Basic Financial Statements, Required Supplementary Information, and Other Financial Information

University Health System
Bexar County, Texas
Years Ended December 31, 2010 and 2009
With Report of Independent Auditors

Ernst & Young LLP

Ernst & Young

University Health System
Bexar County, Texas

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Years Ended December 31, 2010 and 2009

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Report of Independent Auditors

The Board of Managers
University Health System
San Antonio, Texas

We have audited the accompanying basic financial statements of the Bexar County Hospital District d/b/a University Health System (the System), a component unit of Bexar County, Texas, and its discretely presented component units, as of December 31, 2010 and 2009, and for the years then ended, which collectively comprise the System's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of the University Health System Pension Plan (the Pension Plan), a discretely presented component unit of the System. Those financial statements were audited by other auditors, whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Pension Plan, is based on the report of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the System's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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 and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Bexar County Hospital District d/b/a University Health System and its discretely presented component units as of December 31, 2010 and 2009, and the respective changes in financial position and, where applicable, cash flows, thereof for the years then ended, in conformity with accounting principles generally accepted in the United States.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 8, 2011, on our consideration of the System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Management's discussion and analysis on pages iii through xiv and the schedule of funding progress for the University Health System Retiree Health Trust on page 44 are 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 consisted 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.

The accompanying schedule of expenditures of federal and state awards on pages 45 through 48 is presented for purposes of additional analysis, as required by OMB Circular A-133, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Ernst & Young LLP

June 8, 2011

Required Financial Statements

The basic financial statements report information using Governmental Accounting Standards Board (GASB) accounting principles. The basic financial statements include the financial statements of the Bexar County Hospital District d/b/a University Health System (the System), the University Health System Pension Plan (the Plan), and the University Health System Retiree Health Trust (the OPEB Trust). The Plan's audited financial statements are available at the System's offices in San Antonio, Texas. The System's basic financial statements offer short-term and long-term financial information about its activities. The balance sheet includes all of the System's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to System creditors and bond holders (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of the System, and assessing the liquidity and financial flexibility of the System. All of the current year's revenues and expenses are accounted for in the statement of revenue, expenses, and changes in net assets. This statement measures changes in the System's operations over the past two years and can be used to determine whether the System has been able to recover all of its costs through its ad valorem taxes (property taxes) provided, patient service revenue, and other revenue sources. The final required financial statement is the statement of cash flows. The primary purpose of this statement is to provide information about the System's cash from operations, investing, and financing activities and to provide answers to such questions as where did cash come from, what was cash used for, and what was the change in cash balance during the reporting period.

Management's Discussion and Analysis

Financial Highlights

- The System's net assets increased by $58.9 million (8.8%) and $58.2 million (9.5%) in 2010 and 2009, respectively, given the results of operating and nonoperating activities.

- During 2010, the System's total operating revenue increased by $9.4 million or 1.4%, while expenses increased by $25.2 million or 2.8%.

- During 2009, the System's total operating revenue increased by $59.5 million or 9.8%, while expenses increased by $64.8 million or 7.9%.

- During 2010 and 2009, the System made the following significant capital acquisitions:

2010	2009
• Purchase and remodeling of Diagnostic Pavilion building and relocation of UH ExpressMed Clinic to the Diagnostic Pavilion • Relocation and remodeling	• Bi-Plane Cardiac Cath Lab and uninterrupted power source • South Dialysis Clinic, equipment and dialysis machines • Chilled water expansion

2010

costs for the UH Outpatient Dialysis Unit move to 7540 Louis Pasteur

- Northwest clinic relocation and remodeling at 7726 Louis Pasteur
- Information systems virtualization project consolidation of servers
- Operating room equipment, surgical tables, endoscopic/laparoscopic units/scopes
- Interim staff parking lot
- Phone switch (VOIP) for CMA clinics
- Par Excellence UH Inventory System and Central Supply renovations
- Server storage, upgrades, data integration, wireless technology and patient portal
- Radiology equipment, voice recognition software system and X-Ray and ultrasound machines

2009

- System wide EMR
- PACS storage system Echocardiography system
- Server storage, software licenses and upgrades, hardware and fiber optic interfaces
- Administrative offices and information services relocation
- Pathology equipment, scopes, sonograms, ventilators, and monitors
- Digital imaging system for UHC-Downtown

The source of the funding for these projects was derived from operations and from funds designated for capital acquisitions and improvements.

In 2010, significant progress was made on the Capital Improvement Program (CIP). Achievements at the UH Campus include completion of a temporary remote parking lot for employees and commencement of construction for a new parking garage; relocation of the MRI Department and Express Med Clinic; commencement of construction for a new Heliport and enhanced site utilities; and partial demolition of the 1987 Building. Achievements at the Robert B. Green Campus include completion of a new parking lot; upgrades to the existing employee parking lot; and groundbreaking for the new Clinical Services Building.

In 2009, significant progress was made on the implementation of the CIP. The focus was on: securing contracts for the lead program manager; securing the Architect and

Engineer for the University Hospital (UH) and UHC-Downtown projects; the Central Plant consulting and design and the Project managers for both the UH and UHC-Downtown campuses; and key specialty consultants for food services, material handling, and distribution.

The primary source of the funding for these projects was from bond proceeds.

Financial Analysis of the System

The balance sheets and the statements of revenue, expenses, and changes in net assets report information about the System's financial activities. These two statements report the net assets of the System and changes in them. Increases or decreases in the System's net assets are one indicator of whether its financial health is improving or deteriorating. However, other nonfinancial factors such as changes in economic conditions, population growth, growth in the number of uninsured and working poor, taxable property values and tax rates, and new or changed state and federal government funding should also be considered.

Net Assets

A summary of the System's balance sheets is presented in Table 1 as follows:

TABLE 1
Condensed Balance Sheets
(In Millions)

	December 31		
	2010	**2009**	**2008**
Current and other assets	**$ 1,545**	$ 1,401	$ 1,075
Capital assets	**366**	250	226
Total assets	**$ 1,911**	$ 1,651	$ 1,301
Long-term debt outstanding	**$ 745**	$ 553	$ 276
Other liabilities	**437**	428	413
Total liabilities	**$ 1,182**	$ 981	$ 689
Invested in capital assets, net of related debt	**$ 223**	$ 218	$ 226
Restricted	**2**	1	1
Unrestricted	**504**	451	385
Total net assets	**$ 729**	$ 670	$ 612

As can be seen in Table 1, net assets increased by $59 million to $729 million in fiscal year 2010, up from $670 million in fiscal year 2009. Net assets increased by $58 million to $670 million in fiscal year 2009, up from $612 million in fiscal year 2008. The change in net assets results primarily from positive increases in nonoperating revenue over losses from operations.

During 2010, the System obtained approval from the Bexar County Commissioners Court for the third and final debt issuance, which consisted of a Series B Certificates of Obligation, Taxable Direct Subsidy Build America Bonds (BABs) in the amount of $204.9 million as detailed in Note 7 to the financial statements. The System obtained credit ratings from three rating services. Fitch Ratings increased the rating to AAA from AA+, Moody's Investor Services, Inc. increased the rating to Aal from Aa2, and Standard & Poor's Ratings Services remained the same at AA+.

During 2009, the System obtained approval from the Bexar County Commissioners Court for a second debt issuance, which consisted of a Series A tax exempt Certificates of Obligation in the amount of $36.2 million and a Series B Certificates of Obligation, Taxable Direct Subsidy Build America Bonds in the amount of $246.4 million as detailed in Note 7 to the financial statements. The System obtained ratings of AA+ from Fitch Ratings, Aa2 from Moody's Investor Services, Inc. and an increase to AA+ from the previous AA rating in 2008 from Standard & Poor's Ratings Services.

Summary of Revenue, Expenses, and Changes in Net Assets

The following table presents a summary of the System's historical revenues and expenses for each of the fiscal years ended December 31, 2010, 2009, and 2008:

TABLE 2
Condensed Statements of Revenue, Expenses, and Changes in Net Assets
(In Thousands)

	Year Ended December 31		
	2010	**2009**	**2008**
Net patient service revenue	**$ 360,380**	$ 366,257	$ 339,017
Premium revenue	**268,562**	258,007	224,605
Other operating revenue	**47,606**	42,828	44,014
Total operating revenue	**676,548**	667,092	607,636
Maintenance and operation expenses	**641,085**	616,160	598,030
Medical claims expense	**236,282**	239,552	195,532
Depreciation expense	**37,208**	33,705	31,054
Total operating expenses	**914,575**	889,417	824,616
Operating loss	**(238,027)**	(222,325)	(216,980)
Nonoperating revenue	**296,350**	280,030	250,515
Income before contributions	**58,323**	57,705	33,535
Capital contributions received, net	**549**	516	245
Change in net assets	**58,872**	58,221	33,780
Total net assets – beginning of year	**670,188**	611,967	578,187
Total net assets – end of year	**$ 729,060**	$ 670,188	$ 611,967

Sources of Revenue

Table 3 presents a summary of the System's historical sources of revenue:

TABLE 3
Sources of Revenue by Percentage

	Year Ended December 31		
	2010	**2009**	**2008**
Operating revenue:			
Net patient service revenue	**37.0%**	38.6%	39.5%
Premium revenue	**27.6**	27.3	26.2
Other operating revenue	**4.9**	4.5	5.1
Total operating revenue	**69.5**	70.4	70.8
Nonoperating revenue:			
Property taxes	**28.3**	28.1	25.7
Investment income	**.5**	.5	2.5
Proceeds from tobacco settlement	**.6**	1.0	1.0
Build America Bond interest subsidy	**.9**	–	–
Premium deficiency reserve	**.2**	–	–
Total nonoperating revenue	**30.5**	29.6	29.2
Total revenue	**100.0%**	100.0%	100.0%

Operating Revenue

During fiscal year 2010, the System derived approximately 69.5% of its total revenue from operating revenue, compared to 70.4% in fiscal year 2009. Operating revenue decreased as a percentage of total revenue due to an increase in nonoperating property tax revenue given a higher tax rate to support debt payments. Operating revenue includes, among other items, patient service revenue provided under the Medicare and Medicaid programs, patients or their third-party carriers who pay for care in the System's facilities, health maintenance organization (HMO) premium revenue, Disproportionate Share (DSH)/Upper Payment Limit (UPL) revenue, cafeteria sales, parking fees, grants, research, reimbursement for physician practice and resident expenses, and funds for uncompensated trauma care.

Table 4 presents the relative percentages of gross charges billed for patient services by payor for the fiscal years ended December 31, 2010, 2009, and 2008:

TABLE 4
Payor Mix by Percentage

	Year Ended December 31		
	2010	**2009**	**2008**
Medicare	**19%**	19%	19%
Medicaid	**19**	21	18
Self-pay	**43**	41	44
Commercial insurance	**18**	18	18
Other	**1**	1	1
Total	**100%**	100%	100%

Nonoperating Revenue

During fiscal year 2010, the System derived 28.3% of its total revenue from ad valorem taxes (property taxes), compared to 28.1% in fiscal year 2009. The increase in property tax receipts was due to a tax rate increase in support of the 2010 debt issuance. The Commissioners Court is authorized to levy taxes on property within Bexar County to provide for the maintenance and operations of the System's facilities and for debt service on approved debt issuances.

