



**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Financial Statements  
June 30, 2018 and 2017  
(With Independent Auditors' Report Thereon)

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

**Table of Contents**

|  | <b>Page(s)</b> |
|--|----------------|
| Independent Auditors' Report   | 1-2            |
| Management's Discussion and Analysis (Unaudited)   | 3-13           |
| Basic Financial Statements:  |                |
| Statements of Net Position   | 14             |
| Statements of Revenues, Expenses, and Changes in Net Position  | 15             |
| Statements of Cash Flows   | 16-17          |
| Notes to Financial Statements  | 18-52          |
| Required Supplementary Information:  |                |
| Schedules of the Hospital's Contributions (Unaudited)  | 53             |
| Schedules of the Hospital's Proportionate Share of the Net Pension Liability (Unaudited)                               | 54             |
| Schedules of the Hospital's Proportionate Share of the Total Other Postemployment Benefit (OPEB) Liability (Unaudited) | 55             |



KPMG LLP  
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## Independent Auditors' Report

The Board of Directors  
University Hospital:

### Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activity of University Hospital (the Hospital), a component unit of the State of New Jersey, as of and for the years ended June 30, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements for the years then ended, as listed in the table of contents.

### Management's Responsibility for the Financial Statements

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

### Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

### Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of University Hospital as of June 30, 2018 and 2017, and the changes in financial position and, where applicable, cash flows thereof for the years then ended, in accordance with U.S. generally accepted accounting principles.



### **Emphasis of a Matter**

As discussed in note 2(s) to the financial statements, in 2018, the Hospital adopted Governmental Accounting Standards Board (GASB) Statement 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. Our opinion is not modified with respect to this matter.

### **Other Matters**

#### *Required Supplementary Information*

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 13 and the Schedules of the Hospital's Contributions, the Schedules of the Hospital's Proportionate Share of the Net Pension Liability, and the Schedule of the Hospital's Proportionate Share of the Other Postemployment Benefit (OPEB) Liability on pages 53 through 55, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the GASB who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated March 29, 2019 on our consideration of the Hospital's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of the Hospital's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Hospital's internal control over financial reporting and compliance.

**KPMG LLP**

March 29, 2019

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

This section of the Hospital's annual financial report presents management's discussion and analysis of the summarized assets, liabilities, and net position as of June 30, 2018 compared to June 30, 2017 balances and June 30, 2017 compared to June 30, 2016 balances. This section also presents management's discussion and analysis of the financial performance during the years ended June 30, 2018 compared to June 30, 2017 and June 30, 2017 financial performance compared to June 30, 2016. The purpose is to provide an objective analysis of the financial activities of the Hospital based on currently known facts, decisions, and conditions. Please read it in conjunction with the financial statements, which follow this section.

**New Jersey Medical and Health Sciences Education and Restructuring Act**

In accordance with Public Law 2012, c. 45, the New Jersey Medical and Health Sciences Education and Restructuring Act (the Restructuring Act), effective July 1, 2013, the Hospital was separated from the University of Medicine and Dentistry of New Jersey (UMDNJ) as a new stand-alone entity was formed. The Hospital continues to be the primary teaching hospital for the Newark-based schools of the Rutgers School of Biomedical and Health Sciences.

The mission of the Hospital is to improve the quality of life for everyone who comes in contact with the Hospital through effective patient care, education, research, and community service. As the core teaching facility in Newark, the Hospital is the center of referral for many of the State's most advanced medical services and specialty care programs. The Hospital is committed to education, primary care, and specialized referral.

The Hospital shall maintain its public mission to provide a comprehensive healthcare program and services to the greater Newark community, including outreach and mobile health services, as well as services in collaboration with the Newark-based schools of the Rutgers School of Biomedical and Health Sciences. The Hospital is committed to act in accordance with the spirit and intent of the "Agreements Reached between Community and Government Negotiators Regarding New Jersey College of Medicine and Dentistry and Related Matters of April 30, 1968."

**Overview of the Financial Statements**

This annual report consists of two parts – management's discussion and analysis and the basic financial statements.

The basic financial statements include statements of net position, statements of revenues, expenses, and changes in net position, statements of cash flows, and notes to financial statements. These statements present the financial position of the Hospital at June 30, 2018 and 2017, and the changes in net position and its financial activities for the years then ended. The statements of net position include all of the Hospital's assets and liabilities in accordance with U.S. generally accepted accounting principles. The statements of revenues, expenses, and changes in net position, present each year's activities on the accrual basis of accounting, that is, when services are provided or obligations are incurred, not when cash is received or bills are paid. The financial statements also report the Hospital's net position and how it has changed. Net position, or the difference between assets and liabilities, deferred inflows and deferred outflows, is a way to measure the Hospital's financial health or position. The statements of cash flows provide relevant information about each year's cash receipts and cash payments and classify them as to operating, noncapital financing, capital and related financing, and investing activities. Notes to financial statements explain information in the statements and provide more detailed data.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

A summarized comparison of the Hospital's combined assets, liabilities, and net position at June 30, 2018, 2017, and 2016 are as follows (in thousands):

|  | <u>2018</u>         | <u>2017</u>      | <u>2016</u>      |
|--|---------------------|------------------|------------------|
| <b>Assets:</b>                         |                     |                  |                  |
| Current assets:                        |                     |                  |                  |
| Cash and cash equivalents              | \$ 63,989           | 79,400           | 100,512          |
| Restricted investments                 | 6,114               | 6,042            | 6,334            |
| Patient accounts receivable, net       | 83,100              | 80,778           | 75,468           |
| Other current assets                   | 67,182              | 55,858           | 37,542           |
| Noncurrent assets:                     |                     |                  |                  |
| Restricted investments, net            | 89,755              | 104,857          | 125,323          |
| Prepaid bond insurance                 | 16,143              | 16,730           | 17,317           |
| Capital assets, net                    | 206,004             | 198,475          | 204,689          |
| Total assets                           | <u>\$ 532,287</u>   | <u>542,140</u>   | <u>567,185</u>   |
| Deferred outflows of resources         | \$ 175,218          | 151,254          | 58,981           |
| <b>Liabilities:</b>                    |                     |                  |                  |
| Current liabilities                    | \$ 107,006          | 92,550           | 102,428          |
| Long-term debt and capital leases, net | 342,709             | 346,480          | 347,457          |
| Pension liability                      | 541,572             | 552,097          | 410,860          |
| Other long-term liabilities            | 18,657              | 21,703           | 20,720           |
| Total liabilities                      | <u>\$ 1,009,944</u> | <u>1,012,830</u> | <u>881,465</u>   |
| Deferred inflows of resources          | \$ 76,673           | —                | 2,028            |
| <b>Net position:</b>                   |                     |                  |                  |
| Net investment in capital assets       | \$ 10,604           | 15,274           | 40,762           |
| Unrestricted                           | <u>(389,716)</u>    | <u>(334,719)</u> | <u>(298,089)</u> |
| Total net position                     | <u>\$ (379,112)</u> | <u>(319,445)</u> | <u>(257,327)</u> |

*Overall Financial Position and Operations*

The Hospital's total net position from the period June 30, 2017 to June 30, 2018, decreased by \$59.7 million. Net investment in capital assets decreased by \$4.7 million during 2018. The Hospital's unrestricted position decreased \$55 million from (\$334.7) million at June 30, 2017 to (\$389.7) million at June 30, 2018. The decrease was due to \$44.4 million of pension expense during fiscal 2018 related to GASB 68. (Pension expense, without consideration for GASB 68, was \$11.4 million during 2018). Without giving effect to the pension expense for GASB 68, the Hospital's unrestricted position decreased by \$10.6 million in fiscal year 2018.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

The Hospital's total net position from the period June 30, 2016 to June 30, 2017, decreased by \$62.1 million. Net investment in capital assets decreased by \$25.5 million during 2017 as the Hospital's depreciation exceeded purchases of capital assets and decrease in capital reserve funds (unspent proceeds related to debt). The Hospital's unrestricted position decreased \$36.6 million from (\$298.1) million at June 30, 2016 to (\$334.7) million at June 30, 2017. The decrease was due to \$46.9 million of pension expense during fiscal 2017 related to GASB 68 (Pension expense, without consideration for GASB 68, was \$9.2 million during 2017). Without giving effect to the pension expense for GASB 68, the Hospital's unrestricted position increased by \$10.3 million in fiscal year 2017.

Significant financial ratios are as follows:

|   | <u>2018</u> | <u>2017</u> | <u>2016</u> |
|---|-------------|-------------|-------------|
| Current ratio                           | 2.06        | 2.40        | 2.15        |
| Quick ratio                             | 1.21        | 1.53        | 1.89        |
| Days cash on hand                       | 34.19       | 45.45       | 59.73       |
| Net days revenue in patient receivables | 58.69       | 59.38       | 55.54       |

The current ratio, quick ratio, and day's cash on hand are common liquidity indicators. The net day's revenue in patient receivables is an indicator of how quickly the Hospital collects its patient receivables.

*Variances in Financial Statements*

In this section, the Hospital explains the reasons for certain financial statement items with variances relating to 2018 amounts compared to 2017 and, where appropriate, 2017 amounts compared to 2016.

**Statement of Net Position**

*Cash and cash equivalents* – decreased by \$15.4 million as compared to the prior year. This can be primarily attributed to the timing of the NJ state subsidy of \$6.7 million, as well as \$3.7 million in State Appropriation payments for fiscal year (FY) 2018 received in FY 2019 and \$2.5 million of capital acquisitions in FY 2018 not recovered from restricted investments. Cash and cash equivalents decreased by \$21.1 million from June 30, 2016 to June 30, 2017, which can be attributed to payments made for retroactive wage increases of \$13.9 million, as well as the reduction of \$10 million from State Appropriation payments received during 2017.

*Patient accounts receivable, net* – increased \$2.3 million from June 30, 2017 to June 30, 2018 primarily due to a \$1.2 million decrease in the reconciled Medicare periodic interim payments (PIP) balance and due to the increase in net patient service revenue as compared to the prior year. Days in-patient accounts receivable of 58.69 are 0.7 days less than the prior year. Patient accounts receivable, net increased \$5.3 million from June 30, 2016 to June 30, 2017 primarily due to a \$4.4 million decrease in the reconciled Medicare PIP balance as compared to the prior year. Days in-patient accounts receivable of 59.38 are 3.84 days more than the prior year.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

*Other current assets* – increased \$11.3 million from June 30, 2017 to June 30, 2018. This is due primarily from delayed payments from the State of NJ for charity care and other subsidies of \$6.7 million, and appropriation of \$3.7 million, all of which was received in July 2018 and the 340B program pharmacy reimbursement receivable increased \$0.8 million. Other current assets increased \$18.3 million from June 30, 2016 to June 30, 2017 due to an increase in the NJ Department of Health Delivery System Reform Incentive Payment (DSRIP) program receivable of \$8.2 million, an \$8.4 million increase in receivables due from Rutgers University for reconciled rent payments, as well as \$1.4 million for EMS services provided to the City of Newark.

*Restricted investments (current and long term)* – decreased by \$15.0 million from June 30, 2017 to June 30, 2018 due to the drawdown of capital funds used in the financing of routine and emergency capital needs and technology to replace the services formerly provided by Rutgers University and capital upgrades, as well as additions to various services and facilities. Restricted investments decreased by \$20.7 million from June 30, 2016 to June 30, 2017 due to the drawdown of capital funds used in the financing of routine and emergency capital needs and technology to replace the services formerly provided by Rutgers University and capital upgrades, as well as additions to various services and facilities.

*Prepaid bond insurance* – decreased \$0.6 million from June 30, 2017 to June 30, 2018 and from June 30, 2016 to June 30, 2017 due to amortization. The cost of the prepaid bond insurance was \$17.6 million and \$1.5 million has been amortized as of June 30, 2018 while \$0.9 has been amortized as of June 30, 2017.

