 2008 and by $1.5 million, or 5.5 percent, in 2008 compared to 2007 due to increased capital expenditures.

Insurance expense totaled $5.6 million in 2009, compared to $4.8 and $5.3 million in 2008 and 2007, respectively. The Medical Center is insured through the University's malpractice and general liability programs.

Non-operating Revenues (Expenses)
Non-operating revenue, which includes interest earned on invested cash balances, interest expense on debt, and losses from disposal or retirement of capital assets, increased by $1.5 million from 2008. This increase is due primarily to a $2.9 million decrease in interest expense offset partially by a $1.4 million decrease in interest income on average daily invested cash. The decrease in interest expense is due to an increase in capitalized interest on construction projects funded with unrestricted funds. The decrease in interest income is due to both a decrease in the average daily invested cash balance and a decrease in the average short term investment pool earning rate. Non-operating expenses for 2008 increased by $0.5 million from 2007 due primarily to increased interest income resulting from an increase in average daily invested cash.

Income before Other Changes in Net Assets
The Medical Center reported income before other changes in net assets of $96.0 million in 2009 compared to $61.3 million in 2008 and $67.2 million in 2007.

Other Changes in Net Assets
The lower section of the statements of revenues, expenses and changes in net assets shows the other changes to net assets in addition to the income or loss. Net assets are the difference between the total assets and total liabilities. The other changes in net assets represent additional funds the Medical Center receives and cash outflow for support and transfers to other university entities.

Included in the other changes in net assets in 2009 and 2008 are the following:

- Proceeds from state capital appropriations of $1.9 million and $3.5 million, respectively.
- Donated assets of $1.8 million and $13.2 million, respectively
- Health system support represents transfers primarily to the School of Medicine for academic and clinical support including support for the School of Medicine's primary care activities. The Medical Center transferred $32.9 million and $31.3 million, respectively.
- Transfers from the University of $16.6 million and $9.3 million, respectively.

In total, the net assets increased for the year ended June 30, 2009 by $83.0 million to $568.9 million. In 2008, net assets increased by $56.4 million to $485.9 million.

Statements of Net Assets

The following table is an abbreviated statement of net assets at June 30, 2009, 2008 and 2007 (dollars in thousands):

	2009	2008	2007
Current assets:			
Cash	$ 150,789	$ 132,348	$ 127,683
Patient accounts receivable (net)	123,060	130,658	107,874
Other current assets	51,475	50,951	41,477
Total current assets	325,324	313,957	277,034
Capital assets (net)	450,805	362,821	319,189
Other assets	5,958	4,819	4,057
Total assets	782,087	681,597	600,280
Current liabilities	130,208	104,508	75,488
Long-term debt	82,987	91,149	95,274
Total liabilities	213,195	195,657	170,762
Net assets:			
Invested in capital assets (net)	320,904	258,570	218,243
Unrestricted	247,988	227,370	211,275
Total net assets	$ 568,892	$ 485,940	$ 429,518

Total current assets increased by $11.4 million in 2009 over 2008. Total current assets at June 30, 2008 were $36.9 million higher than the previous year.

Cash increased by $18.4 in million in 2009. The increase was primarily due to cash from operations and investing exceeded cash used for capital investments and non-capital financing. In 2008, cash increased by $4.7 million over 2007.

Patient accounts receivable, net of estimated uncollectibles, decreased by 5.8 percent in 2009 over 2008 due to an 11 day decrease in days outstanding in account receivable. The decrease in days outstanding in accounts receivable in 2009 is due to improved collections resulting from revenue cycle initiatives. In 2008, net patient accounts receivable increased by 21.1 percent over 2007 due to increased patient revenues and a 3 day increase in days outstanding in account receivable.

Other current assets, which include third party payor settlement, non-patient receivables, inventory, and prepaid expenses, increased by $0.5 million, or 1.0 percent, from 2008 due to the following: third party payor settlements and other receivables decreased by $1.5 million due primarily to collection of prior year amounts due from affiliated institutions for housestaff rotations; the total value of the Medical Center's pharmaceutical and supply inventories increased by $1.0 million due to the impact of inflation; and prepaid expenses increased by $1.0 million due to increases in prepaid equipment maintenance and building rent. In 2008, other current assets increased by $9.5 million, or 22.8 percent, from 2007 due to the following: third party payor settlements increased by $9.8 million due primarily to the recording in 2008 of receivables of $3.8 million related to settlement of prior year cost report appeals and an increase in the receivable for outstanding Medicare cost reports; non-patient receivables decreased by $1.5 million while the total value of the Medical Center's pharmaceutical and supply inventories decreased by $0.3 million from the prior year; and prepaid expense increased by $1.5 million over the prior year due primarily to the prepayment of $1.1 million for design fees and rent related to a radiation oncology modular facility to be delivered in 2009.

Capital assets increased by 24.2 percent in 2009 over 2008 due to an increase in capital spending on seismic safety work at the Hillcrest site, increased expenditures on the Thornton Expansion/Cardiovascular Center project, and increased expenditures for major clinical equipment in radiology, cardiology, and radiation oncology. Capital assets increased by 13.7 percent in 2008 over 2007 due to similar expenditures for facilities improvements and expansion.

In 2009, other assets increased by $1.1 million from the prior year due an increase in investment in joint ventures. In 2008, other assets increased by $0.8 million from the prior year due primarily to investment in the UCSD Ambulatory Surgery Center LLC in 2008.

Current liabilities increased by $25.7 million, or 24.6 percent, from 2008 due primarily to a $34.6 million increase in the current portion of long-term debt, offset by an $8.9 million decrease in accounts payable, third party payor settlement and other accrued expenses. The increase in the current portion of long-term debt is due primarily to $34.3 million of commercial paper borrowing from the University for interim financing for the Thornton Expansion/Cardiovascular project. The decrease in other current liabilities is due primarily to a decrease in days outstanding in accounts payable. Current liabilities increased by $29.0 million, or 38.4 percent, in 2008 over 2007 due primarily to an $19.6 million increase in accounts payable due to an increase in days outstanding in accounts payable and an increase in construction spending, and a $9.2 million increase in accrued salaries and benefits due primarily to timing of bi-weekly payrolls.

Long-term debt decreased by $8.2 million from the prior year due as principal payments exceeded new borrowings. Long-term debt decreased by $4.1 million in 2008 from 2007 for similar reasons.

Net assets increased by $83.0 million in 2009 over the prior year. The change in net assets includes the excess of revenues over expenses of $96.0 million, receipt of $1.9 million of state capital appropriations, $1.8 million of donated assets, and $16.6 million of transfer from the University and other changes. These increases to net assets were reduced by the transfer of approximately $32.9 million of funds to the University as health system support. During fiscal years 2008 and 2007, the Medical Center transferred $31.1 million and $30.3 million of funds to the University as health system support, respectively.