For the years ended December 31, 2010 and 2009, respectively, investment income comprised .5% and .5% of total revenue and was made up of interest income, net realized gains/losses, and net unrealized market gains/losses. Investment income continued to be a lower percentage of total income due to lower interest rates caused by declines in economic and market conditions.

For the years ended December 31, 2010 and 2009, tobacco revenue comprised .6% and respectively, 1.0%, of total revenue and represented the System's allocation of earnings on the state's permanent trust funds from a settlement with tobacco companies in 1998. The amount allocated to the System in 2010 was $4.2 million or 43% less than the allocated amount in 2009. This was due to lower amounts available for distribution caused by lower investment performance.

For the year ended December 31, 2010, the Build America Bond interest subsidy comprised .9% of total revenue and was made up of the $8.6 million in funds paid by the U.S. Treasury to subsidize interest costs on the BABs bond issuances.

Operating and Financial Performance

The following summarizes the System's statements of revenue, expenses, and changes in net assets for the years ended December 31, 2010, and 2009:

Overall activity at the System, as measured by patient discharges adjusted for outpatient activity, decreased 0.8% to 38,408 in 2010 from 38,710 in 2009. The slight decrease in adjusted discharges in 2010 was attributed to capacity constraints at University Hospital. Management continues to address length of stay issues and appropriate use of inpatient beds to improve existing capacity.

The System had patient days of 126,484 in 2010, a decrease of 1.8% from patient days of 128,802 in 2009, and discharges of 20,004, a 3.9% decrease from discharges in 2009 of 20,812.

Hospital outpatient activity in 2010, which includes hospital-based outpatient services, urgent care and other clinics, and emergency visits, was 146,540, an increase of 5.8% above the 2009 level of 138,456. During 2009, hospital outpatient activity increased 10.5% over the 2008 level of 125,249. Clinic visits at the System's community-based clinics were 362,390 in 2010, which represented a 6.7% increase from 2009. In 2009, the community-based clinic's visits increased 2.4% to 339,644 from 331,790 in 2008. In 2010, the preventive health clinics had 45,752 visits, an increase of 85% from 24,727 in 2009.

Net patient service revenue decreased by $5.9 million to $360.4 million in 2010 or 1.6%. Decreases were due to lower revenue from the DSH and UPL programs and lower adjusted discharges. Revenue received under the DSH and UPL programs decreased in 2010 due to the recording in 2009 of a $14.5 million reconciliation for 2008 (see Note 10 to the financial statements). Without this one-time adjustment, DSH and UPL revenue would have reflected an increase due to a temporary rise in the Federal Medical Assistance Percentage (FMAP) rate under the American Recovery and Reinvestment Act.

Net patient service revenue increased by $27.2 million to $366.3 million in 2009 or 8.0%. Increases were due to improvements in revenue collections from commercial insurance contracts, the Care*Link* Plus Program, and Medicaid. Revenue received under the DSH and UPL programs increased in 2009 also due to the temporary rise in the FMAP.

Excluded from net patient service revenue are charges forgone for patient services falling under the System's charity care policy. Based on established rates, gross charges of $412.7 million were forgone during 2010, an 8.1% increase over the prior fiscal year. There was an increase of 13.2% to $381.7 million for charges forgone during 2009. The System diligently pursues payment for medical and hospital services it provides or arranges and actively pursues available funding for patients who present without insurance or other sources of funding. Contributing to the increase in 2010 and 2009 was the overall impact of economic conditions.

The System recognized premium revenue through its not-for-profit HMO subsidiary, Community First Health Plans (CFHP). During 2010, premium revenue increased by $10.6 million to $268.6 million or 4.1%. The increase in premium revenue resulted from increased membership in STAR Medicaid, CHIP, and ERS (state employees) products, offset by lower PPO, commercial, and CHIP Perinate products.

Premium revenue increased by $33.4 million to $258.0 million or 14.9% in 2009. The increase in premium revenue resulted from increased membership in STAR Medicaid, CHIP, and CHIP Perinate products, offset by lower PPO and commercial products.

Other operating revenue of $47.6 million increased by $4.8 million or 11.2% in 2010 from $42.8 million in 2009 due to higher revenue for residents serving other providers, grant revenue, and research revenue.

In 2009, other operating revenue of $42.8 million decreased by $1.2 million or 2.7% due to the net of higher grant revenue and an earned incentive at the CFHP subsidiary and the expiration of the one year inter-local agreement with the city of San Antonio to transfer the clinical preventive health services to the System. Reimbursement for these clinics is now included in the maintenance and operations tax rate.

Overall, total operating revenue of $676.5 million increased by $9.4 million or 1.4% in 2010, compared to the total of $667.1 million, which increased by $59.5 million or 9.8% in 2009.

Maintenance and operation expenses consist of employee compensation, supplies, purchased services, and medical services. Overall maintenance and operation expenses of $641.1 million increased by $24.9 million or 4.0% in 2010, compared to the total of $616.2 million, which increased by $18.2 million or 3.0% in 2009. The discussion of significant variances of each expense category is as follows:

- Employee compensation increased by $10.4 million or 3.6% in 2010 and $8.5 million or 3.0% in 2009. The System increased salaries to employees by $6.3 million in 2010 and $8.0 million in 2009.

  - Increases in 2010 were attributed to an increase in staffing for new grants, such as the Methodist Health Care After-Hours Program at the Northwest Clinic, which opened in August 2010; additional staffing for ambulatory clinics; and staff to support hospital patient care. Management initiatives of improving productivity were expanded to ambulatory areas in addition to inpatient clinical areas, which offset some of these increases. Also contributing were annual merit increases. Employee benefits increased due to higher utilization of the health plan and higher required contributions to the OPEB and Pension plans.

  - Increases in 2009 were attributed to increased staffing for the new South Dialysis Unit, which opened in June 2009; incremental increase of market adjustments for key clinical staff and other specialty occupations; and annual merit increases. Management implemented initiatives to measure and improve productivity in inpatient clinical areas, which offset a portion of these increases. Employee benefits also increased due to annual required contributions for the Pension and OPEB plans.

- Supplies increased by $6.0 million or 5.5% in 2010 and $2.0 million or 1.9% in 2009. Supply costs increased in 2010 due to the implementation of an interventional radiology program, higher costs of surgical implants and medical supplies used in operating rooms, and higher costs of blood and blood products. Management negotiated an agreement to lower blood costs and continues to work with physicians to standardize preference items.

  – In 2009, supplies cost increased due to the higher cost of surgical implants, medical supplies used in operating rooms, and higher costs of blood and blood products. Management implemented processes to reduce the cost of supplies through initiatives to analyze utilization of physician preference items, value analysis programs, and standardization. In 2008, supply costs increased due to the use of high-cost surgical supplies and sutures in the operating and special procedures rooms, and the escalating costs associated with blood products, pathological supplies, and pharmaceuticals.

- Purchased services increased by $5.2 million or 5.2% in 2010 due primarily to higher transplant organ acquisition costs given an increase in the number of transplants, equipment repairs, temporary personnel, and professional services. In 2009, purchased services increased by $2.9 million or 2.9% due primarily to higher maintenance costs for new software and professional services.

- Medical services increased by $3.3 million or 2.9% in 2010 and by $4.3 million or 3.9% in 2009. The increase in 2010 resulted from higher physician costs at CMA to increase the number of primary care physicians and expand specialty services such as neonatology, endocrinology, and behavioral health, and increases for House Staff. These increases were offset by lower costs to the University of Texas Health Science Center at San Antonio (UTHSCSA) physicians for indigent care services that were transferred to affiliated entities under the Regional UPL program. The increase in 2009 resulted from an increase in payments to the UTHSCSA for recruitment and retention and care for indigent patients and increases for House Staff and CMA physicians.

- Other expenses increased by $62,000 in 2010 or 4.0% and by $401,000 in 2009 or 35.2% due to changes in property taxes levied in the respective years that are used as the basis in determining fees paid to the Bexar County Appraisal District to support its operating budget.

Medical claims expense at CFHP decreased by $3.3 million or 1.4% in 2010, and increased by $44.0 million or 22.5% in 2009. The decrease in 2010 resulted from lower at-risk membership and significant initiatives implemented by management to reduce medical care costs. The increase in 2009 was due to higher at-risk membership and a higher member benefit ratio.

Depreciation and amortization expense increased by $3.7 million or 10.4% in 2010 and $2.7 million or 8.5% in 2009 due to a higher level of capital investment and the depreciation of long-term projects placed in service.

Overall, total operating expenses increased by $26.7 million to $916.1 million or 3.0% in 2010 and by $64.8 million to $889.4 million or 7.9% in 2009.

Overall, nonoperating revenue (expense) of $296.4 million increased by $16.4 million or 5.9% from 2009. Nonoperating revenue consists of property tax revenue, investment income, proceeds from the tobacco settlement (the settlement of litigation between the State Attorney General and various tobacco companies), BABs subsidy, and a premium deficiency reserve for CFHP.

- In 2010, property taxes were levied to support maintenance and operations (M&O) and debt service (DS). Overall property taxes increased by $8.4 million to $275.4 million compared to the 2009 taxes of $267.0 million. Of the $275.4 million, $241.9 million was to support maintenance and operations. This was an $8.4 million increase over 2009 and was due to increases in new properties. The remaining $33.5 million increase is a debt service property tax to fund the payment of principal and interest (debt service) on the issuance of Certificates of Obligation in 2008, 2009, and 2010.

- Investment income increased by $0.4 million or 7.7% in 2010 and decreased by $17.0 million or 77.8% in 2009. Investment income in 2010 increased marginally due to higher interest rates. In 2009, investment income decreased due to lower interest rates that resulted from the credit crisis and extreme volatility in the financial markets during those years.

- In fiscal years 2010 and 2009, the System received payments totaling $5.6 million and $9.8 million, respectively, from the Tobacco Settlement distribution. These amounts represent decreases of 43.0% and 18.3%, respectively. The decrease in tobacco funding resulted from the System's pro rata share of earnings on the permanent trust fund.

- The increase in the Build America Bond Interest Subsidy resulted from guidance by the Governmental Accounting Standards Board that the portion of interest paid by the U.S. Treasury should be recognized as nonoperating revenue.

- The Premium Deficiency Reserve of $1.6 million in 2010 was the result of amortizing the expense required by the Texas Department of Insurance for CFHP for projected losses under the CHIP contract in 2009.

Capital contributions in 2010 and 2009 consist of the net of amounts donated to the System for specific programs or projects offset by amounts disbursed in satisfaction of donations made in prior years.