*Capital assets, net* – increased \$7.5 million from June 30, 2017 to June 30, 2018 due mainly to \$31.5 million of acquisitions that were partially offset by current year depreciation of \$20.8 million. In addition, Rutgers University's capital lease revaluation resulted in a reduction of the leased asset of \$2.6 million. Capital assets, net decreased \$6.2 million from June 30, 2016 to June 30, 2017 due to \$14.3 million of acquisitions that were offset by current year depreciation in the amount of \$20.5 million.

*Accounts payable and accrued expenses* – increased by \$3.1 million from June 30, 2017 to June 30, 2018 and \$9.8 million from June 30, 2016 to June 30, 2017 due to timing of normal operating activity. The Hospital continues with the practice of paying vendors within 45 days after providing services. The Hospital had days in accounts payable of 58.55 and 55.28 days as of June 30, 2018 and 2017, respectively.

*Accrued salaries and related payroll taxes* – increased by \$5.1 million from June 30, 2017 to June 30, 2018 as a result of estimated retroactive wage increases of \$4.0 million, as well as \$0.7 million change for accrued days. Accrued salaries and related payroll taxes decreased by \$17.3 million from June 30, 2016 to June 30, 2017 as a result of payments for retroactive wage increases of \$13.9 million, as well as \$5.9 million change in prior years estimated wage increase.

*Due to Rutgers University* – increased approximately \$9.3 million from June 30, 2017 to June 30, 2018 and \$3.9 million from June 30, 2016 and June 30, 2017 as the Hospital and Rutgers University continue to work toward a collegial relationship that would allow both entities to pay within agreed timeframes. The balance at June 30, 2018 and 2017 represents liabilities for both clinical and facility services. The payment timeframes depend on the service ranging from advanced payments to 45 days from date of invoice.



**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

*Accrued workers' compensation* – decrease \$2.8 million from June 30, 2017 to June 30, 2018 due to an updated actuarial analysis. The Hospital continues to record this liability on an undiscounted basis. Accrued workers' compensation decreased \$1.2 million from June 30, 2016 to June 30, 2017 due to an updated actuarial analysis. The Hospital continues to record this liability on an undiscounted basis.

*Estimated third-party payor settlements* – decreased by \$3.3 million from June 30, 2017 to June 30, 2018 primarily due to settlements of prior year cost reports and changes in reserve estimates. Estimated third-party payor settlements decreased by \$0.9 million from June 30, 2016 to June 30, 2017 primarily due to settlements of prior year cost reports and changes in reserve estimates.

*Current portion of long-term debt* – increased slightly from June 30, 2017 to June 30, 2018 as a result of the principal amount due the New Jersey Educational Facilities Authority (NJEFA) and capital lease obligations. Principal payments on the Series 2015A bonds are not set to commence until July 1, 2021. Current portion of long-term debt increased slightly from June 30, 2016 to June 30, 2017 as a result of the principal amount due the NJEFA and capital lease obligations. Principal payments on the Series 2015A bonds are not set to commence until July 1, 2021.

*Long-term debt* – decreased \$3.8 million from June 30, 2017 to June 30, 2018, as a result of the amortization of the net bond premium and due to the Rutgers University's capital lease revaluation, which resulted in a reduction of the lease liability by \$2.6 million. Long-term debt decreased \$1.0 million from June 30, 2016 to June 30, 2017, as a result of the amortization of the net bond premium.

*Pension liability, deferred inflows of resources, and deferred outflows of resources* – decreased \$10.5 million, increased \$76.7 million and increased \$23.9 million respectively, from June 30, 2017 to June 30, 2018 due to changes in assumptions and proportion. Pension liability, deferred inflows of resources, and deferred outflows of resources increased \$141.2 million, decreased \$2.0 million, and increased \$92.3 million respectively, from June 30, 2016 to June 30, 2017 due to changes in assumptions and proportion.

**Changes in Components of Net Position**

*Net investment in capital assets* – decreased \$4.7 million from June 30, 2017 to June 30, 2018 as a result of \$15.4 million of capital additions not attributable to capital reserve funds reduced by depreciation expense of \$20.7 million. Net investment in capital assets decreased \$25.5 million from June 30, 2016 to June 30, 2017 as a result of the increase in related capital debt mainly due to the reduction of capital reserve funds of \$20.4 million.

*Unrestricted net position*, other than those mentioned above, resulted in a decrease of \$55 million for year 2018. Unrestricted net position, other than those mentioned above, resulted in a decrease of \$36.6 million for year 2017.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

A summarized comparison of the Hospital's revenues, expenses, and changes in net position for the years ended June 30, 2018, 2017, and 2016 are as follows (in thousands):

|  | <u>2018</u>         | <u>2017</u>      | <u>2016</u>      |
|--|---------------------|------------------|------------------|
| Operating revenues:  |                     |                  |                  |
| Net patient service revenue  | \$ 516,789          | 496,544          | 495,993          |
| Grants revenue   | 5,603               | 5,335            | 6,409            |
| Other revenue  | 19,876              | 26,587           | 20,936           |
|  | <u>542,268</u>      | <u>528,466</u>   | <u>523,338</u>   |
| Operating expenses:  |                     |                  |                  |
| Personnel services, fringes benefits, pension,<br>physician, and resident fees | 486,602             | 469,083          | 442,338          |
| Other postretirement benefit expense   | 36,409              | —                | —                |
| Supplies and other expenses  | 225,320             | 217,113          | 210,566          |
| Depreciation   | 20,796              | 20,493           | 20,256           |
|  | <u>769,127</u>      | <u>706,689</u>   | <u>673,160</u>   |
| Operating loss   | (226,859)           | (178,223)        | (149,822)        |
| Nonoperating income (expense):   |                     |                  |                  |
| Appropriations from the State of New Jersey                                    | 141,786             | 129,843          | 137,348          |
| Other postemployment benefit revenue   | 36,409              | —                | —                |
| Contributions and special events   | 108                 | —                | —                |
| Fundraising expenses   | (117)               | —                | —                |
| Interest income  | 1,091               | 463              | 156              |
| Interest expense   | (15,167)            | (15,190)         | (13,448)         |
|  | <u>(62,749)</u>     | <u>(63,107)</u>  | <u>(25,766)</u>  |
| Loss before other changes in<br>net position                                   | (62,749)            | (63,107)         | (25,766)         |
| Other changes in net position:   |                     |                  |                  |
| Capital contributions  | 3,082               | 989              | 3,291            |
|  | <u>(59,667)</u>     | <u>(62,118)</u>  | <u>(22,475)</u>  |
| Decrease in net position   | (59,667)            | (62,118)         | (22,475)         |
| Net position at beginning of year  | <u>(319,445)</u>    | <u>(257,327)</u> | <u>(234,852)</u> |
| Net position at end of year  | <u>\$ (379,112)</u> | <u>(319,445)</u> | <u>(257,327)</u> |

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

**Statements of Revenues, Expenses, and Changes in Net Position**

*Net patient service revenue* – Net patient service revenue relates to patient care services, under contractual arrangements with governmental payors and private insurers. Net patient service revenues, excluding subsidies, 2018 exceeded 2017 by \$10.2 million, primarily due to an increase in observation volume, as well as \$5.5 million in additional Medicaid Graduate Medical Education (GME) reimbursement and the additional of an out-patient clinic. Net patient service revenues, excluding subsidies, 2017 exceeded 2016 by \$8.6 million, primarily due to an increase in observation volume, as well as \$6.5 million in additional GME reimbursement.

The Hospital's net patient service revenues totaled \$516.8 million (including patient subsidies) in 2018. The Hospital is a major source of primary care and serves as the safety net hospital for the inner city municipalities of Newark, East Orange, Irvington, and Orange. The Hospital's role in the community is reflected in its payor mix and commitment to the medically indigent. It has traditionally been the largest provider of charity care services in the state, and Medicaid and uninsured patients account for almost 58% of its gross revenues. As a result, the Hospital must deal with the financial impact of revenue collections and reimbursements related to these patients and their payors.

The majority of the Hospital's admissions are initially treated in the emergency/trauma department. Emergency room visits of 91,700 in 2018 were over slightly from 2017 by 1,125 visits. Inpatient discharges for 2018, which account for approximately 68% of the Hospital's net patient service revenues, were over 2017 by 1.4%. Clinic visits for 2018, which generate outpatient revenues, increased from 2017 levels by 3.6%. Emergency room visits of 90,575 in 2017 were under slightly from 2016 by 185 visits. Inpatient discharges for 2017, which account for approximately 70% of the Hospital's net patient service revenues, were under 2016 by 1.9%. Clinic visits for 2017, which generate outpatient revenues, decreased from 2016 levels by 4.2%.

The level of charity care services provided by the Hospital represents nearly 8.2% of its overall patient care services. Charity care funding from the State of New Jersey (the State) totaled \$48.1 million and \$40.4 million in 2018 and 2017, respectively. Charity care funding is based upon Medicaid reimbursement rates, which have historically been in the range of 60 to 70% of cost. The level of charity care funding is critical to the Hospital's financial results.

*Patient subsidies* – The Hospital received a total of \$67.1 million in patient subsidies payments in 2018 with the major components represented by payments of \$48.1 million for the New Jersey Charity Care Subsidy Program and \$18.2 million for the DSRIP Program. The Hospital received a total of \$57.1 million in patient subsidies payments in 2017 with the major components represented by payments of \$40.4 million for the New Jersey Charity Care Subsidy Program and \$15.9 million for the DSRIP Program. The Hospital's \$10.0 million overall increase in subsidy funding from 2018 to 2017 is mainly attributable to the increase of the charity care subsidy of \$7.7 million and the recording of the DSRIP of \$2.4 million. While the overall charity care funding pool was reduced by \$50.0 million, the increase to UH can be attributed to the fact that the state has allocated more of its funding to safety net hospitals. A result of the overall success of the Affordable Care Act in providing Medicaid coverage to those previously uninsured.

*Other Revenue* – was \$19.9 million for the year ended June 30, 2018 compared to \$26.6 million for the year ended June 30, 2017 for a decrease of \$6.7 million. This was mainly due to the settlement of rent receivable of \$5.0 million from Rutgers University in fiscal year 2017.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

*Personnel services, fringe benefits, pension, physician, and resident fees* – were \$486.6 million for the year ended June 30, 2018 and were unfavorable by \$14.6 million compared to prior year. Personnel services costs for the year ended June 30, 2018 of \$260.8 million were \$17.5 million over 2017, which was mainly due to an increase in 2018 full-time equivalents (FTEs) of 3,351 compared to 3,266 for 2017. In addition to the increase in FTEs, payroll liabilities increased \$4.0 million for prior year retroactive accruals for both union and nonunion employees' salary adjustments and settlements. Pension costs \$55.8 million for the year ended June 30, 2018 relating to GASB 68 remained flat compared to prior year. Cost for medical staff and residents for the year ended June 30, 2018 of \$80.1 million contracted with Rutgers University increased by \$4.6 million as compared to the prior year. Personnel services, fringe benefits, pension, physician, and resident fees were \$469 million for the year ended June 30, 2017 and were unfavorable by \$26.7 million compared to June 30, 2016. This was due mainly to an increase in pension costs related to GASB 68 for approximately \$24.8 million.

*Other postemployment benefits expense* – The FY 2018 of \$36.4 million of other postemployment benefit (OPEB) expense represents the Hospital's proportionate share of OPEB expenses under GASB 75. This expense is equal to the OPEB nonoperating income that was recognized in FY 2018. See note 10 for additional information on OPEB.

*Supplies and other expenses* – increased by \$8.2 million from June 30, 2017 to June 30, 2018 and \$6.6 million from June 30, 2016 to June 30, 2017. This increase in supplies can be attributed to economic factor adjustments.