Liquidity and Capital Resources

During 2009, the Medical Center generated $123.1 million of cash from operations and $2.4 million from investing activities. Capital expenditures for equipment, facilities, and information systems totaled $118.0 million, of which $1.9 million of capital was acquired with state funds, $16.3 million was acquired with state lease revenue bond funds under the Hospital Facilities Seismic Safety Act ("SB1953"), $1.8 million was acquired with donated funds, and $1.0 million was acquired under capital lease obligations.

In 2009, cash used for debt repayments was $8.7 million. An additional $32.9 million of funds were transferred to the University as health system support to fund clinical program development and activities of the School of Medicine and other areas of health sciences.

The following table shows key liquidity and capital ratios for 2009, 2008 and 2007:

	2009	2008	2007
Days cash on hand	83	77	84
Days of revenue in accounts receivable	61	72	69
Capital investment ($ in millions)	$118.0	$71.6	$39.7
Debt service coverage ratio	13.5	7.8	8.2

Days cash on hand increased from 77 days at June 30, 2008 t o83 days at June 30, 2009. The goal set by the University of California Office of the President is a minimum of 60 days.

The days of revenue in accounts receivable measures the average number of days it takes to collect patient accounts receivable. In 2009, net days in receivables decreased 11 days to 61 due to a reduction in the initial denial rate and other process improvements related to revenue cycle initiatives.

The debt service coverage ratio for 2009 was 12.2 times debt service compared to 7.8 times debt service in 2008. Total debt service payments were $13.2 million in 2009 and $11.9 million in 2008.

Looking Forward

The Hospital Facilities Seismic Safety Act ("SB 1953")
During 2009, the UC San Diego Medical Center's capital program continued to address the requirements in State of California Senate Bill 1953 ("SB 1953"). The projected cost for the Medical Center, which will be compliant with the statutory requirements by January 1, 2013, is $48 million. The capital cost of compliance will be financed through the use of state lease revenue bond funds and Hospital Reserves. In 2009 and 2008, $16.3 million and $13.4 million, respectively, were spent on these requirements.

Payments from Federal and State Health Care Programs
Entities doing business with governmental payors, including Medicare and Medicaid (Medi-Cal in California), are subject to risks unique to the government-contracting environment that are difficult to anticipate and quantify. Revenues are subject to adjustment as a result of examination by government agencies as well as auditors, contractors, and intermediaries retained by the federal, state, or local governments (collectively "Government Agents"). Resolution of such audits or reviews often extends (and in some cases does not even commence until) several years beyond the year in which services were rendered and/or fees received.

Moreover, different Government Agents frequently interpret government regulations and other requirements differently. For example, Government Agents might disagree on a patient's principal medical diagnosis, the appropriate code for a clinical procedure, or many other matters. Such disagreements might have a significant effect on the ultimate payout due from the government to fully recoup sums already paid. Governmental agencies may make changes in program interpretations, requirements, or "conditions of participation," some of which may have implications for amounts previously estimated. In addition to varying interpretation and evolving codification of the regulations, standards of supporting documentation and required data are subject to wide variation.

In accordance with generally accepted accounting principles, to account for the uncertainty around Medicare and Medicaid revenues, the Medical Center estimates the amount of revenue that will ultimately be received under the Medicare and Medi-Cal programs. Amounts ultimately received or paid may vary significantly from these estimates.

Medicaid Reform

In 2005, California implemented a new Medicaid fee-for-service ("FFS") inpatient hospital payment system. The new payment system is the result of a new federal Medicaid hospital financing waiver ("waiver") that will govern Medicaid FFS inpatient hospital payments through fiscal year 2010. The California state legislature enacted Senate Bill 1100 ("SB 1100") to implement the new waiver. SB 1100 is designed to protect baseline Medicaid funding for the University's medical centers from 2006 through 2010 – at a minimum medical centers will receive the Medicaid inpatient hospital payments they received in 2005 adjusted for yearly changes in costs. SB 1100 also allows the University's medical centers to receive additional waiver growth funding subject to the availability of funds. Payments to the University's medical centers under SB 1100 include a combination of Medi-Cal inpatient FFS payments, Medi-Cal DSH payments and SNCP payments. The recently enacted federal economic stimulus package, which increases California's federal DSH allotment and the federal matching rate for FFS payments, will increase the net payment amounts under the waiver to the Medical Centers for the period October 2008 through December 2010. Although the federal inpatient hospital financing waiver and SB 1100 are designed to ensure a predictable Medicaid supplemental payment funding level and provide growth funding, the full financial impact of these changes in the future cannot be determined.

Children's Hospital Bond Act of 2008

In 2008, California voters passed Proposition 3 that enables the state of California to issue $980 million in General Obligation bonds to fund capital improvement projects for children's hospitals. Each of the University medical centers is eligible for $39 million of grant funding from this pool of funds. Grant funds must be used for capital projects associated with the care of children and must be used prior to June 30, 2018.

University of California Retirement Plan

The University of California Retirement Plan ("UCRP") costs are funded by a combination of investment earnings, employee member and employer contributions. Since 1990, there have not been any Medical Center contributions to the UCRP. In addition, since 1990, the required employee member contributions to the UCRP have been suspended. However, employee member contributions are required to be made to the separate defined contribution plan maintained by the University.

Effective with the July 1, 2008 actuarial valuation, a new funding policy, including a three-year amortization period for any initial surplus, was adopted for the Plan. The new funding policy determines recommended total contributions based upon the Plan's Normal Cost adjusted for any surplus or underfunding, starting with the Plan Year beginning July 1, 2009. University and member contributions to the plan have generally not been required since November 1, 1990 for most membership classifications. Member pretax contributions made to the Plan are redirected to the University of California Defined Contribution plan on a mandatory basis.

The Regents has authorized the initial resumption of shared employer and employee contributions to the Plan beginning in the last quarter of 2010. The University will implement a multi-year contribution strategy under which shared employer and employee contribution rates will increase gradually over time, shared between the Medical Center and employees, based upon UCRP's current normal cost.

Cautionary Note Regarding Forward-Looking Statements

Certain information provided by the Medical Center, including written as outlined above or oral statements made by its representatives, may contain forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, which address activities, events or developments that the Medical Center expects or anticipates will or may occur in the future contain forward-looking information.

In reviewing such information it should be kept in mind that actual results may differ materially from those projected or suggested in such forward-looking information. This forward-looking information is based upon various factors and was derived using various assumptions. The Medical Center does not undertake to update forward-looking information contained in this report or elsewhere to reflect actual results, changes in assumptions or changes in other factors affecting such forward-looking information.