Capital Assets

During fiscal years 2010 and 2009, the System invested by $154.0 million and $57.6 million, respectively, in a broad range of capital assets. Table 5 presents an analysis of capital asset balances between 2008, 2009 and 2010:

TABLE 5
Capital Assets
(In Thousands)

	December 31		
	2010	**2009**	**2008**
Land and land improvements	**$ 9,578**	$ 8,329	$ 7,835
Building and leasehold improvements	**303,759**	277,052	267,881
Equipment	**278,828**	253,005	238,964
	592,165	538,386	514,680
Less accumulated depreciation	**(377,133)**	(339,913)	(309,546)
Construction-in-progress	**151,190**	51,684	21,134
Net capital assets	**$ 366,222**	$ 250,157	$ 226,268

Construction-in-progress increased by $99.5 million in 2010 due to the implementation of the CIP including capitalized interest, architectural and engineering costs, construction costs of the west parking garage and clinical services building as well as management's ongoing focus on replacing and upgrading existing equipment and facilities.

In 2009, net capital assets increased due to the acquisition of new medical technology, clinical information systems, and a new technology building purchased to free up needed clinical long-term space and parking at the hospital campus. The System is in the process of addressing its strategic plans and implementing master facility and financing plans to address near-term initiatives and facility needs.

Economic Factors and Next Year's Budget

The System's Board and management considered many factors when setting the fiscal year 2011 budget. The years 2010 through 2013 are the prelude years to health care reform. As such, the System 2011 Budget will focus on the following strategic initiatives to position itself to be an efficient, high quality, and patient-focused provider of care in the community:

- Reengineer the care process, focusing on quality, evidence-based medicine and provider accountability for the continuum of care;
- Improve the System's capacity to provide care;
- Increase operating efficiencies, using key matrix and benchmarks to track progress;

- Improve alignment between CFHP and the Health System clinical services; and
- Align payment methodology with physician practice and Health Systems aims.

Over the next three years, the System's planning process will continue to address economic conditions such as:

- Health care reform
- Decline in property values
- State legislative budget cuts
- Federal legislative budget cuts
- Impact of interest rates on invested funds
- Costs of supplies and new technology
- Possible impact of Medicare RAC initiatives

The main objective of this planning process is to ensure that strategic issues identified are addressed to advance the financial and operational position in the future so that the System can successfully carry out its important mission.

Contacting the System's Financial Manager

This financial report is designed to provide our citizens, customers, bond holders, and creditors with a general overview of the System's finances and to demonstrate the System's accountability for the money it receives. The report is available at www.UniversityHealthSystem.com. If you have questions about this report or need additional financial information, contact the University Health System's Financial Offices, 4502 Medical Drive, San Antonio, Texas 78229.

University Hospital
4502 Medical Drive
San Antonio, TX 78229

University Health System
www.UniversityHealthSystem.com

University Hospital

University Health Center – Downtown

University Center for Community Health / Texas Diabetes Institute

University Family Health Centers:
- North
- Northwest
- Southeast
- Southwest

University Health System Clinics:
- Eastside
- Good Health Clinic
- Kenwood
- Naco Perrin
- Old Hwy 90
- Salinas
- South Flores
- Westend
- Zarzamora

University Health System Business Center

Report of Management Responsibility

The management of University Health System (the System) is responsible for the preparation and integrity of the financial information presented in this report. The basic financial statements have been prepared in accordance with accounting principles generally accepted in the United States as promulgated by the Governmental Accounting Standards Board, and include amounts based on judgments and estimates made by management. Management also prepares the management's discussion and analysis, discreetly presented component units, required supplementary information and other financial information included in the report and is responsible for its accuracy and consistency with the financial statements.

The basic financial statements have been audited by the independent accounting firm of Ernst & Young LLP, who was given unrestricted access to all financial records and related data, including the minutes of all meetings of the Board of Managers. The Board of Managers, through its Budget and Finance Committee (the committee) provides oversight to the financial reporting process. Integral to this process is the committee's review and discussion with management of the monthly financial statements and the external auditors for the annual financial statements.

The System maintains a system of internal control over financial reporting, which is designed to provide reasonable assurance that transactions are executed as authorized and accurately recorded, that assets are properly safeguarded, and also provides reasonable assurance to our management and the Board of Managers regarding the reliability of our financial statements. The internal control system includes:

- A documented organizational structure and division of responsibility;
- Established policies and procedures which are routinely reviewed by management, regularly communicated to staff and that demand highly ethical conduct from all employees.

The System's Integrity Services Department monitors the operation of the internal control system and reports findings and recommendations to management and the Board of Managers as appropriate. Corrective actions are taken to address control deficiencies and other opportunities for improvement as they are identified.

University Health System

George B. Hernandez, Jr.
President/Chief Executive Officer

Peggy Deming
Executive Vice President/
Chief Financial Officer

MAGNET RECOGNITION
AMERICAN NURSES CREDENTIALING CENTER

THE JOINT COMMISSION
NATIONAL QUALITY APPROVAL

University Health System
Bexar County, Texas

University Health System – Balance Sheets

	December 31	
	2010	**2009**
	(In Thousands)	
Assets		
Current assets:		
Cash and cash equivalents	**$ 141,941**	$ 175,465
Short-term investments	**39,202**	6,644
Patient receivables, less allowance for charity and doubtful accounts and discounts (2010 – $167,125; 2009 – $166,316)	**63,466**	62,429
Property taxes receivable	**165,121**	178,014
Prepaid assets and other current assets	**51,742**	46,875
Total current assets	**461,472**	469,427
Noncurrent cash and investments:		
Noncurrent investments	**35,455**	26,184
Internally designated for capital acquisitions and improvements	**166,701**	161,152
Internally designated for contingencies	**147,868**	144,651
Held by trustee for professional self-insurance	**10,157**	9,710
Restricted accounts:		
Project Fund series 2008 Certificates of Obligation	**198,032**	277,887
Project Fund series 2009 Certificates of Obligation	**281,732**	281,175
Project Fund series 2010 Certificates of Obligation	**202,408**	–
Certificate Fund	**19,408**	10,396
Total noncurrent cash and investments	**1,061,761**	911,155
Long-term patient receivables, less allowance for charity and doubtful accounts (2010 – $31,768; 2009 – $26,916)	**14,238**	14,238
Capital assets, net of accumulated depreciation	**366,222**	250,157
Other assets	**7,534**	5,865
Total assets	**$ 1,911,227**	$ 1,650,842

	December 31	
	2010	**2009**
	(In Thousands)	
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 50,898**	$ 46,129
Compensated absences	**14,711**	14,084
Estimated third-party payor settlements	**15,908**	13,119
Accrued liabilities	**27,969**	25,738
Medical claims payable	**35,338**	36,100
Deferred tax revenue	**278,816**	268,968
Deferred other revenue	**–**	227
Current maturities of long-term debt	**11,960**	7,790
Total current liabilities	**435,600**	412,155
Long-term debt, less current maturities	**745,239**	553,008
Estimated self-insurance reserves	**1,263**	1,353
Long-term deferred revenue	**65**	14,138
Total liabilities	**1,182,167**	980,654
Net assets:		
Invested in capital assets, net of related debt	**223,449**	217,776
Restricted	**1,582**	1,033
Unrestricted	**504,029**	451,379
Total net assets	**729,060**	670,188
Total liabilities and net assets	**$ 1,911,227**	$ 1,650,842

See accompanying notes.

University Health System
Bexar County, Texas

University Health System – Statements of Revenue, Expenses, and Changes in Net Assets

	Year Ended December 31 2010	2009
	(In Thousands)	
Operating revenue:		
Net patient service revenue, net of provision for bad debt (2010 – $35,967; 2009 – $34,362)	**$ 360,380**	$ 366,257
Premium revenue	**268,562**	258,007
Other revenue	**47,606**	42,828
Total operating revenue	**676,548**	667,092
Operating expenses:		
Employee compensation	**299,738**	289,376
Supplies	**114,988**	108,997
Purchased services	**106,181**	100,963
Medical services	**118,575**	115,283
Medical claims expense	**236,282**	239,552
Depreciation and amortization	**37,208**	33,705
Other	**1,603**	1,541
Total operating expenses	**914,575**	889,417
Operating loss	**(238,027)**	(222,325)
Nonoperating revenue (expense):		
Property taxes	**275,419**	266,981
Investment income	**5,194**	4,853
Proceeds from tobacco settlement	**5,577**	9,778
Build America Bond interest subsidy	**8,578**	–
Premium deficiency reserve	**1,582**	(1,582)
Total nonoperating revenue (expense)	**296,350**	280,030
Excess of revenues over expenses before contributions	**58,323**	57,705
Capital contributions received, net	**549**	516
Increase in net assets	**58,872**	58,221
Total net assets – beginning of year	**670,188**	611,967
Total net assets – end of year	**$ 729,060**	$ 670,188

See accompanying notes.

University Health System
Bexar County, Texas

University Health System – Statements of Cash Flows

	Year Ended December 31	
	2010	2009
	(In Thousands)	
Operating activities		
Receipts from and on behalf of patients and contractors	**$ 659,144**	$ 675,653
Payments to suppliers	**(571,840)**	(592,213)
Payments to employees	**(299,149)**	(293,996)
Net cash used in operating activities	**(211,845)**	(210,556)
Noncapital financing activities		
Receipt of property taxes	**260,684**	256,287
Proceeds from tobacco settlement	**5,577**	9,778
Proceeds received from restricted contributions	**549**	516
Net cash provided by noncapital financing activities	**266,810**	266,581
Capital and related financing activities		
Receipt of property taxes for debt service	**37,476**	30,081
Purchase of capital assets, net	**(153,273)**	(57,594)
Issuance of long-term debt	**204,191**	284,400
Payment of debt issuance costs	**(1,669)**	(3,194)
Repayment of long-term debt	**(7,790)**	(12,935)
Interest on long-term debt	**1,968**	7,002
Receipt of Build America Bond interest subsidy	**8,578**	–
Net cash provided by capital and related financing activities	**89,481**	247,760
Investing activities		
Interest income and realized gains and losses on investments	**6,294**	8,341
Purchases of investments	**(1,117,514)**	(537,727)
Proceeds from sales of investments	**1,074,585**	533,940
Increase in designated assets	**(141,335)**	(305,979)
Net cash used in investing activities	**(177,970)**	(301,425)
Net increase (decrease) in cash and cash equivalents	**(33,524)**	2,360
Cash and cash equivalents, beginning of year	**175,465**	173,105
Cash and cash equivalents, end of year	**$ 141,941**	$ 175,465

University Health System
Bexar County, Texas

University Health System – Statements of Cash Flows (continued)

	Year Ended December 31	
	2010	**2009**
	(In Thousands)	
Reconciliation of operating loss to net cash used in operating activities		
Operating loss	**$ (238,027)**	$ (222,325)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization expense	**37,208**	33,705
Provision for bad debts	**35,967**	34,362
Changes in operating assets and liabilities:		
Patient receivables	**(37,004)**	(35,254)
Prepaid assets and other current assets	**(4,867)**	(25,703)
Other assets	**–**	139
Accounts payable	**4,769**	(751)
Compensated absences	**627**	884
Estimated third-party payor settlements	**2,789**	(521)
Accrued liabilities	**263**	(5,226)
Medical claims payable	**(762)**	1,115
Estimated self-insurance reserves	**(90)**	540
Deferred other revenue	**(14,300)**	10,061
Premium deficiency reserve	**1,582**	(1,582)
Net cash used in operating activities	**$ (211,845)**	$ (210,556)

See accompanying notes.