*State appropriations* – The Hospital recorded \$141.8 million in State Appropriations in 2018. These amounts include \$97.2 million for fringe benefits of Hospital employees paid by the State, \$0.7 million malpractice costs and a special Higher Education Appropriation of \$43.9 million for those expenses incurred as a result of the New Jersey Medical and Sciences Education Restructuring Act and Institutional Support. The Hospital recorded \$129.8 million in State Appropriations in 2017. These amounts include \$96.0 million for fringe benefits of Hospital employees paid by the State, nominal malpractice costs and a special Higher Education Appropriation of \$33.8 million for those expenses incurred as a result of the New Jersey Medical and Sciences Education Restructuring Act and Institutional Support.

*Other postemployment benefits nonoperating income* – The FY 2018 of \$36.4 million of other postemployment benefits nonoperating income represents the Hospital's proportionate share of OPEB expenses under GASB 75. This noncash nonoperating income is equal to the OPEB expenses that were recognized in FY 2018. See note 10 for additional information on OPEB.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

**Capital Assets, Net and Long-Term Debt Activity**

*Capital Assets, Net*

At June 30, the Hospital had capital assets, net of accumulated depreciation, as shown in the table below (in thousands of dollars):

|                                      | <u>2018</u>       | <u>2017</u>    | <u>2016</u>    |
|--------------------------------------|-------------------|----------------|----------------|
| Land and land improvements           | \$ 1,598          | 1,598          | 1,598          |
| Buildings and leasehold improvements | 317,206           | 309,693        | 310,452        |
| Equipment                            | 236,475           | 237,516        | 226,300        |
| Capital leases                       | 73,851            | 77,031         | 77,031         |
| Construction in progress             | 29,612            | 5,094          | 1,973          |
| Total                                | <u>658,742</u>    | <u>630,932</u> | <u>617,354</u> |
| Less accumulated depreciation        | <u>452,738</u>    | <u>432,457</u> | <u>412,665</u> |
| Net capital assets                   | <u>\$ 206,004</u> | <u>198,475</u> | <u>204,689</u> |

The Hospital had 2018 additions to capital assets as follows:

- \$31.5 million in overall additions with \$6.4 million in major movable equipment comprises patient furnishings and medical equipment and investments in information technology system upgrades, as well as \$25.1 million in renovations, which includes building renovation projects and a sprinkler system upgrade. The estimate to complete is approximately \$21.8 million.

The Hospital had 2017 additions to capital assets as follows:

- \$11.9 million in major movable equipment comprises patient furnishings and medical equipment and investments in information technology system upgrades, as well as \$2.4 million in renovations, which includes building renovation projects and a sprinkler system upgrade.

More detailed information about the Hospital's capital assets is presented in note 6 to the financial statements.

*Long-Term Debt*

At June 30, 2018, the Hospital has approximately \$269 million in long-term debt financing. On December 22, 2015, the Hospital issued \$255 million of New Jersey Healthcare Facilities Financing Authority (NJHCFFA) Series 2015A Bonds. Total proceeds from the sale were \$295.8 million and included a net premium of \$15.8 million, as well as \$25.0 million from trustee-held debt service and reserve funds. Proceeds from the sale were used to; (i) defease \$150.0 million of NJHCFFA Bond Anticipation Notes (BAN) debt; (ii) fund current debt service reserve requirements of \$17.3 million; (iii) fund bond insurance costs of \$17.6 million; (iv) paying bond issuance costs of \$2.7 million; and (v) fund various capital projects consisting of routine and emergency capital expenditures, information systems, and technology to replace the services provided by Rutgers University and capital upgrades and additions to various services and facilities, including the cancer program, diagnostic imaging services, and additional operating and procedure rooms and HVAC upgrades.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

The Series 2015A Notes were placed by the Authority with TD Bank, National Association, as Trustee. The Hospital entered into a Loan Agreement (the Loan Agreement) with the Authority relating to the Series 2015A bonds. A security feature for this obligation is provided by a lock box arrangement with the Trustee, TD Bank, N.A. Debt service requirements will be funded by unrestricted state appropriations, including state charity pools, DSRIP, GME, and individual state supplemental appropriations that will flow through the lock box. Any excess funds will then be released to the Hospital for operations. As of July 5, 2018, the underlying credit rating for the Hospital was BB- from Fitch Ratings.

Principal payments on the bonds will be due annually and are not set to commence until July 1, 2021. Interest will be paid semiannually on July 1 and January 1, with the first payment due July 1, 2016. The bonds are set at fixed interest rates and are as follows: (i) \$65.3 million in serial bonds at 5.000%, (ii) \$78.2 million in term bonds at 4.125%, and (iii) \$111.5 million in term bonds at 5.000%.

In addition, the Hospital assumed a portion of UMDNJ, New Jersey Educational Facilities Authority's, Higher Education Capital Improvement Fund, Series A (as revised) in the amount of \$0.7 million. The debt bears interest at fixed rates and requires annual principal payments until August 2020. More detailed information about the Hospital's long-term debt is presented in note 8 to the financial statements.

On July 1, 2013, the Hospital entered into five capital lease agreements with Rutgers, the State University of New Jersey for space in various locations on its Newark campus. The agreements are for 76 years and require monthly rent payments in advance. The Hospital has capitalized the present value of the lease payments, based on the Hospital's incremental borrowing rate, and will amortize the asset over the estimated useful life of each of the buildings. During 2018, there were amendments to the lease terms and which resulted in a re-evaluation of the lease liability resulting in a reduction of the lease liability by \$2.6 million.

### **Hospital Issues and Challenges**

The Hospital continues to adapt to the ever-increasing fiscal challenges placed on healthcare institutions in the New Jersey metropolitan area. Specifically, these challenges include the following:

Potential reductions in Medicaid and Medicare reimbursements due to state and federal budget reductions

Continued implementation of Health Care Exchanges and its effect on the uninsured

Federal Disproportionate Share Hospital (DSH) funding cuts

Reductions in Newark EMS services reimbursement

Penetration of managed care and tiered health plans in the market place

Uncertainty of Delivery System Reform Incentive Payments (DSRIP)

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Management's Discussion and Analysis (Unaudited)  
June 30, 2018, 2017, and 2016

The Hospital has responded to these significant challenges by managing labor and staffing more efficiently, as well as eliminating waste and duplication in order to offset unanticipated operating expenses. In addition, Hospital administration has developed monthly monitoring reporting tools to help management target and use benchmark data as a means of controlling costs and enhance productivity. Hospital administration has also identified performance initiatives intended to develop new services and revenue streams, increase patient volume, as well as restructure and streamline throughput processes.

**Contacting the Hospital's Financial Management**

This financial report provides the citizens of Newark, the Hospital's patients, bondholders, and creditors with a general overview of the Hospital's finances and operations. If you have questions about this report or need additional financial information, please contact Thomas Daly, Chief Financial Officer, University Hospital, 150 Bergen Street, Newark, NJ 07103.

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

Statements of Net Position

June 30, 2018 and 2017

(In thousands)

| <b>Assets</b>  | <u><b>2018</b></u> | <u><b>2017</b></u> |
|--|--------------------|--------------------|
| <b>Current assets:</b>   |                    |                    |
| Cash (note 3)  | \$ 63,989          | 79,400             |
| Restricted investments (note 7)  | 6,114              | 6,042              |
| Patient accounts receivable, net (note 5)                                | 83,100             | 80,778             |
| Due from State of New Jersey   | 30,819             | 19,190             |
| Supplies   | 17,934             | 18,231             |
| Grants receivable  | 4,214              | 1,453              |
| Other current assets   | <u>14,215</u>      | <u>16,992</u>      |
| Total current assets   | <u>220,385</u>     | <u>222,086</u>     |
| <b>Noncurrent assets:</b>  |                    |                    |
| Restricted investments (notes 7 and 8)                                   | 89,755             | 104,849            |
| Prepaid bond insurance   | 16,143             | 16,730             |
| Capital assets, net (notes 6 and 8)                                      | <u>206,004</u>     | <u>198,475</u>     |
| Total noncurrent assets  | <u>311,902</u>     | <u>320,054</u>     |
| Total assets   | 532,287            | 542,140            |
| <b>Deferred Outflows of Resources</b>                                    |                    |                    |
| Pension related (note 10)  | <u>175,218</u>     | <u>151,245</u>     |
| Total assets and deferred outflows of resources                          | <u>\$ 707,505</u>  | <u>693,385</u>     |
| <b>Liabilities</b>   |                    |                    |
| <b>Current liabilities:</b>  |                    |                    |
| Accounts payable and accrued expenses                                    | \$ 36,330          | 33,188             |
| Accrued salaries and related payroll taxes                               | 17,839             | 12,698             |
| Accrued vacation and sick pay  | 11,991             | 12,614             |
| Due to Rutgers University (note 9)                                       | 33,997             | 24,709             |
| Current portion of accrued claims liability (note 11)                    | 5,209              | 4,971              |
| Estimated third-party payor settlements, net (note 11)                   | 661                | 3,914              |
| Current portion of long-term debt and capital lease obligations (note 8) | 354                | 207                |
| Other current liabilities  | <u>625</u>         | <u>257</u>         |
| Total current liabilities  | <u>107,006</u>     | <u>92,558</u>      |
| <b>Noncurrent liabilities:</b>   |                    |                    |
| Accrued claims liability, net of current portion (note 11)               | 18,657             | 21,695             |
| Capital lease obligations, net of current portion (note 8)               | 73,589             | 76,497             |
| Long-term debt (note 8)  | 269,120            | 269,983            |
| Pension liability (note 10)  | <u>541,572</u>     | <u>552,097</u>     |
| Total noncurrent liabilities   | <u>902,938</u>     | <u>920,272</u>     |
| Total liabilities  | <u>1,009,944</u>   | <u>1,012,830</u>   |
| <b>Deferred Inflows of Resources</b>                                     |                    |                    |
| Pension related (note 10)  | <u>76,673</u>      | —                  |
| Total liabilities and deferred inflows of resources                      | <u>1,086,617</u>   | <u>1,012,830</u>   |
| Commitments and contingencies (note 11)                                  |                    |                    |
| <b>Net Position</b>  |                    |                    |
| Net investment in capital assets   | 10,604             | 15,274             |
| Unrestricted   | <u>(389,716)</u>   | <u>(334,719)</u>   |
| Total net position   | <u>(379,112)</u>   | <u>(319,445)</u>   |
| Total liabilities and net position                                       | <u>\$ 707,505</u>  | <u>693,385</u>     |

See accompanying notes to financial statements.



**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Statements of Revenues, Expenses, and Changes in Net Position  
Years ended June 30, 2018 and 2017  
(In thousands)

|   | <u>2018</u>         | <u>2017</u>      |
|---|---------------------|------------------|
| Operating revenues:   |                     |                  |
| Net patient service revenue (notes 4, 5, and 11)              | \$ 516,789          | 496,544          |
| Grants revenue  | 5,603               | 5,335            |
| Other revenue   | 19,876              | 26,587           |
| Total operating revenues                                      | <u>542,268</u>      | <u>528,466</u>   |
| Operating expenses:   |                     |                  |
| Personnel services  | 260,781             | 245,523          |
| Contracted physician and resident fees (note 9)               | 80,109              | 75,679           |
| Fringe benefits (notes 2 and 10)                              | 89,898              | 91,765           |
| Other postemployment benefits (note 10)                       | 36,409              | —                |
| Pension (note 10)   | 55,814              | 56,116           |
| Supplies and other expenses (note 9)                          | 225,320             | 217,113          |
| Depreciation (note 6)   | 20,796              | 20,493           |
| Total operating expenses                                      | <u>769,127</u>      | <u>706,689</u>   |
| Operating loss  | (226,859)           | (178,223)        |
| Nonoperating income (expenses):                               |                     |                  |
| Appropriations from the State of New Jersey (notes 10 and 11) | 141,786             | 129,843          |
| Other postemployment benefits (note 10)                       | 36,409              | —                |
| Contributions and special events                              | 108                 | —                |
| Fundraising expenses  | (117)               | —                |
| Interest income   | 1,091               | 463              |
| Interest expense  | (15,167)            | (15,190)         |
| Loss before other changes in net position                     | <u>(62,749)</u>     | <u>(63,107)</u>  |
| Other changes in net position:                                |                     |                  |
| Capital contributions funded by grantors and donors           | 3,082               | 989              |
| Total other changes in net position                           | <u>3,082</u>        | <u>989</u>       |
| Decrease in net position                                      | (59,667)            | (62,118)         |
| Net position at beginning of year                             | <u>(319,445)</u>    | <u>(257,327)</u> |
| Net position at end of year                                   | <u>\$ (379,112)</u> | <u>(319,445)</u> |

See accompanying notes to financial statements.