University of California, San Diego Medical Center
Statements of Net Assets
June 30, 2009 and 2008
(Dollars in thousands)

	2009	2008
Assets		
Current assets:		
Cash	$ 150,789	$ 132,348
Patient accounts receivable, net of estimated uncollectibles of $17,332 and $9,430, respectively	123,060	130,658
Other receivables, net of estimated uncollectibles of $191 and $163, respectively	8,848	19,445
Third-party payor settlements	18,847	9,777
Inventory	13,551	12,524
Prepaid expenses and other assets	10,229	9,205
Total current assets	325,324	313,957
Capital assets, net	450,805	362,821
Deferred costs of issuance	1,515	1,627
Prepaid expenses and other assets, net of current portion	4,443	3,192
Total assets	782,087	681,597
Liabilities		
Current liabilities:		
Accounts payable and accrued expenses	45,940	58,032
Accrued salaries and benefits	39,271	37,961
Third-party payor settlements	1,840	–
Current portion of long-term debt and capital leases	43,157	8,515
Total current liabilities	130,208	104,508
Long-term debt and capital leases, net of current portion	82,987	91,149
Total liabilities	213,195	195,657
Net Assets		
Invested in capital assets, net of related debt	320,904	258,570
Unrestricted	247,988	227,370
Total net assets	$ 568,892	$ 485,940

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

University of California, San Diego Medical Center
Statements of Revenues, Expenses and Changes in Net Assets
For the Years Ended June 30, 2009 and 2008
(Dollars in thousands)

	2009	2008
Net patient service revenue, net of provision for doubtful accounts of $28,892 and $14,303, respectively	$ 770,679	$ 702,279
Other operating revenue:		
Clinical teaching support	7,853	8,318
Other	5,925	6,012
Total other operating revenue	13,778	14,330
Total operating revenue	784,457	716,609
Operating expenses:		
Salaries and wages	278,809	261,726
UCRP, retiree health and other employee benefits	86,204	77,045
Professional services	30,054	26,170
Medical supplies	164,592	152,732
Other supplies and purchased services	95,139	105,432
Depreciation and amortization	29,763	27,598
Insurance	5,560	4,806
Total operating expenses	690,121	655,509
Income from operations	94,336	61,100
Non-operating revenues (expenses):		
Interest income	3,688	5,113
Interest expense	(1,740)	(4,606)
Loss on disposal of capital assets	(295)	(334)
Total non-operating revenues (expenses)	1,653	173
Income before other changes in net assets	95,989	61,273
Other changes in net assets:		
State capital appropriations	1,918	3,453
Donated assets	1,849	13,185
Health system support	(32,907)	(31,297)
Transfers from University, net	16,627	9,286
Other	(524)	522
Total other changes in net assets	(13,037)	(4,851)
Increase in net assets	82,952	56,422
Net assets – beginning of year	485,940	429,518
Net assets – end of year	$ 568,892	$ 485,940

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

University of California, San Diego Medical Center
Statements of Cash Flows
For the Years Ended June 30, 2009 and 2008
(Dollars in thousands)

	2009	2008
Cash flows from operating activities:		
Receipts from patients and third-party payors	$ 784,494	$ 670,205
Payments to employees	(315,045)	(285,428)
Payments to suppliers	(328,332)	(289,301)
Payments for benefits	(70,116)	(62,127)
Other receipts, net	52,095	48,682
Net cash provided by operating activities	123,096	82,031
Cash flows from noncapital financing activities:		
Health system support	(32,907)	(31,297)
Net cash used by noncapital financing activities	(32,907)	(31,297)
Cash flows from capital and related financing activities:		
State capital appropriations	1,918	3,453
Transfers from the University	16,627	9,286
Proceeds from debt issuance	34,314	–
Proceeds from the sale of capital assets	4	39
Purchases of capital assets	(117,890)	(64,821)
Principal paid on long-term debt and capital leases	(8,726)	(7,319)
Interest paid on long-term debt and capital leases	(1,721)	(4,587)
Gifts and donated funds	1,849	13,185
Other	(525)	522
Net cash used by capital and related financing activities	(74,150)	(50,242)
Cash flows from investing activities:		
Interest income received	3,688	5,113
Investments in joint venture	(1,286)	(940)
Net cash provided by investing activities	2,402	4,173
Net increase in cash	18,441	4,665
Cash – beginning of year	132,348	127,683
Cash – end of year	$ 150,789	$ 132,348

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

University of California, San Diego Medical Center
Statements of Cash Flows (Continued)
For the Years Ended June 30, 2009 and 2008
(Dollars in thousands)

	2009	2008
Reconciliation of income from operations to net cash provided by operating activities:		
Income from operations	$ 94,336	$ 61,100
Adjustments to reconcile income from operations to net cash provided by operating activities:		
Depreciation and amortization expense	29,763	27,598
Provision for doubtful accounts	28,892	14,303
Changes in operating assets and liabilities:		
Patient accounts receivable	(21,294)	(37,087)
Other receivables	10,597	1,503
Inventory	(1,027)	338
Prepaid expenses and other assets	(989)	(1,472)
Accounts payable and accrued expenses	(11,262)	17,175
Accrued salaries and benefits	1,310	9,257
Third-party payor receivable settlements	(9,070)	(10,684)
Third-party payor payable settlements	1,840	–
Net cash provided by operating activities	$ 123,096	$ 82,031
Supplemental noncash activities information:		
Capitalized interest	$ 2,964	$ –
Capital assets acquired through capital lease obligations	985	4,391
Amortization of deferred financing costs	112	112
Amortization of bond premium	93	93

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

1. Organization

The University of California, San Diego Medical Center (the "Medical Center") is a part of the University of California (the "University"), a California public corporation established under Article IX, Section 9 of the California Constitution. The University is administered by The Regents of the University of California ("The Regents"), an independent board composed of 26 members. The Medical Center's activities are monitored by The Regents' Committee on Health Services, with direct management authority being delegated to the Medical Center Director by the Chancellor of the San Diego campus. The Medical Center operates licensed bed facilities as follows: the 398 bed UCSD Medical Center in Hillcrest, near downtown San Diego, the 119 bed John M. and Sally B. Thornton Hospital ("Thornton Hospital") located in La Jolla, and the 35 bed child and adolescent programs at Alvarado Hospital.

2. Summary of Significant Accounting Policies

Basis of Presentation

The financial statements of the Medical Center have been prepared in accordance with accounting principles generally accepted in the United States of America, including all applicable statements of the Governmental Accounting Standards Board ("GASB"), and all statements of the Financial Accounting Standards Board through November 30, 1989. The proprietary fund method of accounting is followed and uses the economic resources measurement focus and the accrual basis of accounting. In addition, these statements follow generally accepted accounting principles applicable to the health care industry, which are included in the American Institute of Certified Public Accountants' Audit and Accounting Guide, *Health Care Organizations*, to the extent that these principles do not contradict GASB standards.

GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, was adopted by the Medical Center during the fiscal year ended June 30, 2009. This Statement establishes criteria to ascertain whether certain events result in a requirement for the Medical Center to estimate the components of any expected pollution remediation costs and determine whether these costs should be accrued as a liability or, if appropriate, capitalized. The implementation of Statement No. 49 had no effect on the Medical Center's net assets or changes in net assets for the years ended June 30, 2009 and 2008.

Cash

All University operating entities maximize the returns on their cash balances by investing in a short-term investment pool ("STIP") managed by the Treasurer of The Regents. The Regents are responsible for managing the University's STIP and establishing investment policy, which is carried out by the Treasurer of The Regents.

2. Summary of Significant Accounting Policies (Continued)

Cash (Continued)
Substantially all of the Medical Center's cash is deposited into the STIP. All Medical Center deposits into the STIP are considered demand deposits. Unrealized gains and losses associated with the fluctuation in the fair value of the investments included in the STIP (and predominately held to maturity) are not recorded by each operating entity but are absorbed by the University, as the manager of the pool.

The Medical Center's cash at June 30, 2009 and 2008 was $150,789 and $132,348, respectively. None of these amounts are insured by the Federal Deposit Insurance Corporation.

Interest income is reported as non-operating revenue in the statements of revenues, expenses and changes in net assets.

Additional information on cash and investments can be obtained from the 2008-2009 annual report of the University.

Inventory
The Medical Center's inventory consists primarily of pharmaceuticals and medical supplies which are stated on a first-in, first-out basis at the lower of cost or market.

Prepaid Expenses and Other Assets
The Medical Center's prepaid expenses and other assets are primarily prepayments for pharmaceuticals and medical supplies, rent, equipment and maintenance contracts. Also included in other assets, are joint venture arrangements with various third party entities that include providing bone marrow transplantation services and ambulatory surgery services of which the Medical Center does not have control of its activities.

Capital Assets
The Medical Center's capital assets are reported at cost. Depreciation is recorded on a straight-line basis over the estimated useful lives of the assets. Equipment under capital leases is amortized over the shorter period of the lease term or the estimated useful life of the equipment. Lease amortization is included in depreciation and amortization expense. The range of the estimated useful lives for buildings and land improvements is 10 to 40 years and for equipment is 3 to 20 years. Interest on borrowings and imputed interest on excess operating funds used to finance facilities is capitalized during construction. University guidelines mandate that land purchased with Medical Center funds be recorded as an asset of the Medical Center. Land utilized by the Medical Center but purchased with other sources of funds is recorded as an asset of the University. Incremental costs, including salaries and employee benefits, directly related to the acquisition, development and installation of major software projects are included in the cost of the capital assets.

2. Summary of Significant Accounting Policies (Continued)

Deferred Costs of Issuance
Costs incurred in the issuance of long-term debt, including legal fees, bank fees, and accounting and consulting costs have been capitalized and are being amortized as interest expense on the straight-line basis over the term of the related long-term debt, which approximates the effective interest method.

Bond Premium
The premium received in the issuance of long-term debt is amortized as a reduction to interest expense over the term of the related long-term debt.

Net Assets
Net assets are required to be classified for accounting and reporting purposes in the following categories:

- Invested in capital assets, net of related debt – Capital assets, net of accumulated depreciation, reduced by outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

- Restricted – The Medical Center classifies net assets resulting from transactions with purpose restrictions as restricted net assets until the resources are used for the specific purpose or for as long as the provider requires the resources to remain intact.

    - Nonexpendable – Net assets subject to externally imposed restrictions that must be retained in perpetuity by the Medical Center.

    - Expendable – Net assets whose use by the Medical Center is subject to externally imposed restrictions that can be fulfilled by actions of the Medical Center pursuant to those restrictions or that expire by the passage of time.

- Unrestricted – Net assets that are neither restricted nor invested in capital assets, net of related debt. Unrestricted net assets may be designated for specific purposes by management or The Regents. Substantially all unrestricted net assets are allocated for operating initiatives, programs, or for capital programs.

Revenues and Expenses
Revenues received in conducting the programs and services of the Medical Center are presented in the financial statements as operating revenue.

2. Summary of Significant Accounting Policies (Continued)

Revenues and Expenses (Continued)
Operating revenue includes net patient service revenue reported at the estimated net realizable amounts from patients, third-party payors including Medicare and Medi-Cal, and others for services rendered, including estimated retroactive audit adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Laws and regulations governing the Medicare and Medi-Cal programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

Substantially all of the Medical Center's operating expenses are directly or indirectly related to patient care activities.

Non-operating revenue and expense includes interest income and expense, and the gain or loss on the disposal of capital assets.

State capital appropriations, health system support, donated assets and other transactions with the University are classified as other changes in net assets.

Retiree Health Benefits Expense
The University established the University of California Retiree Health Benefit Trust ("UCRHBT") to allow certain University locations and affiliates, including the Medical Center, to share the risks, rewards and costs of providing for retiree health benefits and to accumulate funds on a tax-exempt basis under an arrangement segregated from University assets.

The UCRHBT provides retiree health benefits to retired employees of the Medical Center. Contributions from the Medical Center to the UCRHBT are effectively made to a cost-sharing single-employer health plan administered by the University. The Medical Center is required to contribute at a rate assessed each year by the UCRHBT. As a result, the Medical Center's required contributions are recognized as an expense in the statements of revenues, expenses and changes in net assets.

UCRP Benefits Expense
The University of California Retirement Plan ("UCRP") provides retirement benefits to retired employees of the Medical Center. Contributions from the Medical Center to the UCRP are effectively made to a cost-sharing single-employer defined benefit pension plan administered by the University. The Medical Center is required to contribute at a rate assessed each year by the UCRP. As a result, the Medical Center's required contributions, if any, are recognized as an expense in the statements of revenues, expenses and changes in net assets.

2. Summary of Significant Accounting Policies (Continued)

Charity Care

The Medical Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Amounts determined to qualify as charity care are not reported as net patient service revenue. The Medical Center also provides services to other indigent patients under publicly sponsored programs, which may reimburse at amounts less than the cost of the services provided to the recipients. The difference between the cost of services provided to these indigent persons and the expected reimbursement is included in the estimated cost of charity care.

Transactions with the University and University Affiliates

The Medical Center has various transactions with the University and University affiliates. The University, as the primary reporting entity, has at its discretion the ability to transfer cash from the Medical Center at will (subject to certain restrictive covenants or bond indentures) and use that cash at its discretion. The Medical Center records expense transactions where direct and incremental economic benefits are received by the Medical Center. Payments, which constitute subsidies or payments for which the Medical Center does not receive direct and incremental economic benefit, are recorded as health system support in the statements of revenues, expenses and changes in net assets.