University Health System
Bexar County, Texas

University Health System Pension Plan – Statements of Plan Net Assets

	December 31	
	2010	**2009**
	(In Thousands)	
Assets		
Current assets	**$ 4,458**	$ 2,408
Noncurrent investments:		
Mutual funds – common stocks	**61,466**	52,261
Mutual funds – U.S. government	**33,117**	27,395
Mutual funds – international common stock	**22,178**	21,043
Investment in limited partnership	**16,446**	12,398
Common stocks	**17,487**	13,964
Other assets	**1,681**	–
Total assets	**156,833**	129,469
Liabilities		
Accounts payable and accrued expenses	**40**	41
Net assets held in trust for pension benefits	**$ 156,793**	$ 129,428

See accompanying notes.

University Health System
Bexar County, Texas

University Health System Pension Plan –
Statements of Changes in Plan Net Assets

	Year Ended December 31 2010	2009
	(In Thousands)	
Additions:		
Contributions	**$ 18,313**	$ 16,028
Net investment income:		
Interest income	**1,430**	9
Dividend income	**1,148**	1,166
Net appreciation in fair value of investments	**15,409**	21,877
Investment expense	**(447)**	(367)
	17,540	22,685
Total additions	**35,853**	38,713
Deductions:		
Benefit payments	**8,361**	5,515
Administrative expenses	**127**	104
Total deductions	**8,488**	5,619
Changes in net assets held in trust for pension benefits	**27,365**	33,094
Net assets – beginning of year	**129,428**	96,334
Net assets – end of year	**$ 156,793**	$ 129,428

See accompanying notes.

University Health System Retiree Health Trust – Statements of Plan Net Assets

	December 31 2010	December 31 2009
	(In Thousands)	
Assets		
Current assets:		
Money market	**$ 145**	$ 9,270
Noncurrent assets:		
U.S. government securities	**3,176**	–
Mutual funds – equities	**10,344**	–
Other assets	**26**	–
Total assets	**13,691**	9,270
Liabilities		
Accounts payable and accrued expenses	**4**	–
Net assets held in trust for other postemployment benefits	**$ 13,687**	$ 9,270

See accompanying notes.

University Health System
Bexar County, Texas

University Health System Retiree Health Trust – Statements of Changes in Plan Net Assets

	Year Ended December 31	
	2010	**2009**
	(In Thousands)	
Additions:		
Contributions	**$ 3,060**	$ 2,702
Net investment income:		
Interest income	**–**	1
Dividend income	**325**	–
Net appreciation in fair value of investments	**1,041**	–
Investment expense	**(9)**	–
Total additions	**4,417**	2,703
Changes in net assets held in trust for other pension benefits	**4,417**	2,703
Net assets – beginning of year	**9,270**	6,567
Net assets – end of year	**$ 13,687**	$ 9,270

See accompanying notes.

1. Organization

University Health System and Reporting Entity

The Bexar County Hospital District d/b/a University Health System is a hospital district established under Article IX, Section 4 of the Texas Constitution and Chapter 281 of the Texas Health and Safety Code. It is a political subdivision of the state of Texas, created to provide medical and hospital care to the needy and indigent of Bexar County, and is a discrete component unit of Bexar County (legally separate from Bexar County, Texas). Its Board is composed of seven members appointed by the Commissioners Court for staggered terms of two years (or until a successor is appointed and qualified). Board members are "public officers" under the Texas Constitution who, as a body, exercise sovereign functions of government largely independent of the control of others, and serve without pay.

The accompanying basic financial statements include the financial statements of Bexar County Hospital District d/b/a University Health System (the System), the University Health System Pension Plan (the Plan), and the University Health System Retiree Health Trust (the OPEB Trust).

The System is the fourth-largest public health system in the state of Texas. Its staff of just over 5,135 health care employees operates University Hospital, San Antonio's only civilian Level 1 Trauma Center; the University Center for Community Health, devoted to the prevention and treatment of diabetes; the University Health Center – Downtown; four University Family Health Centers; University Dialysis – Southeast; South Dialysis; nine preventive health clinics; and a health care program at Bexar County's correctional facilities. Its network of community outpatient and inpatient facilities provides primary care, preventive care, and specialty outpatient care throughout Bexar County. Additionally, the System has had a long-standing affiliation with The University of Texas Health Science Center at San Antonio (UTHSCSA). The System's facilities serve as the major teaching facilities for many of UTHSCSA's health care programs, including the graduate medical education (GME) program. The System is exempt from federal income tax under Section 115(a) of the Internal Revenue Code.

1. Organization (continued)

The System has established various affiliated nonprofit, tax-exempt organizations to facilitate the funding, delivery, and management of its health care mission, as described below.

The University Health System Foundation (the Foundation) (formerly the University Health System Development Corporation) was created in 1984 to raise funds for the System. The Foundation is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code and is a legally separate entity from the System. The Board of Managers of the System appoints a voting majority of the Board of the Foundation, and the Foundation provides services exclusively to the System. The Foundation is included as a blended component unit of University Health System.

Community First Health Plans, Inc. (CFHP) was established in 1994 to assist the System with providing and arranging health care services in accordance with the Texas Health Maintenance Organization Act (Chapter 20A, Vernon's Texas Insurance Code). CFHP is exempt from federal income tax under Section 501(c)(4) of the Internal Revenue Code.

Community First Group Hospital Service Corporation (the PPO) was incorporated in 2001 and licensed by the state of Texas on August 3, 2001, to operate as a group hospital services corporation under Chapter 20 of the Texas Insurance Code. The PPO is a nonprofit, taxable company, and is a subsidiary of CFHP. The PPO provides hospital accident coverage and preferred provider organization medical insurance to policyholders through their employer. The services provided by CFHP and its subsidiary, the PPO, benefit the System; therefore, CFHP and its subsidiary are included as a blended component unit of University Health System. In March 2010, the PPO filed a withdrawal plan with the Texas Department of Insurance.

In June 1996, the System established Community Medicine Associates (CMA), a Texas nonprofit health organization certified by the Texas State Board of Medical Examiners pursuant to Section 501(a) of the Texas Medical Practice Act, now codified at Section 162.001 of the Texas Occupations Code. CMA was activated by the System on April 1, 2000, to provide primary care physician services at the System's Family Health Centers. CMA is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. The services provided by CMA benefit the System; therefore, CMA is included as a blended component unit of University Health System.

1. Organization (continued)

Management of the System believes the basic financial statements of University Health System presented on a comparative basis to be the most reflective of the System's activities. Patient service revenue and medical claims expense for CFHP members amounting to $10,345,000 and $8,809,000 in 2010 and 2009, respectively, are not eliminated in the basic financial statements. Additionally, other revenue of $1,631,000 and $1,606,000 in 2010 and 2009, respectively, for payments made from the System to CFHP are not eliminated in the basic financial statements. All other significant intercompany accounts and transactions have been eliminated in the basic financial statements.

The basic financial statement presentation also includes the discrete presentation of the Plan. The Plan is a legally separate component unit. It is fiscally dependent on the System and performs services exclusively for employees of the System. A board appointed by the System governs the Plan. Separate financial statements of the Plan are available at the System's administrative offices.

The basic financial statement presentation also includes the discrete presentation of the OPEB Trust. The OPEB Trust is a legally separate component unit. It is fiscally dependent on the System and performs services exclusively for employees of the System. A board appointed by the System governs the OPEB Trust.

Other Significant Relationships

The System and Vanguard Health System (VHS) (as the successor organization to Baptist Health System) mutually control Texas AirLife, Inc. d/b/a San Antonio AirLife, Inc. (AirLife), a Texas nonprofit corporation, which provides air ambulance services to Bexar County and South Texas. The System and VHS retain control over AirLife through the retention of specific reserve powers, including the appointment of AirLife board members. AirLife is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

The System is a member of the Hospital Laundry Cooperative Association (HLCA), an organization established under Chapter 301, Subchapter B of the Texas Health and Safety Code. The System's economic interest in HLCA is determined by "units of interest" under the terms of a Membership Agreement executed by the System on August 17, 1995. HLCA is a taxable cooperative under the Internal Revenue Code.

1. Organization (continued)

The System's ownership in AirLife and HLCA is recorded using the equity method of accounting in the accompanying basic financial statements.

In 1994, UTHSCSA established University Physicians Group (UPG), a Texas nonprofit corporation organized under Section 501(a) of Article 4495b of the Texas Medical Practice Act, now codified at Section 162.001 of the Texas Occupations Code. Effective May 1, 2006, UPG legally changed its name to UT Medicine San Antonio (UT Medicine). UT Medicine serves as a contracting vehicle for physician services with the System and other payors, including managed care organizations.

Effective June 6, 2000, the System and Bexar County became the sole sponsors for the Center for Health Care Services (CHCS). The terms of the relationship are governed by a Sponsorship Agreement with Bexar County dated May 2, 2000. CHCS is a community center established under Chapter 534 of the Texas Health and Safety Code to provide a comprehensive array of mental health, mental retardation, and drug and alcohol abuse services throughout Bexar County. CHCS was originally established by a coalition of 17 local taxing authorities in 1966.

The Department of Aging and Disability Services (DADS) required CHCS to divest its dual roles as a local authority and provider of mental retardation services, which it did by transferring its responsibility for mental retardation authority to the Alamo Area Council of Governments (AACOG) effective September 1, 2006. The System entered into a memorandum of understanding with AACOG to connect the sponsorship obligations for mental retardation from CHCS to AACOG.

The balances and transactions of UT Medicine, CHCS, and AACOG are not combined or otherwise included in the accompanying basic financial statements, but the System's transactions with these organizations are included.

2. Significant Accounting Policies

Method of Accounting

The System's basic financial statements are prepared in accordance with Statement No. 34 of the Governmental Accounting Standards Board (GASB), *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, which established standards for external financial reporting for all state and local governmental entities. These standards require presentation of a balance sheet; a statement of revenue, expenses, and changes in net assets; and a direct method statement of cash flows. Additionally, Statement No. 34 requires the classification of net assets into three components: invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any related borrowings that are attributable to the acquisition, construction, or improvement of those assets.

- Restricted – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or constraints imposed by law through constitutional provisions or enabling legislation.

- Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

Additionally, the financial statements of the System are prepared on the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred. Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the System has elected to apply all standards of the Governmental Accounting Standards Board, as well as all relevant pronouncements of the Financial Accounting Standards Board, issued on or before November 30, 1989.

2. Significant Accounting Policies (continued)

The accompanying basic financial statements also reflect the financial position and changes in financial position of the Plan and the OPEB Trust. The Plan is used to account for assets held in trust for the benefit of the employees of the System for the defined benefit pension plan. The OPEB Trust is used to account for assets held in trust related to the postretirement benefit program for employees of the System. In accordance with GASB Statement No. 34, the assets and net assets of the Plan and the OPEB Trust are presented separately from University Health System. The financial statements of the Plan and the OPEB Trust are prepared using the accrual basis of accounting. Employer contributions to the Plan and the OPEB Trust are recognized when due. Benefits are recognized when due and payable in accordance with the terms of the Plan.