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

Statements of Cash Flows

Years ended June 30, 2018 and 2017

(In thousands)

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| Cash flows from operating activities:                                |             |             |
| Cash received from patients and third-party payors                   | \$ 503,418  | 490,332     |
| Receipts from grants   | 2,843       | 6,709       |
| Other receipts   | 19,875      | 26,587      |
| Cash paid for personnel services                                     | (256,263)   | (262,979)   |
| Cash paid for contracted physician and resident fees                 | (72,369)    | (82,446)    |
| Cash paid for fringe benefits  | (12,951)    | (7,380)     |
| Cash paid for supplies and other expenses                            | (219,058)   | (217,258)   |
| Net cash used in operating activities                                | (34,505)    | (46,435)    |
| Cash flows from noncapital financing activity:                       |             |             |
| Cash appropriations received from State of New Jersey and other      | 43,830      | 33,841      |
| Net cash provided by noncapital financing activity                   | 43,830      | 33,841      |
| Cash flows from capital and related financing activities:            |             |             |
| Purchase of capital assets   | (28,320)    | (14,279)    |
| Capital contributions by grantors                                    | 3,082       | 989         |
| Payments of capital lease obligation                                 | (118)       | (112)       |
| Payments of long-term debt   | (89)        | (83)        |
| Interest paid  | (15,405)    | (16,252)    |
| Net cash used in capital and related financing activities            | (40,850)    | (29,737)    |
| Cash flows from investing activities:                                |             |             |
| Purchases of investments   | (785)       | —           |
| Sales of investments   | 15,808      | 20,756      |
| Interest received  | 1,091       | 463         |
| Net cash provided by investing activities                            | 16,114      | 21,219      |
| Net decrease in cash   | (15,411)    | (21,112)    |
| Cash at beginning of year  | 79,400      | 100,512     |
| Cash at end of year  | \$ 63,989   | 79,400      |
| Supplemental disclosures:  |             |             |
| Appropriation paid on behalf of the Hospital                         | \$ 97,947   | 96,002      |
| Other postemployment benefits paid on behalf of the Hospital         | 36,409      | —           |
| Capital assets included within accounts payable and accrued expenses | 3,185       | —           |
| Re-evaluation of capital lease obligation                            | 2,674       | —           |

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

Statements of Cash Flows

Years ended June 30, 2018 and 2017

(In thousands)

|   | <b>2018</b>  | <b>2017</b> |
|---|--------------|-------------|
| Reconciliation of operating loss to net cash used in operating activities:        |              |             |
| Operating loss  | \$ (226,859) | (178,223)   |
| Adjustments to reconcile operating loss to net cash used in operating activities: |              |             |
| Amortization of prepaid bond insurance  | 587          | 587         |
| Depreciation  | 20,796       | 20,493      |
| Provision for bad debts   | 172,991      | 143,092     |
| Other postemployment benefits   | 36,409       | —           |
| Appropriations paid on behalf of the Hospital                                     | 97,947       | 96,002      |
| Changes in assets and liabilities:  |              |             |
| Patient accounts receivable, net  | (175,313)    | (148,402)   |
| Due from State of New Jersey  | (11,629)     | (1,209)     |
| Grants receivable   | (2,761)      | 1,374       |
| Supplies and other current assets   | 3,074        | (18,503)    |
| Accounts payable and accrued expenses   | (43)         | 10,046      |
| Accrued salaries and related payroll taxes  | 5,141        | (17,280)    |
| Accrued vacation and sick   | (623)        | (176)       |
| Due to Rutgers University   | 9,288        | 3,861       |
| Accrued claims liability  | (2,800)      | (1,236)     |
| Estimated third-party payor settlements, net                                      | (3,253)      | (902)       |
| Pension liability   | 42,175       | 46,945      |
| Other liabilities   | 368          | (2,904)     |
| Net cash used in operating activities   | \$ (34,505)  | (46,435)    |

See accompanying notes to financial statements.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**(1) Organization**

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

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

Newark AIDS Consortium, Inc. (d/b/a Broadway House for Continuing Care or BHCC) was incorporated in April 1992. BHCC is exempt from federal, state, and local income taxes as 501(c) (3) organizations under the Internal Revenue Code. BHCC is a blended component unit of the Hospital as a result of UH being the sole corporate member.

BHCC issues separate annual financial statement as of December 31, which are available through Jim Hub, Director of Finance, Broadway House, 298 Broadway, Newark, NJ 07104-4003.

The reporting entity, which results from blending UH and BHCC, is collectively referred to as the "Hospital."

**(2) Summary of Significant Accounting Policies**

The Hospital's significant accounting policies are as follows:

**(a) Basis of Presentation**

The accompanying basic financial statements of the Hospital are presented in conformity with Generally Accepted Accounting Principles for state and local governments in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

The financial statements have been prepared on the accrual basis of accounting using the economic resources measurement focus. Under this method of accounting, revenues are recognized when earned and expenses are recorded when liabilities are incurred without regard to receipt or disbursement of cash.

**(b) Restricted Investments**

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

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

Notes to Financial Statements

June 30, 2018 and 2017

Restricted investments are invested in money market funds and are recorded at fair value based on quoted market prices, which are Level 1 investments in the fair value hierarchy.

**(c) Charity Care**

The Hospital provides care to patients who meet certain criteria under its charity care policy at amounts less than its charges or established rates. The Hospital does not pursue collection of amounts determined to qualify as charity care, and they are not reported as revenue (note 4).

**(d) Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates. The change in estimate related to third-party payors and accrued claims liability are disclosed in notes 11(a) and 11(c), respectively.

**(e) Classifications of Revenues and Expenses**

All exchange transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are considered to be operating activities and are reported as operating revenues and operating expenses. Appropriations from the State of New Jersey, contributions and special events, and fundraising expenses, interest income, and interest expense are reported as nonoperating income and expenses. Other changes in net position, which are excluded from loss before other changes in net position, consist of capital contributions funded by grantors or donors.

**(f) Patient Accounts Receivable, Net and Net Patient Service Revenue**

The Hospital has agreements with certain third-party payors that provide for payments at amounts different from its charges or established rates. Payment arrangements include prospectively determined rates, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated third-party payor settlements resulting from audits, reviews, and investigations. These estimated third-party payor settlements are accrued in the period the related services are rendered and adjusted in future periods as revised information becomes known or as years are no longer subject to such audits, reviews, and investigations. Net patient service revenue is reported net of the provision for bad debts of \$173.0 million in 2018 and \$143.1 million in 2017.

The allowance for doubtful patient accounts is the Hospital's estimate of the amount of probable credit losses in its patient accounts receivable. The Hospital determines the allowance based on collection studies and historical write-off experience. Past-due balances are reviewed individually for collectibility. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The allowance for estimated doubtful accounts at June 30, 2018 is \$228.1 million and at June 30, 2017 is \$230.0 million.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**(g) Appropriations from the State of New Jersey**

State appropriations are recognized in the fiscal year during which the State appropriates the funds for the Hospital. The Hospital is fiscally dependent upon these appropriations. The Hospital classifies them as nonoperating income.

The Hospital records both revenues and expenses in an amount equal to expenditures made on its behalf by the State, that is, fringe benefits of the Hospital's employees, settlements of claims for medical malpractice, negligence, other torts, and alleged breach of contracts (see notes 10 and 11).

The State pays on behalf of the Hospital for fringe benefits of employees, medical malpractice settlements, negligence, and other torts. The Hospital is indemnified by the State for the Hospital's malpractice settlements (see note 11). In 2018 and 2017, the fringe benefits of employees paid by the State were \$97.2 million and \$96.0 million, the medical malpractice and general liability settlements paid by the State were \$0.7 million in 2018 and nominal costs in 2017. The State also paid the Hospital \$43.9 million in 2018 and \$33.8 million in 2017 to support the Hospital operations.

All State aid to the Hospital is subject to and dependent upon appropriations being made for such purpose by the New Jersey State Legislature (the State Legislature). The State Legislature has no legal obligation to make such appropriations.

**(h) Government Grants**

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

**(i) Prepaid Bond Insurance**

Prepaid bond insurance costs of \$17.6 million represent costs incurred in connection with the issuance of Series 2015A bonds and are amortized over the life of the bonds. Accumulated amortization of prepaid bond insurance costs amounted to \$1.5 million at June 30, 2018 and \$0.9 million at June 30, 2017.

**(j) Capital Assets and Depreciation**

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

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

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

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

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

Capital assets under capital lease obligations and leasehold improvements are depreciated over the shorter of either the lease term or the estimated useful life.

**(k) Supplies**

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

**(l) Income Taxes**

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

**(m) Due from State of New Jersey**

Due from State of New Jersey represents reimbursements due for fringe benefits paid by the Hospital for employees covered by the State of New Jersey benefit plans and receivables related to the New Jersey Department of Health subsidy program.

**(n) Grants Receivable**

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

**(o) Net Position**

Net positions of the Hospital are classified in various components. *Net investment in capital assets* consist of capital assets net of accumulated depreciation and reduced by outstanding borrowings used to finance the purchase or construction of those assets. *Unrestricted net position* is remaining net position that does not meet the definition of *Net investment in capital assets*. The Hospital first applies restricted resources when unrestricted resources are available for the same purpose.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**(p) Compensated Absences**

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

**(q) Retirement Plans**

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

**(r) Accrued Claims Liability**

Accrued claims liability represents estimated amounts payable related to workers' compensation claims (see note 11(c)).

**(s) Accounting Standard Adopted**

In fiscal year 2018, the Hospital adopted GASB Statement No. 75 (GASB 75), *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions* (OPEB). GASB 75 establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expenses related to OPEB in the basic financial statements, in addition to requiring more extensive note disclosures and required supplementary information. The adoption of GASB 75 resulted in the Hospital recognizing other postemployment benefit expense and nonoperating revenue for its proportionate share of OPEB expense that was paid by the State. See note 10 for additional information on the OPEB plan and GASB 75.

**(t) Fair Value**

Management determines fair value of financial instruments as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Management utilizes valuation techniques that maximize the use of observable inputs (Levels 1 and 2) and minimize the use of unobservable inputs (Level 3) within the fair value hierarchy established by GASB. Financial assets and liabilities carried at fair value are classified and disclosed in one of the following categories:

Level 1: Fair value measurements using unadjusted quoted market prices in active markets for identical, unrestricted assets or liabilities.



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

Notes to Financial Statements

June 30, 2018 and 2017

Level 2: Fair value measurements using observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially that full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted market prices that traded less frequently than exchange-traded instruments.

Level 3: Fair value measurements using significant inputs that are not readily observable in the market and are based on internally developed models or methodologies utilizing significant inputs that are generally less readily observable.

Money market mutual funds are valued at the NAV of the shares held at year-end, based on published market quotations on active markets. The NAV is classified within Level 1 of the fair value hierarchy as the unit price is quoted in an active market.

Corporate bonds are valued using an evaluation price that is based on a compilation of primarily observable market quotations, when available. These are included as Level 2 investments in the fair value hierarchy.

The Hospital does not have any assets or liabilities based upon Level 3 inputs.

**(u) Reclassifications**

Certain amounts have been reclassified from the prior year to conform to current year financial statement presentation.

**(3) Cash**

Custodial credit risk is the risk that, in the event of a bank failure, the Hospital's deposits may not be returned to it. At June 30, 2018 and 2017, the actual amount of cash in the Hospital's bank accounts was \$66.6 million and \$83.6 million (with \$2.6 million and \$4.2 million in outstanding checks), respectively. As of May 29, 2015, a Tri-Party collateral agreement was established between the Hospital, the Bank of America, N.A. and the Bank of New York Mellon to collateralize the Hospital's cash.