Certain expenses are allocated from the University to the Medical Center. Allocated expenses reported as operating expenses in the statements of revenues, expenses, and changes in net assets are management's best estimates of the Medical Center's arms-length payment of such amounts for its market specific circumstances. To the extent that payments to the University exceed an arms-length estimated amount relative to the benefit received by the Medical Center, they are recorded as health system support.

Compensated Absences

The Medical Center accrues annual leave for employees at rates based upon length of service and job classification and compensatory time based upon job classification and hours worked.

Tax Exemption

The Regents of the University of California is a California public corporation qualified as a tax-exempt organization under the provisions of Section 501(c)(3) of the Internal Revenue Code and is exempt from federal and state income taxes on related income.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Although management believes these estimates and assumptions are reasonable, they are based upon information available at the time the estimate or judgment is made and actual amounts could differ from those estimates.

2. Summary of Significant Accounting Policies (Continued)

New Accounting Pronouncements
In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, effective for the Medical Center's fiscal year beginning July 1, 2009. This statement requires capitalization of identifiable intangible assets in the statements of net assets and provides guidance for amortization of intangible assets unless they are considered to have an indefinite useful life.

In June 2008, the GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments,* also effective for the Medical Center's fiscal year beginning July 1, 2009. This Statement requires the Medical Center to report its derivative instruments at fair value. Changes in fair value for effective hedges that are achieved with derivative instruments are to be reported as deferrals in the statements of net assets. Derivative instruments either do not meet the criteria for an effective hedge or are associated with investments that are already reported at fair value are to be classified as investment derivative instruments. Changes in fair value of those derivative instruments are to be reported as investment revenue.

The Medical Center has determined that implementation of Statements No. 51 and 53 will not have a significant effect on its financial statements.

3. Net Patient Service Revenue

The Medical Center has agreements with third-party payors that provide for payments at amounts different from the Medical Center's established rates. A summary of the payment arrangements with major third-party payors follows:

- ***Medicare*** – Medicare patient revenues include traditional reimbursement under Title XVIII of the Social Security Act (non-risk).

  Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient non-acute services, certain outpatient services and medical education costs related to Medicare beneficiaries are paid based, in part, on a cost reimbursement methodology. Medicare reimburses hospitals for covered outpatient services rendered to its beneficiaries by way of an outpatient prospective payment system based on ambulatory payment classifications. The Medical Center does not believe that there are significant credit risks associated with the Medicare program.

3. Net Patient Service Revenue (Continued)

The Medical Center is reimbursed for cost reimbursable items at a tentative rate with final settlement of such items determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. The Medical Center's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization. The Medical Center's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2002. The fiscal intermediary is in the process of conducting their audits of the 2003 and subsequent cost reports. The results of these audits have yet to be finalized and any amounts due to or from Medicare have not been determined. Estimated receivables and payables related to all open cost reporting periods are included on the statements of net assets as third-party payor settlements.

- ***Medi-Cal*** – The Medicaid program is referred to as Medi-Cal in California. Medi-Cal fee-for-service ("FFS") inpatient hospital payments are made in accordance with the federal Medicaid hospital financing waiver and State of California Senate Bill 1100 ("SB 1100"). Medi-Cal Outpatient FFS services are reimbursed based on a fee schedule. SB 1100 also allows the Medical Center to receive additional waiver growth funding subject to the availability of funds. The total payments made to the Medical Center under SB 1100 will include a combination of Medi-Cal inpatient FFS payments, Medi-Cal Disproportionate Share ("DSH") payments, and Safety Net Care Pool ("SNCP"). For the year ended June 30, 2009 and 2008, the Medical Center recorded total Medi-Cal revenue of $185,605 and $158,636, respectively.

- ***Assembly Bill 915*** – State of California Assembly Bill ("AB") 915, *Public Hospital Outpatient Services Supplemental Reimbursement Program*, provides for supplemental reimbursement equal to the federal share of unreimbursed facility costs incurred by public hospital outpatient departments. This supplemental payment covers only Medi-Cal fee-for-service outpatient services. The supplemental payment is based on each eligible hospital's certified public expenditures ("CPE"), which are matched with federal Medicaid funds. For the years ended June 30, 2009 and 2008, the Medical Center recorded revenue of $15,116 and $8,886 respectively.

- ***Senate Bill 1732*** – State of California Senate Bill 1732 ("SB 1732") provides for supplemental Medi-Cal reimbursement to disproportionate share hospitals for costs (i.e., principal and interest) of qualified patient care capital construction. For the years ended June 30, 2009 and 2008, the Medical Center applied for and received additional revenue of $1,950 and $1,950, respectively. The amounts received are related to the reimbursement of costs for certain debt financed construction projects based on the Medical Center's Medi-Cal utilization rate.

(Dollars in thousands)

3. Net Patient Service Revenue (Continued)

- ***Other*** – The Medical Center has entered into agreements with numerous non-government third-party payors to provide patient care to beneficiaries under a variety of payment arrangements. These include arrangements with:
  - Commercial insurance companies that reimburse the Medical Center for reasonable and customary charges. Workers' compensation plans pay negotiated rates and are reported as contract (discounted or per-diem) revenue.
  - Managed care contracts such as those with HMO's and PPO's that reimburse the Medical Center at contracted or per-diem rates, which are usually less than full charges.
  - Counties in the state of California that reimburse the Medical Center for certain indigent patients covered under county contracts.

The most common payment arrangement for inpatient services is a prospectively determined per-diem rate. The most common payment arrangement for outpatient care is a prospective payment system that uses ambulatory payment classifications.

Amounts due from Medicare and Medi-Cal represent 17 percent and 18 percent of net patient accounts receivable at June 30, 2009 and 2008, respectively.

For the years ended June 30, 2009 and 2008, net patient service revenue included $0.7 million and $9.6 million, respectively, due to cost report settlements with Medicare, Medi-Cal and the County Medical Services Program.

Net patient service revenue by major payor for the years ended June 30 is as follows:

	2009	2008
Medicare (non-risk)	$ 159,861	$ 147,494
Medi-Cal (non-risk)	185,605	158,636
Commercial	10,704	10,139
Contract (discounted or per diem)	384,657	355,877
County	21,598	21,078
Non-sponsored/self-pay	8,254	9,055
Total	$ 770,679	$ 702,279

(Dollars in thousands)

4. Charity Care

Information related to the Medical Center's charity care for the years ended June 30 is as follows:

	2009	2008
Charity care at established rates	$ 84,687	$ 78,929
Estimated cost of charity care	$ 23,451	$ 23,538

Estimated cost in excess of reimbursement for indigent patients under publicly sponsored programs was $13,369 and $14,028 for the years ended June 30, 2009 and 2008, respectively.