Statements of Revenue, Expenses, and Changes in Net Assets

For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as revenue and expenses. Operating revenues include those generated from direct patient care and related support services. Nonoperating revenue consists of those revenues that are related to financing and investing types of activities and result from nonexchange transactions or investment income. When an expense is incurred for purposes for which there are both restricted and unrestricted net assets available, it is the System's practice to apply those expenses to restricted net assets to the extent such are available, and then to unrestricted net assets.

Cash and Cash Equivalents

The System considers all highly liquid investments with original maturities of less than 90 days to be cash equivalents. Cash and cash equivalents at year-end include demand deposits, as well as direct and indirect obligations of the U.S. government, and money market mutual funds. All demand deposits are collateralized with securities held in safekeeping at the Federal Reserve Bank in the name of the System.

Investments

Investments of the System are valued at fair value. Statutes and the Board of Managers authorize the System to invest in obligations, as further described in Note 15.

2. Significant Accounting Policies (continued)

Additionally, in order to comply with various statutory requirements under the Texas Department of Insurance, investments of approximately $59,943,000 and $51,467,000 at December 31, 2010 and 2009, respectively, are held in the name of CFHP.

Investments of the Plan are described in the statements of plan net assets. Current assets consist of money market funds, which are valued at fair value. Mutual funds consisting of common stocks, U.S. government securities, and international common stocks are valued based on net asset values at year-end. The Plan invested in Advisory Research Value Equity Fund II, L.P. (the Partnership), a Delaware limited partnership that invests in small-capitalization to mid-capitalization companies. The Partnership's net assets were substantially invested in common stocks, which were recorded at quoted market prices. The Plan's allocable portion of these net assets was $16,446,000 and $12,398,000 at December 31, 2010 and 2009, respectively. The fair value of common stocks of the Plan was based on quoted market prices.

Designated Net Assets

Designated net assets includes assets set aside by the Board of Managers for future capital improvements, future contingencies (reserve fund), and assets held by trustees under self-insurance trust arrangements.

Capital Assets and Depreciation

The System records capital assets at cost and provides for depreciation of capital assets by charging against current operations amounts sufficient to amortize the cost of properties over their estimated useful lives. The System's policy is to capitalize assets greater than $5,000.

Depreciation is computed using the straight-line method. The System uses American Hospital Association guidelines in establishing useful lives, which generally fall within the following ranges:

Land improvements	5–15 years
Buildings and improvements	10–30 years
Equipment	5–15 years

2. Significant Accounting Policies (continued)

Amounts that materially extend useful lives or increase values or capabilities are capitalized, whereas routine maintenance, repair, and replacement costs are charged against current income.

Self-Insurance Cost

The System is self-insured for employee health insurance costs. The self-insured plan is administered by CFHP, which determines the cost of claims paid to community health care providers and estimates a reserve for medical claims incurred but not yet reported. The System also recognizes the incremental cost of services provided by the System to plan participants. The System maintains a stop-loss insurance contract to cover 90% of certain medical costs in excess of $175,000, up to a maximum of $2,000,000 per contract year and $5,000,000 per member lifetime maximum. As of December 31, 2010 and 2009, a reserve of $1,518,000 and $1,330,000, respectively, is recorded.

The System funds a revocable self-insurance trust to provide for the payment of medical malpractice and general liabilities. The funding is based on management's recommendations for settlement of claims to limits of $100,000 per claim and $300,000 per occurrence, in accordance with the limited liability provisions of the Texas Tort Claims Act. The amounts provided for funding and the estimated liability are based on management's estimates. The amounts include estimates of the ultimate cost for both reported claims and incurred but not yet reported claims.

During 2003, the System began self-insuring "tail coverage" for certain employed physicians. This coverage has a limited time exposure and also is subject to claims limits. Amounts are provided for funding, and estimated liabilities for incurred but not yet reported claims are based on management estimates.

The System participates in a self-insurance program that provides for the payment of workers' compensation claims. The funding for this program is based on third-party recommendations for settlement in accordance with Texas workers' compensation laws.

2. Significant Accounting Policies (continued)

Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors and estimated allowances for uncollectible accounts. The allowances are estimated using historical experience and established billing rates. 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 Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The System believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Premium Revenue

CFHP has agreements with plan sponsors to arrange health service benefits for subscribing participants. Under these agreements, CFHP receives monthly premium payments based on the number of each plan sponsor’s participants. In addition, CFHP receives supplementary delivery payments under the Medicaid program.

Compensated Absences

The System’s employees earn paid time off (PTO) at varying rates depending on years of service. Employees may accumulate PTO up to a specified maximum. Employees are paid for accumulated PTO upon voluntary termination, including retirement, as employees who retire from the System may convert accumulated PTO to termination payments at a rate of 50% of their accumulated PTO balances. The estimated amount of PTO payable as termination payments is reported as a current liability in both 2010 and 2009.

2. Significant Accounting Policies (continued)

Medical Claims Expense

CFHP arranges for the provision of comprehensive health care services to its members principally through its contractual relationships with physician groups, ancillary providers, and hospitals, including the System. Physicians, ancillary providers, and hospitals are paid a contracted fee for service or a capitation rate, and CFHP is responsible for any related payments to those providers.

The cost of health care services provided is accrued in the period it is rendered to the enrolled members, based in part on estimates for hospital services and other specialist or out-of-area costs that have been incurred but not yet reported. For the period from January 1, 2009 through December 31, 2010, CFHP has reinsurance contracts to cover 90% of certain medical costs in excess of defined deductibles, up to a per-member maximum of $2,000,000 per contract year, and a $5,000,000 per-member lifetime maximum.

Medical claims expense reserves represent the estimated ultimate net cost of all reported and unreported losses incurred through December 31. The reserves for unpaid medical claims expenses are actuarially determined using individual case-basis valuations and statistical analyses. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes the reserves for medical claims expenses are adequate. The estimates are continually reviewed and adjusted as necessary, as experience develops or new information becomes known; such adjustments are included in current operations.

Changes in the System's aggregate liability for medical claims in fiscal years 2010 and 2009 were as follows:

Year Ended December 31	Beginning of Fiscal Year Liability	Current-Year Claims and Changes in Estimates	Claim Payments	End of Fiscal Year Liability
		(In Thousands)		
2010	**$ 36,100**	**$ 236,282**	**$ 237,044**	**$ 35,338**
2009	$ 34,985	$ 239,552	$ 238,437	$ 36,100

2. Significant Accounting Policies (continued)

Charity Care

The System provides charity care to residents of Bexar County who qualify on a financial basis for the Care*Link* Program and to all others who qualify based on the System's charity policy. The System does not pursue collection of amounts in excess of the established guidelines for those patients who meet the charity criteria. Such excess is considered charity care and is not reported as revenue.

The System's Care*Link* Program is used to discount gross charges for medical services received in the System's facilities. Under this program, residents of Bexar County have an established maximum family liability rather than a discount of total gross charges. Key factors in establishing a family's maximum liability levels are: number of dependents, income, and the relationship of these factors to the current Poverty Index. The System does not pursue collection of amounts in excess of the maximum family liability. Such excess amounts are considered charity care and are not reported as revenue.

Arrangements are made with residents of Bexar County to pay their reduced medical costs in installments. Any amounts designated as not being due prior to December 31, 2010, are classified as long-term patient receivables and are presented net of applicable allowances.

Non-Care*Link* patients meeting the financial and medical indigency criteria established in the charity policy receive a discount from gross charges for emergency and catastrophic medical services received in the System's facilities. Charges for financial indigency are discounted based on family income compared to the Poverty Index. Charges for medical indigency are discounted when charges exceed a certain income and asset level.

The System maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy. The following information measures the level of charity care provided during the years ended December 31:

	2010	**2009**
Charges forgone, based on established rates	**$ 412,701,000**	$ 381,727,000

2. Significant Accounting Policies (continued)

Property Taxes

The Commissioners Court of Bexar County levies for the System an ad valorem tax as provided under state law on properties within the County. These taxes are collected by the Bexar County Tax Assessor-Collector and are remitted to the System when received. The System's tax rate is levied and becomes collectible in October of each year based on the certified assessed value as of the previous January 1. Taxes levied on October 1 are designated to support the System's operations for the following calendar year. The System records the levy, net of an assessment fee and allowance for uncollectible amounts, as a current receivable and deferred tax revenue in the year levied. The deferred tax revenue is accreted to revenue on a straight-line basis in the following year.

Build America Bond Interest Subsidy

The System issued taxable Build American Bonds (BABs) in August 2010 and August 2009. Under the BABs program, the U.S. Treasury pays 35% of the interest as a subsidy to the issuer. The System records the interest subsidy received or receivable from the U.S. Treasury as nonoperating revenue when the System has met all of the eligibility criteria to receive the subsidy. The System recorded $8.6 million of nonoperating revenue in 2010 for the BABs interest subsidy.

Donor-Restricted Funds

Donor-restricted funds are used to differentiate resources, the uses of which are restricted by donors or grantors, from resources or general funds on which donors or grantors place no restrictions or those funds that arise as a result of the operations of the System for its stated purpose. Restricted gifts and other restricted resources are recorded as additions to the appropriate restricted fund.

Resources restricted by donors or grantors for specific operating purposes are reported in other revenue to the extent used in the period.