**(4) Charity Care**

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services furnished under its charity care policy and the estimated cost of those services. The amount of uncompensated care provided to indigent and the broader community for the years ended June 30 (in thousands):

|   | <b>2018</b> | <b>2017</b> |
|---|-------------|-------------|
| Charity care:                                   |             |             |
| Charges foregone, based on established rates    | \$ 248,139  | 233,374     |
| Estimated cost incurred to provide charity care | 69,479      | 61,298      |

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

Notes to Financial Statements

June 30, 2018 and 2017

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| Provision for bad debt:                      |             |             |
| Charges foregone, based on established rates | \$ 172,991  | 143,092     |
| Estimated cost incurred to provide bad debt  | 46,325      | 37,584      |

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

The Hospital recorded \$48.1 million and \$40.4 million from the State's Charity Care Subsidy Fund in 2018 and 2017, respectively, of reimbursement associated with cost of bad debt and charity care and is recorded in net patient service revenue in the statement of revenues, expenses, and changes in net position.

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

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

Included in net patient service revenue are adjustments to prior year estimated third-party payor settlements that were originally recorded in the period the related services were rendered. The adjustments to prior year estimates and other third-party reimbursement receipts or recoveries that relate to prior years resulted in an increase to net patient service revenues (see note 11(a)).

The components of net patient service revenue for the years ended June 30 are as follows (in thousands):

|  | <b>2018</b>  | <b>2017</b> |
|--|--------------|-------------|
| Gross charges                              | \$ 2,716,916 | 2,662,148   |
| Additions (deductions) from gross charges: |              |             |
| Healthcare subsidy fund revenues           | 67,108       | 57,072      |
| Contractual and other allowances           | (2,094,244)  | (2,079,583) |
| Provision for bad debts                    | (172,991)    | (143,092)   |
| Subtotal                                   | (2,200,127)  | (2,165,603) |
| Net patient service revenues               | \$ 516,789   | 496,545     |

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

Net patient service revenue by primary payor for the years ended June 30 are as follows (in thousands):

|                                      | <u>2018</u>       | <u>2017</u>    |
|--------------------------------------|-------------------|----------------|
| Medicaid and Medicaid HMO            | \$ 189,345        | 186,118        |
| Medicare                             | 125,728           | 111,571        |
| Other third-party payors             | 121,732           | 131,914        |
| Self-pay                             | <u>12,876</u>     | <u>9,869</u>   |
| Net patient service revenue by payor | 449,681           | 439,472        |
| Healthcare subsidy fund revenues     | <u>67,108</u>     | <u>57,072</u>  |
| Net patient service revenue          | <u>\$ 516,789</u> | <u>496,544</u> |

The Hospital provides services to its patients, most of who are insured under third-party payor agreements. Patient accounts receivable, net were as follows as of June 30 (in thousands):

|                           | <u>2018</u>      |                | <u>2017</u>      |                |
|---------------------------|------------------|----------------|------------------|----------------|
| Medicaid and Medicaid HMO | \$ 30,166        | 36.3 %         | \$ 29,198        | 36.1 %         |
| Medicare                  | 9,696            | 11.7           | 9,265            | 11.5           |
| Other third-party payors  | 37,156           | 44.7           | 36,340           | 45.0           |
| Self-pay                  | <u>6,082</u>     | <u>7.3</u>     | <u>5,975</u>     | <u>7.4</u>     |
|                           | <u>\$ 83,100</u> | <u>100.0 %</u> | <u>\$ 80,778</u> | <u>100.0 %</u> |

Allowance for doubtful accounts activity for the years ended was as follows (in thousands):

|                              | <u>2018</u>       | <u>2017</u>      |
|------------------------------|-------------------|------------------|
| Beginning balance            | \$ 229,976        | 226,475          |
| Provision for bad debts      | 172,991           | 143,092          |
| Write-off, net of recoveries | <u>(174,908)</u>  | <u>(139,591)</u> |
| Ending balance               | <u>\$ 228,059</u> | <u>229,976</u>   |

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**(6) Capital Assets**

Capital assets activity for the years ended June 30 was as follows (in thousands):

|                                      | <u>June 30, 2017</u><br><u>balance</u> | <u>Acquisitions,</u><br><u>net of</u><br><u>transfers</u> | <u>Sales,</u><br><u>retirements,</u><br><u>and</u><br><u>adjustments</u> | <u>June 30, 2018</u><br><u>balance</u> |
|--------------------------------------|--|---|--|--|
| Land and land improvements \$        | 1,598                                  | —   | —  | 1,598                                  |
| Buildings and leasehold improvements | 309,693                                | 608   | 6,905  | 317,206                                |
| Equipment                            | 237,516                                | 6,379   | (7,420)  | 236,475                                |
| Capital leases                       | 77,031                                 | —   | (3,180)  | 73,851                                 |
| Construction in progress             | 5,094                                  | 24,518  | —  | 29,612                                 |
|                                      | <u>\$ 630,932</u>                      | <u>31,505</u>   | <u>(3,695)</u>   | <u>658,742</u>                         |

|                               | <u>June 30, 2016</u><br><u>balance</u> | <u>Acquisitions,</u><br><u>net of</u><br><u>transfers</u> | <u>Sales,</u><br><u>retirements,</u><br><u>and</u><br><u>adjustments</u> | <u>June 30, 2017</u><br><u>balance</u> |
|-------------------------------|--|---|--|--|
| Land and land improvements \$ | 1,598                                  | —   | —  | 1,598                                  |
| Buildings                     | 310,453                                | (759)   | (690)  | 309,004                                |
| Equipment                     | 226,300                                | 11,906  | —  | 238,206                                |
| Capital leases                | 77,030                                 | —   | —  | 77,030                                 |
| Construction in progress      | 1,973                                  | 3,121   | —  | 5,094                                  |
|                               | <u>\$ 617,354</u>                      | <u>14,268</u>   | <u>(690)</u>   | <u>630,932</u>                         |

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

Notes to Financial Statements

June 30, 2018 and 2017

Related information on accumulated depreciation for the years ended June 30 was as follows (in thousands):

|                                      | <b>June 30, 2017<br/>balance</b> | <b>Acquisitions,<br/>net of<br/>transfers</b> | <b>Sales,<br/>retirements,<br/>and<br/>adjustments</b> | <b>June 30, 2018<br/>balance</b> |
|--------------------------------------|----------------------------------|---|--|----------------------------------|
| Buildings and leasehold improvements | \$ 251,018                       | 7,709   | 1,019  | 259,746                          |
| Equipment                            | 173,799                          | 11,733  | (1,534)  | 183,998                          |
| Capital leases                       | 7,640                            | 1,354   | —  | 8,994                            |
|                                      | <u>\$ 432,457</u>                | <u>20,796</u>                                 | <u>(515)</u>   | <u>452,738</u>                   |

  

|                                      | <b>June 30, 2016<br/>balance</b> | <b>Acquisitions,<br/>net of<br/>transfers</b> | <b>Sales,<br/>retirements,<br/>and<br/>adjustments</b> | <b>June 30, 2017<br/>balance</b> |
|--------------------------------------|----------------------------------|---|--|----------------------------------|
| Buildings and leasehold improvements | \$ 244,057                       | 6,961   | —  | 251,018                          |
| Equipment                            | 162,877                          | 11,623  | (701)  | 173,799                          |
| Capital leases                       | 5,731                            | 1,909   | —  | 7,640                            |
|                                      | <u>\$ 412,665</u>                | <u>20,493</u>                                 | <u>(701)</u>   | <u>432,457</u>                   |

As of June 30, 2018, the Hospital committed \$21.8 million to complete construction projects. Commitments include the costs to complete information technology system upgrades, building renovation projects and a sprinkler system.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**(7) Restricted Investments**

Restricted investments consist of the following as of June 30 (in thousands):

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| Under bond resolutions:                        |             |             |
| Working capital funds (a)                      | \$ 152      | 248         |
| Capital reserve funds (a)                      | 71,503      | 87,337      |
| Debt service reserve funds (a)                 | 17,340      | 17,264      |
| Debt service funds (a)                         | 6,127       | 6,042       |
|  | 95,122      | 110,891     |
| Other investments (b)                          | 747         | —           |
| Less current portion of restricted investments | (6,114)     | (6,042)     |
|  | \$ 89,755   | 104,849     |

- (a) Restricted investments under the terms of the bond resolutions (see note 8) are to provide for debt service requirements and the acquisition of capital assets. Terms of the bond resolutions provide that assets be maintained in separate funds held by the trustee, TD Bank, National Association. The restricted investments are held in money market funds and are classified as Level 1 in the fair value table.
- (b) Other investments are held by BHCC within a portfolio with TD Bank, National Association and are reported at fair value. The portfolio consists of corporate bonds and money market mutual funds. The investments are classified as both current and noncurrent based upon years to maturity for corporate bonds. Money market funds are classified as current. Corporate bonds of \$0.7 million are classified as Level 2 in the fair value hierarchy and money market funds are classified as Level 1 in the fair value hierarchy.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**(8) Long-Term Debt and Capital Lease Obligations**

Long-term debt consists of the following as of June 30 (in thousands):

|  | <b>2018</b> | <b>2017</b> |
|--|-------------|-------------|
| Bonds payable:   |             |             |
| New Jersey Health Care Facilities Financing Authority (NJHCFFA) Series 2015A Bond, bearing interest at fixed rates to be paid semi-annually; with principal payments to be paid annually and set to commence on July 1, 2021 (a) | \$ 254,975  | 254,975     |
| NJHCFFA Series 2015A net premium and amortized over the 30 year life of the bond (a)   | 13,900      | 14,671      |
| New Jersey Educational Facilities Authority (NJEFA) Higher Education Capital Improvement Fund, Series 2000 A annual principal payments (b)   | 337         | 426         |
| Capital lease obligations (c)  | 73,851      | 76,615      |
|  | 343,063     | 346,687     |
| Less current installments  | 354         | 207         |
|  | \$ 342,709  | 346,480     |

Long-term debt activity for the years ended June 30 was as follows (in thousands):

|                           | <b>June 30, 2017<br/>balance</b> | <b>Additions</b> | <b>Reductions</b> | <b>June 30, 2018<br/>balance</b> | <b>Amounts<br/>due within<br/>1 year</b> |
|---------------------------|----------------------------------|------------------|-------------------|----------------------------------|--|
| Long-term debt:           |                                  |                  |                   |                                  |  |
| Bonds payable 2015A       | \$ 269,646                       | —                | (771)             | 268,875                          | —  |
| Bonds payable NJEFA       | 426                              | —                | (89)              | 337                              | 92                                       |
| Capital lease obligations | 76,615                           | —                | (2,764)           | 73,851                           | 262                                      |
| Net long term debt        | \$ 346,687                       | —                | (3,624)           | 343,063                          | 354                                      |

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

Notes to Financial Statements

June 30, 2018 and 2017

|                           | <u>June 30, 2016</u><br><u>balance</u> | <u>Additions</u> | <u>Reductions</u> | <u>June 30, 2017</u><br><u>balance</u> | <u>Amounts</u><br><u>due within</u><br><u>1 year</u> |
|---------------------------|--|------------------|-------------------|--|--|
| Long-term debt:           |  |                  |                   |  |  |
| Bonds payable 2015A       | \$ 270,416                             | —                | (770)             | 269,646                                | —  |
| Bonds payable NJEFA       | 509                                    | —                | (83)              | 426                                    | 89   |
| Capital lease obligations | 76,727                                 | —                | (112)             | 76,615                                 | 118  |
| Net long term debt        | <u>\$ 347,652</u>                      | <u>—</u>         | <u>(965)</u>      | <u>346,687</u>                         | <u>207</u>   |

- (a) On December 22, 2015, the Hospital issued \$255 million of New Jersey Healthcare Facilities Financing Authority Series (NJHCFFA or the Authority) 2015A Bonds (2015A Bonds). Total proceeds from the sale were \$295.8 million and included a net premium of \$15.8 million, as well as \$25.0 million from trustee-held debt service and reserve funds. Proceeds from the sale were used for the purpose of: (i) the defeasance of \$150 million of NJHCFFA Bond Anticipation Notes debt (ii) funding current debt service reserve requirements of \$17.3 million; (iii) funding capital projects of \$102.8 million, including information services and technology capital, heating, ventilation, and air conditioning improvements, operating room renovations, Cancer Center expansion, and routine and emergency capital needs; (iv) funding bond insurance costs of \$17.6 million; (v) and paying bond issuance costs of \$2.7 million. The Series 2015A Notes were placed by and between the Authority and TD Bank, National Association, as Trustee. The Hospital entered into a Loan Agreement (the Loan Agreement) with the Authority relating to the Series 2015A bond. A security feature for this obligation is provided by a lock box arrangement with the Trustee, TD Bank, N.A. Debt service requirements will be funded by unrestricted state appropriations, including state charity pools, Delivery System Reform Incentive Payments, Graduate Medical Education (GME) and individual state supplemental appropriations that will flow through the lock box. Any excess funds will then be released to the Hospital for operations. Under the Loan Agreement, the Hospital is required to maintain certain covenants.