5. Capital Assets

The Medical Center's capital asset activity for the years ended June 30 is as follows:

	2007	Additions	Disposals	2008	Additions	Disposals	2009
Original Cost							
Land	$ 4,550	$ –	$ –	$ 4,550	$ –	$ –	$ 4,550
Buildings and improvements	374,836	7,715	–	382,551	11,586	(101)	394,036
Equipment	114,023	16,580	(5,994)	124,609	25,132	(7,507)	142,234
Construction in progress	38,691	47,947	(639)	85,999	81,328	–	167,327
Capital assets, at cost	$ 532,100	$ 72,242	$ (6,633)	$ 597,709	$ 118,046	$ (7,608)	$ 708,147
	2007	**Depreciation**	**Disposals**	**2008**	**Depreciation**	**Disposals**	**2009**
Accumulated Depreciation and Amortization							
Buildings and improvements	$ 149,648	$ 14,606	$ –	$ 164,254	$ 15,325	$ (101)	$ 179,478
Equipment	63,263	12,992	(5,621)	70,634	14,438	(7,208)	77,864
Accumulated depreciation and amortization	$ 212,911	$ 27,598	$ (5,621)	$ 234,888	$ 29,763	$ (7,309)	$ 257,342
Capital assets, net	$ 319,189			$ 362,821			$ 450,805

Equipment under capital lease obligations and related accumulated amortization is $19,065 and $10,196 in 2009, respectively, and $18,079 and $6,982 in 2008, respectively.

The University has acquired certain facilities and equipment under capital leases with the State of California Public Works Board. These facilities and equipment were contributed at cost by the University to the Medical Center to support the operations of the Medical Center. Principal and interest payments required under the leases are the obligations of the University and are not reflected in the financial statements of the Medical Center.

(Dollars in thousands)

5. Capital Assets (Continued)

The Medical Center is currently making seismic improvements in order to be in compliance with Senate Bill 1953, the *Hospital Facilities Seismic Safety Act*. A portion of the improvements will be financed under a lease revenue bond with the State of California Public Works Board. These amounts totaling $16,340 and $8,441 for the years ended June 30, 2009 and 2008, respectively, are included in Transfers from University for building program on the statements of revenues, expenses and changes in net assets.

6. Long-term Debt and Capital Leases

The Medical Center's outstanding debt at June 30 is as follows:

	2009	2008
University of California Medical Center Pooled Revenue Bonds 2007 Series A, interest rates ranging from 4.5 percent to 5.0 percent, payable semi-annually, with annual principle payments beginning in 2012 through 2047	$ 19,230	$ 19,230
University of California Hospital Revenue Bonds 2000, interest rates from 4.125 percent to 10 percent, payable semi-annually, with annual principal payments through 2019	47,935	51,195
University of California General Revenue Bonds 2003 Series B, interest rates from 2.0 percent to 5.25 percent, payable semi-annually, with annual principal payments through 2023	13,641	14,518
University of California Commercial Paper Program, interim financing for construction through the University of California	34,314	–
Capital lease obligations, primarily for computer and medical equipment, with fixed interest rates of 3.28 percent to 7.79 percent, payable through February 2010, collateralized by underlying equipment	9,893	13,498
Unamortized bond premium	1,131	1,223
Total debt and capital leases	126,144	99,664
Less: Current portion of debt and capital leases	(43,157)	(8,515)
Noncurrent portion of debt and capital leases	$ (82,987)	$ 91,149

(Dollars in thousands)

6. Long-term Debt and Capital Leases (Continued)

The activity with respect to current and noncurrent debt for the years ended June 30 is as follows:

	Revenue Bonds	Capital Lease Obligations	Commercial Paper	Total
Year Ended June 30, 2009				
Current portion at June 30, 2008	$ 4,229	$ 4,286	$ –	$ 8,515
Reclassification from noncurrent	4,402	4,745	34,314	43,461
Principal payments	(4,136)	(4,590)	–	(8,726)
Amortization of bond premium	(93)	–	–	(93)
Current portion at June 30, 2009	$ 4,402	$ 4,441	$ 34,314	$ 43,157
Noncurrent portion at June 30, 2008	$ 81,937	$ 9,212	$ –	$ 91,149
New obligations	–	985	34,314	35,299
Reclassification to current	(4,402)	(4,745)	(34,314)	(43,461)
Noncurrent portion at June 30, 2009	$ 77,535	$ 5,452	$ –	$ 82,987
Year Ended June 30, 2008				
Current portion at June 30, 2007	$ 4,064	$ 3,347	$ –	$ 7,411
Reclassification from noncurrent	4,229	4,287	–	8,516
Principal payments	(3,971)	(3,348)	–	(7,319)
Amortization of bond premium	(93)	–	–	(93)
Current portion at June 30, 2008	$ 4,229	$ 4,286	$ –	$ 8,515
Noncurrent portion at June 30, 2007	$ 86,166	$ 9,108	$ –	$ 95,274
New obligations	–	4,391	–	4,391
Reclassification to current	(4,229)	(4,287)	–	(8,516)
Noncurrent portion at June 30, 2008	$ 81,937	$ 9,212	$ –	$ 91,149

Medical Center Pooled Revenue Bonds are issued to provide financing to the University's medical centers and are collateralized by a joint and several pledge of the operating revenues, as defined in the indenture, of all five of the University's medical centers. The Medical Center Pooled Revenue Bond indenture requires the medical centers to set rates, charges and fees each year sufficient for the medical center operating revenues to pay for the annual principal and interest on the bonds and certain other financial covenants. Total Medical Center Pooled Revenue Bonds outstanding at June 30, 2009 are $1.04 billion of which $19,230 are specifically for capital projects at the Medical Center. Combined operating revenues of the University's five medical centers for the years ended June 30, 2009 and 2008 were $5.56 billion and $5.0 billion, respectively.

6. Long-term Debt and Capital Leases (Continued)

In January 2007, Medical Center Pooled Revenue Bonds totaling $19,230 were issued specifically for the Medical Center to refinance a portion of the UCSD Cancer Center construction costs. Proceeds, including a bond premium of $243, were used to pay for issuance costs and repay interim commercial paper financing prior to the issuance of the bonds. The bonds require interest only payments through November 2011, mature at various dates through 2047 and have a weighted average interest rate of 4.55 percent.

University of California Hospital Revenue Bonds have also financed certain improvements at the Medical Center. The Hospital Revenue Bonds are collateralized solely by revenues of the Medical Center. Under the bond indenture, the Medical Center is required to maintain a debt service coverage ratio of not less than 1.2 and between 1.2 and 2.0 depending upon various circumstances, and has limitations as to additional borrowings, the purchase or sale of business assets and the disposition of liquid assets.

General Revenue Bonds Series 2003, collateralized solely by general revenues of the University, finance certain Medical Center projects. The Medical Center is charged for its proportional share of total principal and interest payments made on the General Revenue Bonds pertaining to Medical Center projects.