3. Property Taxes

Property Taxes Receivable

Property taxes receivable are composed of the following as of December 31:

	2010	2009
	(In Thousands)	
Current taxes, net of allowance for uncollectible amounts of $2,840 in 2010 and $6,423 in 2009	**$ 152,916**	$ 167,071
Delinquent taxes, net of allowance for uncollectible amounts of $4,182 in 2010 and $3,592 in 2009	**8,128**	7,272
Penalty and interest, net of allowance for uncollectible amounts of $4,758 in 2010 and $4,096 in 2009	**4,077**	3,671
	$ 165,121	$ 178,014

Property Taxes Revenue

As indicated in Note 2, the Bexar County Commissioners Court levies an ad valorem tax on the value of property in Bexar County to support the provision of care to indigent residents of Bexar County. In 2010 and 2009, the Commissioners Court levied a tax rate for maintenance and operations (M&O) and debt service (DS) to support the System's operations and long-term debt, described in Note 7. The revenues received for 2010 and 2009 were classified as follows:

	2010	2009
	(In Thousands)	
Maintenance and operations	**$ 241,872**	$ 240,829
Debt service	**33,547**	26,152
	$ 275,419	$ 266,981

4. Designated Net Assets

Of the $502,258,000 and $451,379,000 of unrestricted net assets reported as of December 31, 2010 and 2009, respectively, certain amounts have been designated by the System's Board of Managers for various purposes. Designated funds remain under the control of the Board of Managers, which may, at its discretion, later use the funds for other purposes. The composition of designated net assets is set forth in the following table:

	2010	**2009**
	(In Thousands)	
Designated by the Board:		
Capital acquisitions and improvements:		
Cash and short-term investments	**$ 51,056**	$ 96,831
U.S. government agencies	**113,126**	61,820
U.S. Treasury notes	**2,519**	2,501
	$ 166,701	$ 161,152
Contingency fund:		
Cash and short-term investments	**$ 9,294**	$ 16,488
U.S. government agencies	**134,983**	124,667
U.S. Treasury notes	**3,591**	3,496
	$ 147,868	$ 144,651
Professional self-insurance held in trust:		
Cash and short-term investments	**$ 371**	$ 377
U.S. government agencies	**4,563**	4,651
U.S. Treasury notes	**5,223**	4,682
	$ 10,157	$ 9,710

5. Property, Plant, and Equipment

The System's investment in property, plant, and equipment consists of the following:

	January 1, 2010	Additions/ Transfers	Retirements/ Transfers	December 31, 2010
		(In Thousands)		
Capital assets:				
Land and land improvements	**$ 8,329**	**$ 1,249**	**$ –**	**$ 9,578**
Buildings and improvements	**277,052**	**26,707**	**–**	**303,759**
Equipment	**253,005**	**25,823**	**–**	**278,828**
Total at historical cost	**538,386**	**53,779**	**–**	**592,165**
Less:				
Accumulated depreciation – buildings and improvements	**(149,354)**	**(12,633)**	**–**	**(161,987)**
Accumulated depreciation – equipment	**(190,559)**	**(24,587)**	**–**	**(215,146)**
Total accumulated depreciation	**(339,913)**	**(37,220)**	**–**	**(377,133)**
Construction-in-progress	**51,684**	**99,506**	**–**	**151,190**
Total capital assets, net of accumulated depreciation	**$ 250,157**	**$ 116,065**	**$ –**	**$ 366,222**

	January 1, 2009	Additions/ Transfers	Retirements/ Transfers	December 31, 2009
		(In Thousands)		
Capital assets:				
Land and land improvements	$ 7,835	$ 494	$ –	$ 8,329
Buildings and improvements	267,881	9,171	–	277,052
Equipment	238,964	17,536	(3,495)	253,005
Total at historical cost	514,680	27,201	(3,495)	538,386
Less:				
Accumulated depreciation – buildings and improvements	(137,465)	(11,889)	–	(149,354)
Accumulated depreciation – equipment	(172,081)	(21,927)	3,449	(190,559)
Total accumulated depreciation	(309,546)	(33,816)	3,449	(339,913)
Construction-in-progress	21,134	30,550	–	51,684
Total capital assets, net of accumulated depreciation	$ 226,268	$ 23,935	$ (46)	$ 250,157

As of December 31, 2010 and 2009, included in construction-in-progress is capitalized interest of $50,214,000 and $20,416,000, respectively.

6. Leases

Rental expense pursuant to noncancelable operating leases amounted to $7,140,000 and $7,112,000 for the years ended December 31, 2010 and 2009, respectively. Minimum annual lease obligations relating to noncancelable leasing arrangements are as follows (in thousands):

2011	$	4,374
2012		3,971
2013		2,657
2014		1,377
2015		765
2016–2019		2,222
Total	$	15,366

7. Long-Term Debt

A schedule of changes in the System's long-term debt for 2010 and 2009 follows:

	Balance at January 1, 2010	Additions	Reductions	Balance at December 31, 2010	Amounts Due Within One Year
			(In Thousands)		
Bonds payable:					
Certificates of Obligation, series 2008, net	**$ 276,098**	**$ –**	**$ 4,357**	**$ 271,741**	**$ 4,770**
Certificates of Obligation, series 2009A, net	**38,305**	**–**	**4,127**	**34,178**	**3,145**
Certificates of Obligation, series 2009B, net	**246,395**	**–**	**–**	**246,395**	**–**
Certificates of Obligation, series 2010B, net	**–**	**204,885**	**–**	**204,885**	**4,045**
Total long-term debt	**$ 560,798**	**$ 204,885**	**$ 8,484**	**$ 757,199**	**$ 11,960**

7. Long-Term Debt (continued)

	Balance at January 1, 2009	Additions	Reductions	Balance at December 31, 2009	Amounts Due Within One Year
			(In Thousands)		
Bonds payable:					
Certificates of Obligation, series 2008, net	$ 289,333	$ –	$ 13,235	$ 276,098	$ 4,105
Certificates of Obligation, series 2009A, net	–	38,305	–	38,305	3,685
Certificates of Obligation, series 2009B, net	–	246,395	–	246,395	–
Total long-term debt	$ 289,333	$ 284,700	$ 13,235	$ 560,798	$ 7,790

The combination tax and revenue Certificates of Obligation, series 2008 (the 2008 Certificates) were issued in 2008, and mature in various amounts annually on February 15, from 2009 through 2038. These have stated coupon rates ranging from 3.25% to 5.00%, and are collateralized by a levy of ad valorem tax revenue and lien on and pledge of surplus revenues. The tax Certificates of Obligation, series 2009A (the 2009A Certificates) were issued in 2009, and mature in various amounts annually on February 15, from 2010 through 2017, with stated coupon rates ranging from 1.00% to 5.00%. The tax Certificates of Obligation, series 2009B (the 2009B Certificates) were issued in 2009, and mature in various amounts annually on February 15, from 2018 through 2039, with stated coupon rates ranging from 5.269% to 6.904%. The tax Certificates of Obligations, series 2010B (the 2010B Certificates) were issued in 2010, and mature in various amounts annually on February 15, from 2011 through 2040, with stated coupon rates ranging from 0.300% to 5.413%. The 2009B Certificates and 2010B Certificates are designated under the American Recovery and Reinvestment Act of 2009 as “Qualified Build America Bonds” (BABs) debt. The series 2009A Certificates and 2009B Certificates are collateralized by a levy of ad valorem tax revenue. Proceeds of the issuances of debt are maintained in Project Funds for each individual issuance until expended for their designated purpose, and as required by the terms of the 2008 Certificates, 2009A Certificates, 2009B Certificates, and 2010B Certificates. DS ad valorem tax receipts levied annually by the Commissioners Court are maintained in a

7. Long-Term Debt (continued)

Certificate Fund account collectively for all issuances. The Project Funds and Certificate Fund are included within noncurrent cash and investments as restricted accounts on the balance sheets, and their composition is set forth in the following table:

	2010	2009
	(In Thousands)	
Project Fund series 2008 Certificates of Obligation:		
Cash and short-term investments	**$ 72,387**	$ 69,278
U.S. government agencies	**125,645**	20,198
U.S. Treasury notes	**–**	188,411
	$ 198,032	$ 277,887
Project Fund series 2009 Certificates of Obligation:		
Cash and short-term investments	**$ 24,171**	$ 55,789
U.S. government agencies	**257,561**	–
U.S. Treasury notes	**–**	225,386
	$ 281,732	$ 281,175
Project Fund series 2010B Certificates of Obligation:		
Cash and short-term investments	**$ 11,024**	$ –
U.S. government agencies	**191,384**	–
	$ 202,408	$ –
Certificate Fund:		
Cash and short-term investments	**$ 19,408**	$ 10,396

7. Long-Term Debt (continued)

Scheduled principal and interest repayments on long-term debt obligations are as follows (in thousands):

	Principal	Interest	Interest Credit (BABs)	Net Interest
Year ending December 31:				
2011	$ 11,960	$ 39,484	$ (8,814)	$ 30,670
2012	11,485	39,673	(8,954)	30,719
2013	11,735	39,400	(8,933)	30,467
2014	12,495	39,043	(8,913)	30,130
2015	13,560	38,600	(8,894)	29,706
2016–2020	89,575	182,895	(43,357)	139,538
2021–2025	116,225	157,618	(37,966)	119,652
2026–2030	143,535	122,173	(29,639)	92,534
2031–2035	179,085	75,836	(18,855)	56,981
2036–2040	167,140	20,227	(5,701)	14,526
Total	$ 756,795	$ 754,949	$ (180,026)	$ 574,923

The System is a discrete component unit of Bexar County, and the Commissioners Court levies for the System an ad valorem tax on the property values in Bexar County to support the M&O of the System and a DS ad valorem tax to support approved debt service payments. The ad valorem tax rate is adopted annually by the Bexar County Commissioners Court as a designated M&O rate and DS rate. The Commissioners Court passed an order on August 19, 2008, approving and providing for the payment of the 2008 Certificates to finance the construction of permanent public improvements at the System. The 2008 Certificates are payable through February 15, 2038, from the DS ad valorem property tax levy and lien on and pledge of surplus revenues. Principal on the 2008 Certificates has been paid through February 15, 2010, and interest on the 2008 Certificates has been paid through August 15, 2010.

7. Long-Term Debt (continued)

The Commissioners Court passed an order on July 28, 2009, approving and providing for the payment of the 2009A Certificates and 2009B Certificates to finance the construction of permanent public improvements at the System. The 2009A Certificates are payable through February 15, 2017, and the 2009B Certificates are payable through February 15, 2039, from the DS ad valorem property tax levy. Principal on the 2009A and 2009B Certificates has been paid through February 15, 2010, and interest on the 2009A and 2009B Certificates has been paid through August 15, 2010.

The Commissioners Court passed an order on August 17, 2010, approving and providing for the payment of the 2010B Certificates to finance the construction of permanent public improvements at the System. The 2010B Certificates are payable through February 15, 2040, from the DS ad valorem property tax levy and lien on and pledge of surplus revenues. No principal or interest amounts had been paid on the 2010 B Certificates as of December 31, 2010.

8. Net Patient Service Revenue

The System provides services under contract to patients covered under the Medicare and Medicaid programs. The System is reimbursed based on cost or at a predetermined rate based upon diagnosis, plus certain adjustments. Net revenues from these programs are included in patient service revenues at net amounts reflecting customary charges reduced to estimated reimbursement payments. The amounts due to or from these programs are subject to final review and settlement by the respective program's fiscal intermediary. Currently, the System's statements of reimbursable cost have been audited by and settled with the fiscal intermediary through 2006 for Medicare and Medicaid.

At December 31, 2010 and 2009, the System estimated net amounts due to the programs of $15,908,000 and $13,119,000, respectively. Included in net patient service revenue is an increase of $-0- and $1,066,000 for the years ended December 31, 2010 and 2009, respectively, to adjust balances previously estimated as a result of final and tentative settlements and for years that are no longer subject to audits, reviews, or investigations.

The System has also entered into payment agreements with certain commercial insurance carriers, employers, and other third-party administrators. The basis for payment to the System under these arrangements includes prospectively determined daily or per-stay rates and discounts from established charges. Total discounts were $929,466,000 and $880,232,000 for the years ended December 31, 2010 and 2009, respectively.