Principal payments on the bonds will be due annually and are not set to commence until July 1, 2021. Interest will be paid semiannually on July 1 and January 1, with the first payment due July 1, 2016. The bonds are set at fixed interest rates and are as follows: (i) \$65.3 million in serial bonds at 5.000%; (ii) \$78.2 million in term bonds at 4.125% and (iii) \$111.5 million in term bonds at 5.000%.

- (b) In addition on July 1, 2013, the Hospital assumed a portion of the UMDNJ obligation of the New Jersey Educational Facilities Authority's Higher Education Capital Improvement fund, Series 2000A (as revised) in the amount of \$0.7 million. The debt bears interest at a fixed rate of 5.0% and requires principal payments until August 2020.
- (c) On July 1, 2013, the Hospital entered into five capital lease agreements with Rutgers, the State University of New Jersey for space in various locations on its Newark campus. The agreements are for 76 years and require monthly rent payments in advance. The Hospital has capitalized the present value of the lease payments using a discount factor of 5.1%, based on Hospital's incremental borrowing rate, and will amortize the asset over the estimated useful life of each of the buildings. During 2018, there were amendments to the lease terms which resulted in a re-evaluation of the lease liability resulting in a reduction of the lease liability by \$2.6 million.



**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

The following table summarizes debt service requirements for 2015A Bonds and NJEFA as of June 30 (in thousands):

| Year      | Principal         | Interest       | Total          |
|-----------|-------------------|----------------|----------------|
| 2019      | \$ 92             | 12,070         | 12,162         |
| 2020      | 95                | 12,068         | 12,163         |
| 2021      | 5,289             | 12,066         | 17,355         |
| 2022      | 5,495             | 11,805         | 17,300         |
| 2023      | 5,720             | 11,533         | 17,253         |
| 2024–2028 | 33,180            | 53,077         | 86,257         |
| 2029–2033 | 42,130            | 44,137         | 86,267         |
| 2034–2038 | 51,805            | 34,460         | 86,265         |
| 2039–2043 | 64,520            | 21,740         | 86,260         |
| 2044–2046 | 46,986            | 4,774          | 51,760         |
|           | <u>\$ 255,312</u> | <u>217,730</u> | <u>473,042</u> |

The following table summarizes future minimum lease payments under capitalized leases as of June 30 (in thousands):

|                                   |    |                  |
|-----------------------------------|----|------------------|
| Year:                             |    |                  |
| 2019                              | \$ | 3,853            |
| 2020                              |    | 3,853            |
| 2021                              |    | 3,853            |
| 2022                              |    | 3,853            |
| 2023                              |    | 3,853            |
| 2024–2028                         |    | 19,264           |
| 2029–2033                         |    | 19,264           |
| 2034–2038                         |    | 19,264           |
| 2039–2043                         |    | 19,264           |
| 2044–2048                         |    | 19,264           |
| 2049–2054                         |    | 19,264           |
| Thereafter                        |    | <u>132,472</u>   |
| Total                             |    | 267,321          |
| Less amount representing interest |    | <u>(193,470)</u> |
| Net                               | \$ | <u>73,851</u>    |

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

Notes to Financial Statements

June 30, 2018 and 2017

**(9) Due to Rutgers University**

Amounts due to Rutgers University (Rutgers) consist of the following at June 30:

|                                     | <b>2017</b>        |                    |                |                 | <b>2018</b>        |
|-------------------------------------|--------------------|--------------------|----------------|-----------------|--------------------|
|                                     | <b>Balance due</b> | <b>Adjustments</b> | <b>Charges</b> | <b>Hospital</b> | <b>Balance due</b> |
|                                     | <b>to Rutgers</b>  |                    |                | <b>payments</b> | <b>to Rutgers</b>  |
| Information technology services (a) | \$ 487             | 256                | 1,484          | (1,608)         | 619                |
| Contracted physicians (b)           | 5,037              | 231                | 59,698         | (54,458)        | 10,508             |
| Contracted residents (c)            | 7,395              | 106                | 20,299         | (18,136)        | 9,664              |
| Facilities service agreements (d)   | 7,631              | (343)              | 13,259         | (10,883)        | 9,664              |
| Other services (e)                  | 4,159              | (250)              | 11,532         | (11,899)        | 3,542              |
|                                     | <u>\$ 24,709</u>   | <u>—</u>           | <u>106,272</u> | <u>(96,984)</u> | <u>33,997</u>      |

|                                     | <b>2016</b>        |                |                 |                    | <b>2017</b> |
|-------------------------------------|--------------------|----------------|-----------------|--------------------|-------------|
|                                     | <b>Balance due</b> | <b>Charges</b> | <b>Hospital</b> | <b>Balance due</b> |             |
|                                     | <b>to Rutgers</b>  |                | <b>payments</b> | <b>to Rutgers</b>  |             |
| Information technology services (a) | \$ 237             | 1,760          | (1,510)         | 487                |             |
| Contracted physicians (b)           | 12,443             | 56,396         | (63,802)        | 5,037              |             |
| Contracted residents (c)            | 4,216              | 19,247         | (16,068)        | 7,395              |             |
| Facilities service agreements (d)   | 2,536              | 13,168         | (8,073)         | 7,631              |             |
| Other services (e)                  | 1,416              | 7,925          | (5,182)         | 4,159              |             |
|                                     | <u>\$ 20,848</u>   | <u>98,496</u>  | <u>(94,635)</u> | <u>24,709</u>      |             |

The Hospital and Rutgers executed a Master Affiliation Agreement on July 1, 2013 (the effective date) in support of and connection with the New Jersey Medical and Health Sciences Education Restructuring Act, N.J.S.A. 18A:64M-1 (the Act). The Agreement acknowledged that the parties were entering into multiple agreements simultaneously all of which arose out of the Act. The Master Agreement is for a term of three years with provisions for successive three-year renewals. The agreements provide for services delivered by and between the parties and outline the compensation to be remunerated. Among these agreements are the following:

- (a) Information technology services are in support of the Hospital's clinical and business systems. The agreement includes licensing of some software, as well as system support.
- (b) The parties executed a clinical services agreement wherein Rutgers physicians were contracted to provide clinical and administrative services to the Hospital. The agreement is for three years and will expire in July 2019. The agreement calls for the parties to annually have a fair market value analysis prepared by an independent organization.

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

Notes to Financial Statements

June 30, 2018 and 2017

- (c) A Graduate Medical Education affiliation agreement was executed to govern the medical and dental activities of residents and non-Rutgers residents rendering medical and dental services at the Hospital and the compensation of such residents.
- (d) A continuing services agreement was executed that provided for a number of campus infrastructure needs, including energy and utilities, police and security, landscaping and grounds maintenance, as well as parking and snow removal. Rates are determined by an annual review by both parties for utilities and maintenance. Police and security are based upon usage with predetermined hourly rates.
- (e) A transition services agreement that provided for the temporary provision of "Other Services," between the parties. Among these services are included hazardous waste storage, medical license and radiation safety, engineering controls, financial administrative technical support, as well as a support in helping the Hospital achieve independence in these functions. The arrangements were for a period of 3 to 24 months and various extensions have been made on these arrangements. Amounts payable are for the most part based upon fixed predetermined rates.

**(10) Employee Benefits**

*Retirement Plans*

The Hospital has primarily two retirement plans available to its employees, the State of New Jersey Public Employees Retirement System, a defined-benefit plan, and the Alternate Benefit Program, a defined-contribution plan. Under these plans, participants make annual contributions, and the State of New Jersey (the State), in accordance with State statutes, makes employer contributions on behalf of the Hospital for these plans. Pension expense paid directly by the State of New Jersey for 2018 and 2017 aggregated \$20.3 million and \$16.6 million, respectively. The Hospital is charged for contributions on behalf of employees through a fringe benefits charge assessed by the State, which is included within fringe benefits expense in the accompanying statements of revenues, expenses, and changes in net position. Summary information regarding these plans is provided below.

*Public Employees Retirement System (PERS)*

**Plan Description** – PERS is a multiple-employer, public cost-sharing retirement system that is administered by the State of New Jersey under the provisions of N.J.S.A. 43:15A. The payroll for employees covered by PERS for the years ended June 30, 2018 and 2017 was \$120.8 million and \$114.5 million, respectively.

The vesting and benefit provisions are set by N.J.S.A. 43:15A. PERS provides retirement, death, and disability benefits. All benefits vest after ten years of service, except for medical benefits, which vest after 25 years of service or under the disability provisions of PERS.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

The following represents the membership tiers for PERS:

| Tier | Definition   |
|------|--|
| 1    | Members who were enrolled prior to July 1, 2007  |
| 2    | Members who were eligible to enroll on or after July 1, 2007 and prior to November 2, 2008 |
| 3    | Members who were eligible to enroll on or after November 2, 2008 and prior to May 22, 2010 |
| 4    | Members who were eligible to enroll on or after May 22, 2010 and prior to June 28, 2011    |
| 5    | Members who were eligible to enroll on or after June 28, 2011                              |

**Contributions** – Covered Hospital employees were required by PERS to contribute 7.34% and 7.20% of their annual compensation during fiscal years 2018 and 2017, respectively. The PERS contribution rate will increase by 0.14% each year until the 7.5% contribution rate is reached by July 1, 2018. The State’s pension contribution is based on statutory determined amount that includes the employer portion of the normal cost and an amortization of the unfunded accrued liability. The state made contributions in 2018 and 2017. The contribution requirements of the plan members and the Hospital are established and may be amended by the State.

Employees can also make voluntary contributions to two optional State of New Jersey tax-deferred investment plans, the Supplemental Annuity Collective Trust (SACT) and the Additional Contributions Tax Sheltered (ACTS) programs. Both plans are subject to limits within the Internal Revenue Code.

The State issues publicly available financial reports that include financial statements and required supplementary information for PERS. These reports may be obtained by writing to the State of New Jersey, Division of Pensions and Benefits, PO Box 295, Trenton, NJ 08625-0295.

Effective July 1, 2014, the Hospital adopted GASB 68 and GASB 71, resulting in the Hospital recording their net pension liability, deferred inflows and outflows of resources, and pension expense associated with the PERS plan. The PERS’ net pension liability, deferred inflows and outflows of resources, and pension expense is calculated by an external actuary.

At June 30, 2018, the Hospital reported a liability of \$541.6 million, for its proportionate share of the PERS net pension liability. The total pension liability is based on measurement date as of June 30, 2017. The Hospital’s proportion for the net pension liability was based on the Hospital’s share of the actual contributions paid by the State to PERS relative to the total contributions of all participating state group employers for 2017, which was 2.112%.