Medical Center revenues are not pledged for any other purpose than under the indentures for the Medical Center Pooled Revenue Bonds and specific Hospital Revenue Bonds. The pledge of medical center revenues under Medical Center Pooled Revenue Bonds is on a parity with interest rate swap agreements under the obligated group arrangement and subordinate to the Hospital Revenue Bonds. The Medical Center's obligations under the terms of the General Revenue Bonds are subordinate to the Medical Center Pooled Revenue Bonds.

The University has an internal working capital program which allows the Medical Center to receive internal advances up to 60 percent of the Medical Center's accounts receivable for any working capital needs. Interest on any such advance is based upon the earnings rate on the STIP. Repayment of any advances made to the Medical Center under the working capital program is not collateralized by a pledge of revenues. Currently, there are no advances to the Medical Center. The University may cancel or change the terms of the working capital program at its sole discretion. However, the University has historically provided working capital advances under informal or formal programs for the Medical Center.

(Dollars in thousands)

6. Long-term Debt and Capital Leases (Continued)

Future Debt Service

Future debt service payments for each of the five fiscal years subsequent to June 30, 2009 and thereafter are as follows:

Year Ending June 30,	Revenue Bonds	Capital Lease Obligations	Commercial Paper	Total Payments	Principal	Interest
2010	$ 8,179	$ 4,720	$ 34,314	$ 47,213	$ 43,064	$ 4,149
2011	8,174	2,960	–	11,134	7,304	3,830
2012	8,372	1,770	–	10,142	6,615	3,527
2013	8,365	965	–	9,330	6,099	3,239
2014	8,059	–	–	8,059	5,107	2,952
2015 – 2019	40,179	–	–	40,179	29,640	10,539
2020 – 2024	16,187	–	–	16,187	11,699	4,488
2025 – 2029	5,481	–	–	5,481	2,155	3,326
2030 – 2034	5,484	–	–	5,484	2,715	2,769
2035 – 2039	5,482	–	–	5,482	3,385	2,097
2040 – 2044	5,479	–	–	5,479	4,215	1,264
2045 – 2048	3,290	–	–	3,290	3,015	275
Total future debt service	122,731	10,415	34,314	167,460	$ 125,013	$ 42,447
Less: Interest component of future payments	(41,925)	(522)	–	(42,447)		
Principal portion of future payments	80,806	9,893	34,314	125,013		
Adjusted by:						
Unamortized bond premium	1,131	–	–	1,131		
Total debt	$ 81,937	$ 9,893	$ 34,314	$ 126,144		

Additional information on the revenue bonds can be obtained from the 2008-2009 annual report of the University.

(Dollars in thousands)

7. Operating Leases

The Medical Center leases buildings and equipment under agreements recorded as operating leases. Operating lease expense for the years ended June 30, 2009 and 2008 was $4,581 and $4,144, respectively. The terms of the operating leases extend through the year 2016.

Future minimum payments on operating leases with an initial or non-cancelable term in excess of one year are as follows:

Year Ending June 30,	Minimum Annual Lease Payments
2010	$ 4,712
2011	3,546
2012	2,964
2013	2,464
2014	1,962
2015-2016	3,106
Total	$ 18,754

8. Retiree Health Plans

The University administers single-employer health plans to provide health and welfare benefits, primarily medical, dental and vision benefits, to eligible retirees of the University of California and its affiliates. The Regents have the authority to establish and amend the benefit plans.

The contribution requirements of the eligible retirees and the participating University locations, such as the Medical Center, are established and may be amended by the University. Membership in the UCRP is required to become eligible for retiree health benefits. Contributions toward benefits are shared with the retiree. The University determines the employer's contribution. Retirees are required to pay the difference between the employer's contribution and the full cost of the health insurance. Retirees employed by the Medical Center prior to 1990 are eligible for the maximum employer contribution if they retire before age 55 and have at least 10 years of service, or if they retire at age 55 or later and have at least 5 years of service. Retirees employed by the Medical Center after 1989 and not rehired after that date are subject to graduated eligibility provisions that generally require 10 years of service before becoming eligible for 50 percent of the maximum employer contribution, increasing to 100 percent after 20 years of service.

Participating University locations, such as the Medical Center, are required to contribute at a rate assessed each year by the UCRHBT. The contribution requirements are based upon projected pay-as-you-go financing requirements. The assessment rates were $3.09, $2.86 and $2.75 per $100 of UCRP covered payroll resulting in Medical Center contributions of $7,800, $6,400 and $5,600 for the years ended June 30, 2009, 2008 and 2007, respectively.

8. Retiree Health Plans (Continued)

The actuarial value of UCRHBT assets and the actuarial accrued liability associated with the University's campuses and medical centers using the entry age normal cost method as of July 1, 2008, the date of the latest actuarial valuation, were $51,221 and $13.30 billion, respectively. The net assets held in trust for pension benefits on the UCRHBT's Statement of Plan Fiduciary Net assets were $74,370 at June 30, 2009. For the years ended June 30, 2009 and 2008, combined contributions from the University's campuses and medical centers were $278,507 and $268,102, respectively, including an implicit subsidy of $44,079 and $43,036, respectively. The University's annual retiree health benefit expense for its campuses and medical centers was $1.50 billion and $1.36 billion for the years ended June 30, 2009 and 2008. As a result of contributions that were less than the retiree health benefit expense, the University's obligation for retiree health benefits attributable to its campuses and medical centers totaling $2.31 billion at June 30, 2009 increased by $1.23 billion and $1.09 billion for the years ended June 30, 2009 and 2008, respectively.

Information related to plan assets and liabilities as they relate to individual campuses and medical centers is not readily available. Additional information on the retiree health plans can be obtained from the 2008–2009 annual reports of the University of California and the University of California Health and Welfare Program.

9. Retirement Plans

Substantially all full-time employees of the Medical Center participate in the University of California Retirement System ("UCRS") that is administered by the University. The UCRS consists of The University of California Retirement Plan ("UCRP"), a single employer defined benefit plan, and the University of California Retirement Savings Program ("UCRSP") that includes four defined contribution plans with several investment portfolios generally funded with employee non-elective and elective contributions. The Regents has the authority to establish and amend the benefit plans.

The UCRP provides lifetime retirement income, disability protection, and survivor benefits to eligible employees. Benefits are based on average highest three years compensation, age, and years of service and are subject to limited cost-of-living increases.

Contributions to the UCRP may be made by the Medical Center and the employees. The rates for contributions as a percentage of payroll are determined annually pursuant to The Regents' funding policy and based upon recommendations of the consulting actuary. The Regents determine the portion of the total contribution to be made by the Medical Center and by the employees. Employee contributions by represented employees are subject to collective bargaining agreements. As a result of the funded status of the UCRP, during the years ended June 30, 2009 and 2008, there were no required Medical Center or employee contributions.