9. Disproportionate Share Revenue

During 1991, the Texas Legislature issued Senate Bill 82, levying an assessment against certain hospitals and hospital systems. The funds collected via this assessment are pooled by the state in order to receive federal matching funds under the Medicaid Disproportionate Share Program. The state then allocates the federal monies received to hospitals and hospital systems that serve a large disproportionate volume of Medicaid and uninsured patients, the purpose being to increase access to health care for Texas' indigent patients. The amounts received under this program were $12,092,000 and $20,735,000 for 2010 and 2009, respectively, and are included in net patient service revenue. The amounts receivable included in prepaid assets and other current assets at December 31, 2010 and 2009, were $-0- and $5,890,000, respectively.

10. Upper Payment Limit (UPL)

In May 2002, the federal government approved the Upper Payment Limit (UPL) program for the state of Texas, with an effective date of August 31, 2001. The UPL program is a state program that uses federal matching funds to raise state Medicaid reimbursement rates to 100% of equivalent Medicare rates for certain public hospital systems. The amounts received under the UPL program were $71,851,000 and $68,346,000 for 2010 and 2009, respectively, and are included in net patient service revenue. The amounts receivable included in prepaid assets and other current assets at December 31, 2010 and 2009, were $17,240,000 and $15,690,000, respectively.

11. Tobacco Settlement

Allocations of the state of Texas' 1998 Tobacco Settlement for the System were $5,577,000 in 2010 and $9,778,000 in 2009, and are included in nonoperating revenue.

12. Affiliation Agreement

The System and UTHSCSA entered into a 20-year agreement in 1992 that provides that the System will be available to UTHSCSA for teaching and research. Under the agreement and other sub-agreements, UTHSCSA supervises and directs professional services to patients of the System. The System recorded expenses of approximately $14,284,000 and $14,649,000 in 2010 and 2009, respectively, under the terms of the agreements.

13. Pension and Other Postretirement Benefits

Pension Plan

The Plan is a single-employer defined benefit pension plan covering substantially all of the System's employees who work at least 20 hours per week or at least 1,000 hours annually. Employer contributions to the Plan amounted to $13,111,000 and $10,993,000 for the years ended December 31, 2010 and 2009, respectively.

Benefits

Participants are eligible for normal retirement benefits after attaining age 65 and completing five years of vesting service, or after age 55 when years of service plus age equal to 85 (Rule of 85). Annual normal retirement benefits are equal to 1.5% of the average of participants' five highest consecutive years' pay times the number of years of credited service. The Plan's audited financial statements are available at the System's offices in San Antonio, Texas.

At January 1, 2010, the date of the most recent actuarial valuation, Plan membership consisted of:

Inactive participants:	
Retirees and beneficiaries currently receiving benefits	567
Terminated employees with deferred benefits	857
Total inactive participants	1,424
Active participants:	
Fully vested	2,708
Nonvested	1,621
Total active participants	4,329
Total participants	5,753

13. Pension and Other Postretirement Benefits (continued)

Annual Pension Cost and Net Pension Obligation

For fiscal year 2010, the System's annual pension cost and contribution was $13,111,000, resulting in no net pension obligation.

Fiscal Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
	(In Thousands)		
December 31, 2010	**$ 13,111**	**100%**	**$ –**
December 31, 2009	10,993	100%	–
December 31, 2008	10,159	100%	–

The January 1, 2010, 2009, and 2008 pension benefit obligations were determined as a part of actuarial valuations using the projected unit cost method. Significant actuarial assumptions used include: (a) a rate of return on the investment of present and future assets of 8.0% per year compounded annually, (b) projected salary increases of 5.5% per year compounded annually, and (c) an inflation rate of 4.0%.

Contributions Required

The System makes contributions that are actuarially determined to pay the Plan's normal cost plus amortization of unfunded liability. The System amortizes the Plan's unfunded liability over a period ranging from one to 30 years, and is determined in part based on the System's level of contributions. The System's normal cost was approximately $10,607,000, $8,596,000, and $7,744,000 in 2010, 2009, and 2008, respectively, which was 4.68% of covered payroll as of January 1, 2010 (the date of the most recent actuarial report), 4.16% of covered payroll as of January 1, 2009, and 4.11% of covered payroll as of January 1, 2008. The annual covered payroll as of January 1, 2010, 2009, and 2008, was approximately $234,739,000, $214,950,000, and $195,821,000, respectively. Participants are required to contribute 2.00% of annual compensation to the Plan. The System made contributions of $13,111,000, $10,993,000, and $10,159,000, in 2010, 2009, and 2008, respectively.

13. Pension and Other Postretirement Benefits (continued)

Other Postretirement Benefits

Description

In 2007, the System adopted GASB Statement No. 45 (GASB 45), *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions (OPEB).* This statement establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities footnote disclosures. During 2007, the System approved the OPEB Trust to receive contributions and accumulate assets to fund the cost of retiree medical benefits in accordance with the adoption of GASB 45 as a single-employer defined benefit health care plan. Employees eligible to retire from the System may elect to continue medical benefits, currently at the same contribution rates and schedule of benefits as active employees. The financial statements of the OPEB Trust are included as a discretely presented component unit of the System.

Funding Policy

The contribution requirements of plan members and the System are established and may be amended by the Investment Committee of the OPEB Trust. The required contribution is based on projected pay-as-you-go financing requirements. Plan members receiving benefits contributed $274,596 through their required contribution of $52.92 per month for retiree-only coverage, $89.78 for retiree and spouse coverage, $88.37 for retiree and children coverage, and $152.59 for retiree and family coverage.

Annual OPEB Cost and Net OPEB Obligation

The System's annual OPEB cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The adjustment to the ARC shown in the following table is for the portion of the benefits paid to beneficiaries by the System and is recorded in employee compensation expense on a pay-as-you-go basis. The following table shows the

13. Pension and Other Postretirement Benefits (continued)

components of the System's annual OPEB cost for the year, the amount actually contributed to the OPEB Trust, and changes in the System's net OPEB obligation to the OPEB Trust (dollar amounts in thousands):

	Year Ended December 31, 2010
	(In Thousands)
Annual required contribution	$ 3,782
Interest on net OPEB obligation	–
Adjustment to annual required contribution	722
Annual OPEB cost (expense)	3,060
Contributions made	(3,060)
Decrease in net OPEB obligation	–
Net OPEB obligation – beginning of year	–
Net OPEB obligation – end of year	$ –

The System's annual OPEB cost, the percentage of annual OPEB cost contributed to the OPEB Trust, and the net OPEB obligation for 2010 and 2009 are as follows (dollar amounts in thousands):

Fiscal Year Ended	**Annual OPEB Cost**	**Percentage of Annual OPEB Cost Contributed**	**Net OPEB Obligation**
		(In Thousands)	
December 31, 2010	**$ 3,782**	**100%**	**$ –**
December 31, 2009	$ 3,412	100%	–

13. Pension and Other Postretirement Benefits (continued)

Funded Status and Funding Progress

As of January 1, 2010, the most recent actuarial valuation date, the actuarial accrued liability for benefits was approximately $33,227,000, and the actuarial value of assets was $10,072,000, resulting in an unfunded actuarial accrued liability (UAAL) of approximately $23,155,000. The actuarial value of assets as a percentage of the actuarial accrued liability, or funded ratio, was 30.3%. The covered payroll (annual payroll of active employees covered by the OPEB Trust) was $234,739,000 and the ratio of the UAAL to the covered payroll was 10%.

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

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members up to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2010 actuarial valuation, the entry age actuarial cost method was used. The actuarial assumptions included an 8% investment rate of return and an annual health care cost trend and inflation rate of 5%. The actuarial value of assets was determined using techniques that spread the effects of short-term volatility in the market value of investments over a five-year period. The UAAL is being amortized as a level percentage of projected payroll on an open basis. The amortization period at December 31, 2010, was 30 years.

14. Commitments and Contingencies

The System's Board has approved various facility improvements and renovation projects. As of December 31, 2010, the System had outstanding contractual arrangements totaling $5,662,000 for architectural and construction services.

In 2009 and 2010, the System issued long-term debt, as described in Note 7, to fund the construction of capital projects at two of the System's locations. In connection with the construction program, the System entered into agreements for design, program management, and construction of those projects. The System had outstanding contracts totaling $272,551,000 at December 31, 2010.

At December 31, 2010 and 2009, the System was a defendant in certain pending civil litigation, and the System has notice of certain claims that have been asserted against it. In addition, unasserted possible claims exist for known and unknown incidents. The System covers its exposure for asserted and unasserted claims through a program of self-insurance. The System has accrued its best estimate of these contingent losses. The reserves for these contingent losses include estimates of the ultimate cost for both reported claims and claims incurred but not yet reported. In addition, the System has established a reserve in the amount of $1,200,000 to cover potential System exposure for medical malpractice claims arising from a limited number of System-employed physicians. The reserve will provide "tail coverage" for a physician's medical malpractice claim occurring prior to October 1, 2003, the period when such physicians were covered under a "claims made" medical malpractice policy.

The System also self-insures workers' compensation claims. The program provides for specific excess of loss reinsurance for the excess of $500,000 up to a maximum limit of $1,000,000 for any one accident or occurrence. The amounts provided for funding and the estimated liability are based on claims made and claims incurred but not yet reported. During the years ended December 31, 2010 and 2009, the System recognized expense of $2,275,000 and $2,835,000, respectively, associated with the workers' compensation program.

In 2006, the System affiliated with Bexar County's largest providers of health care services to the poor and indigent in a program called Bexar Regional Upper Payment Limit Program (Bexar Regional UPL Program). The program was approved by the Centers for Medicare & Medicare Services (CMS) in July 2006 and further reviewed and approved in April 2008. Through participation in the program, the affiliated hospitals increased the medical care and other services they provide to the poor and indigent. Some of these services are provided in System facilities.

14. Commitments and Contingencies (continued)

As a result of participating in the Bexar Regional UPL Program, the System has realized benefits of lower medical service costs amounting to $61,478,169 and $54,372,468 in 2010 and 2009, respectively. The System also incurred increased costs to supplement the state's funding for the affiliated providers in the amounts of $34,527,997 and $35,600,287 in 2010 and 2009, respectively.

In 2009, the System received a payment from the Health and Human Services Commission (HHSC) of the state of Texas for graduate medical education provided from 1999 to 2001. The payment was in response to an order issued by the 345th District Court, Travis County, Texas, in April 2003 requiring HHSC to reimburse teaching hospitals participating in the Texas Medicaid program according to the mandatory GME formula established by the Texas Legislature in 1997. HHSC has requested federal funding of the GME payment from the CMS. The Region VI CMS office in Dallas, Texas, has rejected the funding request and forwarded the request to the CMS central office for final resolution. The System recorded the amount received, $14.1 million, as a long-term deferred revenue in 2009, and in June 2010 the amount was returned to HHSC pending final resolution of the funding request.

15. Investment Risk

The disclosures required under GASB Statement No. 40 (GASB 40), *Deposit and Investment Risk Disclosures,* for University Health System are reflected below. Separate financial statements of the Plan include applicable investment disclosures.