At June 30, 2017, the Hospital reported a liability of \$552.1 million, for its proportionate share of the PERS net pension liability. The total pension liability is based on measurement date as of June 30, 2016. The Hospital’s proportion for the net pension liability was based on the Hospital’s share of the actual

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

Notes to Financial Statements

June 30, 2018 and 2017

contributions paid by the State to PERS relative to the total contributions of all participating state group employers for 2016, which was 1.878%.

**(a) Actuarial Assumptions**

The total pension liability for the June 30, 2017 measurement date was determined by an actuarial valuation as of July 1, 2016, which was rolled forward to June 30, 2017, and was determined using the following actuarial assumptions:

|                           |                         |
|---------------------------|-------------------------|
| Inflation rate            | 2.25 %                  |
| Salary increases:         |                         |
| Through 2026              | 1.65–4.15% based on age |
| Thereafter                | 2.65–5.15% based on age |
| Investment rate of return | 7.00 %                  |
| Discount rate             | 5.00                    |

The total pension liability for the June 30, 2016 measurement date was determined by an actuarial valuation as of July 1, 2015, which was rolled forward to June 30, 2016, and was determined using the following actuarial assumptions:

|                           |                         |
|---------------------------|-------------------------|
| Inflation rate            | 3.08 %                  |
| Salary increases:         |                         |
| Through 2026              | 1.65–4.15% based on age |
| Thereafter                | 2.65–5.15% based on age |
| Investment rate of return | 7.65 %                  |
| Discount rate             | 3.98                    |

**(i) Mortality Tables**

Preretirement mortality rates for PERS were based on the RP-2000 Employee Preretirement Mortality Tables for male and female active participants. For State employees, mortality tables are set back four years for male and females. In addition, the table provides future improvements in mortality from the base year of 2013 using a generational approach based on the plan actuary's modified MP-2014 projection scale. Postretirement mortality rates were based on the RP-2000 Combined Healthy Male and Female Mortality Tables (setback one year for males and females) for service retirements and beneficiaries of former members and a one-year static projection based on mortality improvement Scale AA. In addition, the table provides future improvements in mortality from the base year of 2013 using a generational approach based on the plan actuary's modified MP-2014 projection scale. Disability retirement rates used to value disabled retirees were based on the RP-2000 Disabled Mortality Table (setback three years for males and setforward one year for females).

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

Notes to Financial Statements

June 30, 2018 and 2017

**(b) Expected Rate of Return on Investments**

In accordance with State statute, the long-term expected rate of return on plan investments is determined by the State Treasurer, after consultation with the Directors of the Division of Investments and Division of Pensions and Benefits, the board of trustees and the actuaries. The long-term expected rate of return was determined using a building block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return for each major asset class included in PERS's target asset allocation as of June 30, 2017 and 2016 are summarized in the following table:

| <u>Asset class</u>                  | <u>2017<br/>Target<br/>allocation</u> | <u>2017<br/>Long-term<br/>expected real<br/>rate of return</u> | <u>2016<br/>Target<br/>allocation</u> | <u>2016<br/>Long-term<br/>expected real<br/>rate of return</u> |
|-------------------------------------|---------------------------------------|--|---------------------------------------|--|
| Cash                                | 5.50 %                                | 1.00 %   | 5.00 %                                | 0.87 %   |
| U.S. Treasuries                     | 3.00                                  | 1.87   | 1.50                                  | 1.74   |
| Investment grade credit             | 10.00                                 | 3.78   | 8.00                                  | 1.79   |
| Mortgages                           | —                                     | —  | 2.00                                  | 1.67   |
| High yield bonds                    | 2.50                                  | 6.82   | 2.00                                  | 4.56   |
| Global diversified credit           | 5.00                                  | 7.10   | —                                     | —  |
| Credit oriented hedge funds         | 1.00                                  | 6.60   | —                                     | —  |
| Debt related private equity         | 2.00                                  | 10.63  | —                                     | —  |
| Debt related real estate            | 1.00                                  | 6.61   | —                                     | —  |
| Private real estate                 | 2.50                                  | 11.83  | —                                     | —  |
| Equity related real estate          | 6.25                                  | 9.23   | —                                     | —  |
| Inflation-indexed bonds             | —                                     | —  | 1.50                                  | 3.44   |
| Broad U.S. equities                 | 30.00                                 | 8.19   | 26.00                                 | 8.53   |
| Non U.S. developed foreign equities | 11.50                                 | 9.00   | 13.25                                 | 6.83   |
| Emerging market equities            | 6.50                                  | 11.64  | 6.50                                  | 9.95   |
| Private equity                      | —                                     | —  | 9.00                                  | 12.40  |
| Hedge funds/absolute return         | 5.00                                  | 5.51   | 12.50                                 | 4.68   |
| Real estate (property)              | —                                     | —  | 2.00                                  | 6.91   |
| Commodities                         | —                                     | —  | 0.50                                  | 5.45   |
| Global debt ex U.S.                 | —                                     | —  | 5.00                                  | (0.25)   |
| REIT                                | —                                     | —  | 5.25                                  | 5.63   |
| Buyout venture capital              | 8.25                                  | 13.80  | —                                     | —  |

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

Notes to Financial Statements

June 30, 2018 and 2017

**(c) Discount Rate**

The discount rate used to measure the total pension liability was 5.00% and 3.98% as of June 30, 2017 and 2016, respectively. This single blended discount rate was based on the long-term expected rate of return on pension plan investments of 7.00% and 7.65%, and a municipal bond rate of 3.58% and 2.85% as of June 30, 2017 and 2016, respectively, based on the Bond Buyer Go 20-Bond Municipal Bond Index, which includes tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher. For the June 30, 2017 measurement date, the projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current member contribution rates and that contributions from employers will be made based on the contributions rate in the most recent fiscal year. The State employer contributed 40% of the actuarially determined contributions and the local employers contributed 100% of their actuarially determined contributions. Based on those assumptions, the plan's fiduciary net position was projected to be available to make projected future benefit payments of current plan members through 2040. Therefore, the long-term expected rate of return on plan investments was applied to projected benefit payments through 2040, and the municipal bond rate was applied to projected benefit payments after that date in determining the total pension liability.

For the June 30, 2016 measurement date, the projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current member contribution rates and that contributions from employers will be made based on the contributions rate in the most recent fiscal year. The State employer contributed 30% of the actuarially determined contributions and the local employers contributed 100% of their actuarially determined contributions. Based on those assumptions, the plan's fiduciary net position was projected to be available to make projected future benefit payments of current plan members through 2034. Therefore, the long-term expected rate of return on plan investments was applied to projected benefit payments through 2034, and the municipal bond rate was applied to projected benefit payments after that date in determining the total pension liability.

The following presents the Hospital's proportionate share of the net pension liabilities, measured as of June 30, 2017 and 2016, calculated using the discount rate as disclosed above, as well as what the Hospital's proportionate share of the net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower or one-percentage-point higher than the current rate (in millions):

|   | <b>2017</b>                    |                                  |                                |
|---|--------------------------------|----------------------------------|--------------------------------|
|   | <b>1% Decrease<br/>(4.00%)</b> | <b>Discount rate<br/>(5.00%)</b> | <b>1% Increase<br/>(6.00%)</b> |
| Hospital's proportionate share of the net pension liability | \$ 629.8                       | 541.6                            | 468.4                          |

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

|   | 2016                   |                          |                        |
|---|------------------------|--------------------------|------------------------|
|   | 1% Decrease<br>(2.98%) | Discount rate<br>(3.98%) | 1% Increase<br>(4.98%) |
| Hospital's proportionate share of the net pension liability | \$ 646.5               | 552.1                    | 474.1                  |

**(d) Collective Deferred Outflows of Resources and Deferred Inflows of Resources**

**Deferred Outflows of Resources from Pensions (in thousands)**

|   | 2018       | 2017    |
|---|------------|---------|
| Differences between expected and actual experience  | \$ 12,407  | 11,750  |
| Changes of assumptions  | 70,841     | 82,522  |
| Changes in proportion   | 3,440      | 9,121   |
| Net difference between projected and actual investment earnings on pension plan investments | 74,892     | 38,678  |
| Total   | \$ 161,580 | 142,071 |

**Deferred Inflows of Resources from Pensions (in thousands)**

|   | 2018      | 2017 |
|---|-----------|------|
| Differences between expected and actual experience  | \$ —      | —    |
| Changes of assumptions  | —         | —    |
| Changes in proportion   | —         | —    |
| Net difference between projected and actual investment earnings on pension plan investments | 76,673    | —    |
| Total   | \$ 76,673 | —    |



**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

The deferred inflows and outflows of resources at June 30, 2018 will be recognized as pension expense as follows (in thousands):

|                      | <b>Amount</b> |
|----------------------|---------------|
| Years ended June 30: |               |
| 2019                 | \$ 28,065     |
| 2020                 | 31,290        |
| 2021                 | 24,361        |
| 2022                 | 4,272         |
| 2023                 | (3,081)       |
|                      | \$ 84,907     |

Contributions made after the measurement date of the net pension liability have been reported as deferred outflows of resources at June 30, 2018 and 2017 in the amount of approximately \$13,638,000 and \$9,174,000, respectively. Contributions are estimated by the State based on information available at the time.

**(e) Annual Pension Expense**

The Hospital's annual pension expense for fiscal year ended June 30, 2018 was approximately \$55.8 million and for the fiscal year ended June 30, 2017 was approximately \$56.1 million.

*(i) Alternate Benefit Program (ABP)*

**Plan Description** – ABP is an employer, defined-contribution State retirement plan established as an alternative to PERS. The payroll for employees covered by ABP for the years ended June 30, 2018 and 2017 was \$86.4 million and \$92.3 million, respectively.

Professional and administrative staff, and certain other salaried employees hired prior to July 1, 2013 are eligible to participate in ABP. Employer (State) contributions vest on reaching one year of credited service. The program also provides long-term disability and life insurance benefits. Benefits are payable upon termination at the member's option unless the participant is reemployed in another institution that participates in ABP.

**Contributions** – The employee mandatory contribution rate for ABP is 5% of base salary and is matched by the State at 8% of base salary. Contributions can be invested with up to seven investment carriers available under the plan for fiscal year 2018. Additional voluntary contributions may be made on a tax-deferred basis, subject to limits within the Internal Revenue Code. Employer contributions for the years ended June 30, 2018 and 2017 were \$6.7 million and \$7.4 million, respectively. Employee contributions for the years ended June 30, 2018 and 2017 were \$4.3 million and \$4.8 million, respectively.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

(ii) *Deferred Compensation Plan*

Hospital employees with membership in PERS or ABP are eligible to participate in the State of New Jersey's Employees Deferred Compensation Plan created in accordance with Internal Revenue Code Section 457. The plan permits employees to elect pretax and/or after-tax Roth contributions to invest a portion of their base salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. The plan is administered by Prudential Financial. The plan does not include any matching employer (State) contributions. All amounts of compensation deferred under the plan, all property and rights purchased with those amounts and all income attributable to those amounts, property or rights, are held in trust by the State for the exclusive benefit of the participating employees and their beneficiaries.

(iii) *Postemployment Benefits Other Than Pensions*

The Hospital's retirees participate in the State Health Benefit State Retired Employees Plan (the Plan).

**Plan description, including benefits provided** – The Plan is a single-employer defined-benefit other postemployment benefit plan, which provides medical, prescription drug, and Medicare Part B reimbursements to retirees and their covered dependents. Although the Plan is a single-employer plan, it is treated as a cost-sharing multiple employer plan for standalone reporting purposes. In accordance N.J.S.A. 52:14-17.32, the State is required to pay the premiums and periodic charges for OPEB of State employees who retire with 25 years or more of credited service, or on a disability pension, from one or more of the following pension plans: PERS, ABP or the Police and Firemen's Retirement System (PFRS). In addition, Chapter 302, P.L. 1996 provides that for purposes of this Plan, the Hospital's employees retain any and all rights to the health benefits in the Plan, even though the Hospital is considered autonomous from the State, therefore, its employees are classified as State employees. As such, the State is legally obligated for the benefit payments on behalf of the retirees of the Hospital; therefore, the Plan meets the definition of a special funding situation as defined in GASB 75.