9. Retirement Plans (Continued)

The actuarial value of UCRP assets and the actuarial accrued liability associated with the University's campuses and medical centers using the entry age normal cost method as of July 1, 2008, the date of the latest actuarial valuation, were $35.61 billion and $34.45 billion, respectively, resulting in a funded ratio of 103.4 percent.. The net assets held in trust for pension benefits on the UCRP Statement of Plan's Fiduciary Net assets were $32.26 billion and $42.02 billion at June 30, 2009 and 2008, respectively.

The University utilizes asset allocation strategies that are intended to optimize the UCRP's investment returns over time in accordance with investment objectives and at acceptable levels of risk. However, the financial markets, both domestically and internationally, deteriorated subsequent to July 1, 2008. As a result, the funded ratio as of July 1, 2009 actuarial valuation for the campuses and medical centers is approximately 94.8 percent.

For the years ended June 30, 2009 and 2008, the University's campuses and medical centers contributed a combined $442 and $2,657, respectively. The University's annual UCRP benefits expense for its campuses and medical centers was $69,131 for the year ended June 30, 2009. As a result of contributions that were less than the UCRP benefits expense, the University's obligation for UCRP benefits attributable to its campuses and medical centers increased by $68,696 for the year ended June 30, 2009. For the year ended June 30, 2008, contributions from the University's campuses and medical centers was equivalent to the annual UCRP benefits expense. As a result, there was no obligation for UCRP benefits at June 30, 2008.

The UCRSP plans (DC Plan, Supplemental DC Plan, 403(b) Plan and 457(b) Plan) provide savings incentives and additional retirement security for all eligible employees. The DC Plan accepts both pre-tax and after-tax employee contributions. The Supplemental DC Plan accepts employer contributions on behalf of certain qualifying employees. The 403(b) and 457(b) plans accept pre-tax employee contributions and the Medical Center may also make contributions on behalf of certain members of management. Benefits from the plans are based on participants' mandatory and voluntary contributions, plus earnings, and are immediately vested.

Information related to plan assets and liabilities as they relate to individual campuses and medical centers is not readily available. Additional information on the retirement plans can be obtained from the 2008–2009 annual reports of the University of California Retirement Plan, the University of California Retirement Savings Plan and the University of California PERS–VERIP.

(Dollars in thousands)

10. University Self-insurance

The Medical Center is insured through the University's malpractice, general liability, workers' compensation, and health and welfare self-insurance programs. All operating departments of the University are charged premiums to finance the workers' compensation and health and welfare programs. The University's medical centers are charged premiums to finance the malpractice insurance. All claims and related expenses are paid from the University's self-insurance funds. Such risks are subject to various per claim and aggregate limits, with excess liability coverage provided by an independent insurer.

Workers' compensation premiums, included as salaries and employee benefits expense in the statements of revenues, expenses and changes in net assets, were $629 and $864 for the years ended June 30, 2009 and 2008, respectively. During 2009 and 2008, as a result of actuarial analysis, the Medical Center received a refund of premiums from the University of $5,812 and $7,144, respectively, that reduced the overall workers' compensation cost for the year.

Combined malpractice and general liability premiums, recorded as insurance expense in the statements of revenues, expenses and changes in net assets, were $5,560 and $4,806 for the years ended June 30, 2009 and 2008, respectively.

11. Transactions with Other University Entities

Services purchased from the University include office and medical supplies, building maintenance, repairs and maintenance, administrative, treasury, medical services, and insurance. Services provided to the University include physician office rentals, pharmaceuticals, billing services, medical supplies and cafeteria services. Such amounts are netted and included in the statements of revenues, expenses and changes in net assets for the years ended June 30 as follows:

	2009	2008
Salaries and employee benefits	$ 2,570	$ 2,584
Professional services	30,054	26,169
Medical supplies	(1,029)	(909)
Other supplies and purchased services	(10,234)	(8,411)
Interest income (net)	(5,446)	(4,365)
Insurance	5,560	4,806
Total	$ 21,475	$ 19,874

11. Transactions with Other University Entities (Continued)

Additionally, the Medical Center makes payments to the University of California, San Diego School of Medicine ("School of Medicine"). Services purchased from the School of Medicine include physician services that benefit the Medical Center, such as emergency room coverage, physicians providing medical direction to the Medical Center, and the Medical Center's allocation of malpractice insurance. Such expenses are reported as operating expenses in the statements of revenue, expenses and changes in net assets. Health system support includes amounts paid by the Medical Center to fund School of Medicine operating activities, payments to support clinical research, transfers to faculty practice plans, as well as other payments made to support various School of Medicine programs.

The total net amount of payments made by the Medical Center to the School of Medicine were $53,382 and $51,171 in 2009 and 2008, respectively. Of these amounts, $21,475 and $19,874 are reported as operating expenses for the years ended June 30, 2009 and 2008, respectively, and $32,907 and $31,297 are reported as health system support for the years ended June 30, 2009 and 2008, respectively.

12. State Funds for Capital Acquisitions

The 2000 State Budget Act provided $50 million in state capital appropriations for non-seismic capital improvement (i.e., infrastructure) projects at the University's medical centers. The Medical Center was allocated $25 million of the $50 million state capital appropriation. During fiscal years 2009 and 2008, $1,918 and $3,453, respectively, was expended and received by the Medical Center and reflected as a state capital appropriation in the statements of revenues, expenses and changes in net assets.

13. Commitments and Contingencies

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. Compliance with these laws and regulations is subject to periodic government review, interpretation and audits, as well as regulatory actions unknown and unasserted at this time.

The University is contingently liable in connection with certain claims and contracts, including those currently in litigation, arising out of the normal course of its activities. Management and General Counsel are of the opinion that the outcome of such matters will not have a material effect on the financial statements.

13. Commitments and Contingencies (Continued)

State of California Senate Bill 1953, *Hospital Facilities Seismic Safety Act*, specifies certain requirements that must be met within a specified time in order to increase the probability that the hospital could maintain uninterrupted operations following major earthquakes. The Medical Center has received an extension to January 1, 2013 to complete the required renovations. By January 1, 2030, all general acute care inpatient buildings must be operational after an earthquake. Previously, the State of California's budget authorized the University to use $600,000 in lease-revenue bond funds for earthquake safety renovations. The Regents have approved the allocation of the $600,000 among the University's medical centers, of which $40,000 was allocated to the Medical Center. The Medical Center spent $16,340 and $8,441 of its allocation during the years ended June 30, 2009 and 2008, respectively, recorded in the statements of revenues, expenses and changes in net assets as a Transfer from University. As of June 30, 2009, any repayment the Medical Center may be obligated for, under these financing arrangements, is still being determined.

The Medical Center has entered into various construction contracts. The remaining cost of these Medical Center projects is estimated to be approximately $208,000, excluding interest, as of June 30, 2009.