(A) Credit Risk and Concentration of Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization (NRSRO). The System and CFHP, its affiliated nonprofit health maintenance organization (HMO), each have formal investment policies adopted by the Board of Managers and Board of Directors, respectively, that limit investment in securities based on an NRSRO credit rating. The System's investments are also subject to the Public Funds Investment Act (the Act), at Government Code Chapter 2256, and CFHP's investments are also subject to regulations enumerated in Title 28, Chapter 11 of the Texas Administrative Code (TAC) and Chapter 20A of the Texas Insurance Code (TIC).

15. Investment Risk (continued)

Investments authorized by the Act and the System's investment policy are limited to: obligations of the United States government or its agencies; repurchase agreements collateralized by obligations of the United States government or its agencies; investment pools with at least an AA-m or better rating by one nationally recognized rating service; commercial paper with a stated maturity of 270 days or less and a credit rating of A-1 or P-1 or its equivalent, by at least two nationally recognized credit rating agencies; certificates of deposit issued by a state bank, national bank, or a savings and loan association domiciled in Texas, with FDIC insurance and collateralized by obligations of the U.S. government or its agencies, with market value of 102% of the insured principal amount; bankers' acceptances of a bank organized and existing under the laws of the United States, whose short-term obligations are rated not less than A-1 or P-1 or its equivalent, by at least one nationally recognized rating agency, and with a stated maturity of 270 days or less; and no-load money market mutual funds registered by the Securities and Exchange Commission with a dollar-weighted-average stated maturity of 90 days or less, and an investment objective of a stable net asset value of one dollar.

Investments authorized by the TAC, TIC, and CFHP's investment policy are limited to obligations of the United States government or its agencies; certificates of deposit with a credit rating of Moody's A2 or S&P A; corporate obligations with a credit rating of Moody's A1 or S&P A+; municipal notes and bonds with a credit rating of Moody's Aaa or S&P AAA; auction rate securities with a credit rating of Moody's A2 or S&P A; and asset-backed securities with a credit rating of Moody's Aaa or S&P AAA.

Per GASB 40, unless there is information to the contrary, obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. GASB 40 also provides that securities with split ratings, or a different rating assignment between NRSROs, are disclosed using the rating indicative of the greatest degree of risk.

15. Investment Risk (continued)

The following table presents each applicable investment type grouped by rating as of December 31, 2010:

Investment Type	Fair Value	Rating
	(In Thousands)	
U.S. government, Treasury	$ 10,822	Exempt from disclosure
U.S. government, Treasury strips	1,667	AAA
Total U.S. government, guaranteed	12,489	
U.S. government, nonguaranteed:		
Federal Home Loan Bank notes	592,023	AAA
Federal National Mortgage Association notes	168,720	AAA
Federal Farm Credit Bank notes	140,005	AAA
Federal Home Loan Mortgage Corporation mortgage-backed securities	11	AAA
Government National Mortgage Association mortgage-backed securities	4	AAA
Total U.S. government, nonguaranteed	900,763	
Cash and cash equivalents – money market funds	329,652	AAA
Total cash and investments	$ 1,242,904	

*Securities comprise greater than 5% of the total.

15. Investment Risk (continued)

In accordance with the System's investment policy, the System has no limit on the amount of investments with a single authorized issuer, other than a 15% limit on repurchase agreements with a single issuer. As of December 31, 2010, the System was in compliance with this policy. According to GASB 40, concentration of credit risk is defined as more than 5% of the market value of the total portfolio invested in securities issued by one issuer. Investments with an explicit guarantee by the U.S. government are exempt from the disclosure requirement.

The System maintained no investments in derivatives at December 31, 2010 and 2009.

(B) Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of failure of a depository financial institution, the System will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The System's policy does not contain specific requirements to limit its exposure to custodial credit risk for deposits or investments. As of December 31, 2010, all investments are registered in the System's name.

15. Investment Risk (continued)

(C) Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair market value to changes in market interest rates. Interest rate risk inherent in the portfolio is measured by monitoring the segmented time distribution of the investments in the portfolio. The System's investment policy limits the maturity periods of its investments by type. The table below summarizes the System's segmented time distribution investment maturities in years by investment type as of December 31, 2010:

		Years		
	Fair Value	**< 1**	**1 to 5**	**6 to 10**
		(In Thousands)		
2010				
Money market	$ 329,652	$ 329,652	$ –	$ –
U.S. government, Treasury	10,822	4,692	5,108	1,022
U.S. government, Treasury strips	1,667	–	1,667	–
U.S. government, Federal Farm Credit Bank notes	140,005	63,009	76,033	963
U.S. government, Federal Home Loan Bank notes and Federal National Mortgage Association notes	760,743	357,720	402,502	521
U.S. government, mortgage-backed securities	15	4	11	–
Total	$ 1,242,904	$ 755,077	$ 485,321	$ 2,506

15. Investment Risk (continued)

(D) Reconciliation of Investments by Type to Balance Sheet Presentation

The following table presents each applicable investment grouped by type and balance sheet presentation at December 31, 2010:

Investment Type	Fair Value	Balance Sheet Line
	(In Thousands)	
Investments, at fair value:		
Money market	$ 140,674	
Cash	1,267	
	141,941	Cash and cash equivalents
U.S. government, guaranteed	39,202	Short-term investments
U.S. government, guaranteed	35,455	Other noncurrent investments
Cash	(712)	
Money market	51,768	
U.S. government, guaranteed	2,519	
U.S. government, nonguaranteed	113,122	
U.S. government, nonguaranteed asset-backed	4	
	166,701	Internally designated for capital acquisitions and improvements

15. Investment Risk (continued)

Investment Type	Fair Value	Balance Sheet Line
	(In Thousands)	
Money market	$ 9,294	
U.S. government, guaranteed	3,591	
U.S. government, nonguaranteed	134,972	
U.S. government, nonguaranteed asset-backed	11	
	147,868	Internally designated for contingency
Money market	371	
U.S. government, guaranteed	5,223	
U.S. government, nonguaranteed	4,563	
	10,157	Held by trustee for professional self-insurance
Cash	(9,560)	
Money market	81,947	
U.S. government, nonguaranteed	125,645	
	198,032	Project Fund series 2008 Certificates of Obligation
Money market	24,171	
U.S. government, nonguaranteed	257,561	
	281,732	Project Fund series 2009 Certificates of Obligation
Money market	11,024	
U.S. government, nonguaranteed	191,384	
	202,408	Project Fund series 2010 Certificates of Obligation
Money market	19,408	Certificate Fund
Total	$ 1,242,904	

Required Supplementary Information

University Health System
Bexar County, Texas

Schedule of Funding Progress –
University Health System Retiree Health Trust
(In Thousands)

Actuarial Valuation Date	**Actuarial Value of Assets**	**Actuarial Accrued Liability (AAL)**	**Unfunded AAL (UAAL)**
January 1, 2010	**$ 10,072**	**$ 33,227**	**$ 23,155**
January 1, 2009	6,783	32,303	25,520
January 1, 2008	2,689	28,099	25,410

Other Financial Information

University Health System
Bexar County, Texas

Schedule of Expenditures of Federal and State Awards

Year Ended December 31, 2010

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Expenditures
Federal Programs			
U.S. Department of Health and Human Services			
Direct awards:			
Family Planning Service Delivery Improvement Research Grants:			
UHS Male Health Program	93.974		$ 185,834
UHS Male Health Program	93.974		109,541
			295,375
State and Territorial and Technical Assistance: Capacity Development Minority HIV/AIDS Demonstration Program:			
The Latino AIDS Advocacy Project of South Texas	93.006		139,471
The Latino AIDS Advocacy Project of South Texas	93.006		99,792
			239,263
Special Projects of National Significance:			
Hepatitis C	93,238		3,624
Total direct awards			538,262
Indirect awards:			
Passed Through the Department of State Health Services			
Family Planning Services:			
Title X Family Planning Services	93.217		217,440
Title X Male Involvement	93.217		155,746
			373,186
Medical Assistance Programs:			
Title XIX Family Planning	93.778		263,609
Title XIX Family Planning	93.778		183,186
			446,795
Social Services Block Grant:			
Title XX Family Planning Services	93.667		997,770
Title XX Family Planning Services	93.667		729,764
			1,727,534

Schedule of Expenditures of Federal and State Awards (continued)

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Expenditures
Federal programs (continued)			
ARRA – Emergency Contingency Fund for Temporary Assistance for Needy Families (TANF) State Program Title XX Family Planning	93,714		$ 10,000
Refugee and Entrant Assistance State Administered Program:			
Refugee Program	93.556, 93.576		692,649
Refugee Program	93.556, 93.576		322,564
			1,015,213
Maternal and Child Health Services Block Grant to the States:			
Title V Child Health	93,994		
Title V Child Injury Prevention	93,994		60,968
Title V Prenatal	93.994		42,945
Title V Prenatal	93.994		39,761
			143,674
Centers for Disease Control and Prevention Investigations and Technical Assistance:			
Breast & Cervical Cancer	93,283		11,648
Breast & Cervical Cancer Patient Navigation	93,283		61,662
			73,310
HIV Prevention Activities Health Department Based			
HIV Rapid Testing to Clients Assessing Emergency Services	93.40		33,385
Passed Through Bexar County:		74-1557491	
HIV Emergency Relief Project Grants A	93.914		149,595
HIV Emergency Relief Project Grants A	93.914		1,366,070
HIV Emergency Relief Project Grants B (Service Delivery)	93.914		27,183
HIV Emergency Relief Project Grants B (Service Delivery)			409,325
HIV Emergency Relief Project Grants B (State Services)	93.914		201

University Health System
Bexar County, Texas

Schedule of Expenditures of Federal and State Awards (continued)

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Expenditures
Federal programs (continued)			
HIV Emergency Relief Project Grants B (State Services)	93.914		$ 81,635
Passed Through the University of Texas Health Science Center SA:		74-1586031	
Coordinated Services and Access to Research for Women, Infants, Children, and Youth:			
South Texas Family AIDS Network (Part D)	93.153		235,341
South Texas Family AIDS Network (Part D)	93.153		196,002
			431,343
Special Projects of National Significance:			
Women's HIV Entry, Access, and Retention in Treatment Initiative	93,928		35,861
Women's HIV Entry, Access, and Retention in Treatment Initiative	93,928		30,334
			66,195
Passed Through the City of San Antonio:			
Head Start	93,600		23,191
ARRA – Head Start	93,708		3,049
			26,240
Total indirect awards			6,380,884
Total federal awards			6,919,146
State programs			
Texas Health & Human Services Commission			
Texas Nurse-Family Partnership Program			519,563
Texas Nurse-Family Partnership Program			254,401
HIV Rapid Testing to Clients Assessing Emergency Services			23,761
Title V Family Planning			80,525
Title V Family Planning			202,425
Title V Primary Health Care			359

Schedule of Expenditures of Federal and State Awards (continued)

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Expenditures
Alamo Area Resource			$ 37,271
HIV/AIDS Health Improvement for Re-Entering Ex-Offenders			20,454
HIV/AIDS Health Improvement for Re-Entering Ex-Offenders			–
Cancer Prevention & Research Institute of Texas			65,236
A Su Salud			
Mammography Utilization Project			8,251
Total state awards			1,212,246
Total federal and state awards			$ 8,131,392

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