Retirees who are not eligible for employer-paid health coverage at retirement can continue in the program by paying the cost of the insurance for themselves and their covered dependents. Pursuant to Chapter 78, P.L. 2011, future retirees eligible for postretirement medical coverage, who have less than 20 years of creditable service on June 28, 2011, will be required to pay a percentage of the cost of their healthcare coverage in retirement provided they retire with 25 years or more of pension service credit. The percentage of the premium for which the retiree will be responsible for will be determined based on the retiree's annual retirement benefit and level of coverage.

The Plan is administered on a pay-as-you-go-basis. Accordingly, no assets are accumulated in a qualifying trust that meets the definition of a trust as per GASB 75.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

**Total OPEB Liability and OPEB Expense** – As of June 30, 2018, the State recorded a liability of \$618.9 million, which represents the portion of the State’s total proportionate share of the collective total OPEB liability that is associated with the Hospital (the Hospital’s share). The Hospital’s share was based on the ratio of its members to the total members of the Plan. At June 30, 2018, the Hospital’s share was 7.5% and 2.2% of the special funding situation and of the Plan, respectively.

For the year ended June 30, 2018, the Hospital recognized OPEB expense of \$36.4 million. As the State is legally obligated for benefit payments on behalf of the Hospital, the Hospital recognized nonoperating income related to the support provided by the State of \$36.4 million.

*Actuarial assumptions and other inputs* – The State’s liability associated with the Hospital at June 30, 2018 was determined by an actuarial valuation as of June 30, 2016, which was rolled forward to the measurement date of June 30, 2017.

|                   |            |
|-------------------|------------|
| Inflation         | 2.50 %     |
| Discount rate     | 3.58       |
| Salary increases: |            |
| Through 2026      | 1.55–8.98% |
| Thereafter        | 2.00–9.98% |

The discount rate is based on the Bond Buyer GO 20-Bond Municipal Bond Index, which includes tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher. Salary increases depend on the pension plan a member is enrolled in. In addition, they are based on age or years of service.

Preretirement mortality rates were based on the RP-2014 Headcount-Weighted Healthy Employee Male/Female mortality table with fully generational mortality improvement projections from the central year using the MP-2017 scale. Postretirement mortality rates were based on the RP-2014 Headcount-Weighted Healthy Annuitant Male/Female mortality table with fully generational improvement projections from the central year using the MP-2017 scale. Disability mortality was based on the RP-2014 Headcount-Weighted Disabled Male/Female mortality table with fully generational improvement projections from the central year using the MP-2017 scale.

Certain actuarial assumptions used in the June 30, 2016 valuation were based on the results of actuarial experience studies of the State of New Jersey’s defined-benefit plans, including PERS (July 1, 2011 through June 30, 2014) ABP (using the experience of the Teacher’s Pension and Annuity Fund – July 1, 2012 through June 30, 2015), and PFRS (July 1, 2010 through June 30, 2013).

*Health Care Trend Assumptions* – For pre-Medicare preferred provider organization (PPO) and health maintenance organization (HMO) medical benefits, this amount initially is 5.9% and decreases to a 5.0% long-term trend rate after nine years. For self-insured post-65 PPO and HMO medical benefits, the trend rate is 4.5%. For prescription drug benefits, the initial trend rate is 10.5% decreasing to a

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

5.0% long-term trend rate after eight years. For the Medicare Part B reimbursement, the trend rate is 5.0%. The Medicare Advantage trend rate is 4.5% and will continue in all future years.

**(11) Commitments and Contingencies**

**(a) Reimbursement**

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

Medicare adjusts the reimbursement rates for capital, medical education, costs related to treating a disproportionate share of indigent patients, and some physician services are reimbursed on a cost basis. Due to these adjustments and other factors, final determination of the reimbursement settlement for a given year is not known until Medicare performs its annual audit. The Hospital's costs reports have been settled by the Medicare fiscal intermediary through June 30, 2015, except for years 2005, 2010, and 2013. The Hospital's Medicaid cost reports have been audited and settled with the Medicaid fiscal intermediary through June 30, 2016.

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

Revenues received under the various reimbursement systems and agreements are subject to audit and adjustment. Accordingly, provisions for estimated adjustments resulting from audit, final settlement, and changes in estimates have been recorded. Differences between the provisions and the amounts settled are recorded in the year of settlement. The Hospital recognized increases in net patient service revenues of \$3.3 million and \$1.6 million in 2018 and 2017, respectively, as a result of changes in estimated third-party settlements.

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

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

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

Notes to Financial Statements

June 30, 2018 and 2017

of health insurance, expands existing efforts to tie Medicare and Medicaid payments to performance and quality, and contains provisions intended to strengthen fraud and abuse enforcement.

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

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

**(b) Legal Matters**

There are outstanding legal claims against the Hospital for alleged negligence, medical malpractice, and other torts, and for alleged breach of contract. Pursuant to the Agreement, the Hospital is indemnified by the State for such costs, which were \$0.7 million for 2018 and there were nominal costs during 2017. The Hospital records these costs when settled by the State as appropriations from the State and as supplies and other expenses in the accompanying financial statements. Accordingly, no provision has been made in the accompanying financial statements for unsettled claims, whether asserted or not.

**(c) Accrued Claims Liability**

The Hospital is self-insured for workers' compensation benefits. At June 30, 2018 and 2017, the accrual for estimated workers' compensation claims, based on an independent actuary's estimate, includes undiscounted estimate of ultimate costs for both reported claims and claims incurred but not reported totaled approximately \$23.9 million and \$26.7 million, respectively, and is included in accrued claims liability in the accompanying statements of net position. In addition, the Hospital maintains an excess Workers' Compensation Policy with a commercial insurance company. In 2018 and 2017, no claims were presented against the policy.

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

Activity in the liability for accrued claims payable, which includes workers' compensation claims, and included in supplies and other expenses, is summarized as follows (in thousands):

|                               | <u>2018</u>      | <u>2017</u>    |
|-------------------------------|------------------|----------------|
| Balances at July 1            | \$ 26,666        | 27,902         |
| Claims incurred               | 5,500            | 6,164          |
| Claims paid                   | (5,600)          | (3,400)        |
| Change in prior year estimate | <u>(2,700)</u>   | <u>(4,000)</u> |
| Balances at June 30           | <u>\$ 23,866</u> | <u>26,666</u>  |

The change in prior year estimate is generally the result of ongoing analysis of recent loss development trends.

**(d) Operating Leases**

The Hospital leases equipment, off-site clinic space, and office space under various operating leases. Total rental expense, recorded in the supplies and other expense, for operating leases was approximately \$3.4 million and \$3.8 million in 2018 and 2017, respectively.

The following is a schedule by years of future minimum rental payments required under operating leases that have initial or remaining noncancelable lease terms in excess of one year as of June 30, 2018:

|            | <u>Total</u>    |
|------------|-----------------|
| Year:      |                 |
| 2019       | \$ 2,057        |
| 2020       | 1,408           |
| 2021       | 1,226           |
| 2022       | 406             |
| 2023       | 413             |
| Thereafter | <u>2,501</u>    |
|            | <u>\$ 8,011</u> |

**(e) Rutgers University and the State**

The Hospital entered into a master affiliation agreement, various real estate agreements, transition service agreement, continuing service agreement, various operational agreements with Rutgers University and the State. The agreements include various real estate leases, information technology services, clinical services, research affiliation, medical education, and other services (see note 9).

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

Notes to Financial Statements

June 30, 2018 and 2017

**(12) Condensed Combining Information**

The condensed combining statement of net position at June 30, 2018 is as follows (in thousands):

|   | UH<br>June 30, 2018 | BHCC<br>December 31,<br>2017 | Elimination | Total     |
|---|---------------------|------------------------------|-------------|-----------|
| <b>Assets:</b>                                      |                     |                              |             |           |
| Current assets:                                     |                     |                              |             |           |
| Cash  | \$ 62,567           | 1,422                        | —           | 63,989    |
| Restricted investments                              | 6,032               | 82                           | —           | 6,114     |
| Patient accounts receivable, net                    | 80,996              | 2,104                        | —           | 83,100    |
| Other current assets                                | 67,108              | 164                          | (90)        | 67,182    |
| Noncurrent assets:                                  |                     |                              |             |           |
| Restricted investments, net                         | 89,090              | 665                          | —           | 89,755    |
| Prepaid bond insurance                              | 16,143              | —                            | —           | 16,143    |
| Capital assets, net                                 | 204,040             | 1,964                        | —           | 206,004   |
| Total assets  | 525,976             | 6,401                        | (90)        | 532,287   |
| Deferred outflows of resources                      | 175,218             | —                            | —           | 175,218   |
| Total assets and deferred outflows of resources     | \$ 701,194          | 6,401                        | (90)        | 707,505   |
| <b>Liabilities:</b>                                 |                     |                              |             |           |
| Current liabilities                                 | \$ 106,287          | 809                          | (90)        | 107,006   |
| Long-term debt and capital leases, net              | 342,709             | —                            | —           | 342,709   |
| Pension liability                                   | 541,572             | —                            | —           | 541,572   |
| Other long-term liabilities                         | 18,657              | —                            | —           | 18,657    |
| Total liabilities                                   | 1,009,225           | 809                          | (90)        | 1,009,944 |
| Deferred inflows of resources                       | 76,673              | —                            | —           | 76,673    |
| Total liabilities and deferred inflows of resources | 1,085,898           | 809                          | (90)        | 1,086,617 |
| <b>Net position:</b>                                |                     |                              |             |           |
| Net investment in capital assets                    | 8,640               | 1,964                        | —           | 10,604    |
| Unrestricted  | (393,344)           | 3,628                        | —           | (389,716) |
| Total net position                                  | (384,704)           | 5,592                        | —           | (379,112) |
| Total liabilities and net position                  | \$ 701,194          | 6,401                        | (90)        | 707,505   |

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

Notes to Financial Statements

June 30, 2018 and 2017

The condensed combining statement of net position at June 30, 2017 is as follows (in thousands):

|  | <u>UH</u><br><u>June 30, 2017</u> | <u>December 31,</u><br><u>2016</u> | <u>Elimination</u> | <u>Total</u>     |
|--|-----------------------------------|------------------------------------|--------------------|------------------|
| <b>Assets:</b>   |                                   |                                    |                    |                  |
| Current assets:  |                                   |                                    |                    |                  |
| Cash and cash equivalents                              | \$ 76,211                         | 3,189                              | —                  | 79,400           |
| Restricted investments                                 | 6,042                             | —                                  | —                  | 6,042            |
| Patient accounts receivable, net                       | 78,814                            | 1,964                              | —                  | 80,778           |
| Other current assets                                   | 55,628                            | 260                                | (22)               | 55,866           |
| Noncurrent assets:                                     |                                   |                                    |                    |                  |
| Restricted investments, net                            | 104,849                           | —                                  | —                  | 104,849          |
| Prepaid bond insurance                                 | 16,730                            | —                                  | —                  | 16,730           |
| Capital assets, net                                    | 196,299                           | 2,176                              | —                  | 198,475          |
| Total assets   | <u>534,573</u>                    | <u>7,589</u>                       | <u>(22)</u>        | <u>542,140</u>   |
| Deferred outflows of resources                         | <u>151,245</u>                    | <u>—</u>                           | <u>—</u>           | <u>151,245</u>   |
| Total assets and deferred<br>outflows of resources     | <u>\$ 685,818</u>                 | <u>7,589</u>                       | <u>(22)</u>        | <u>693,385</u>   |
| <b>Liabilities:</b>                                    |                                   |                                    |                    |                  |
| Current liabilities                                    | \$ 91,907                         | 673                                | (22)               | 92,558           |
| Long-term debt and capital leases, net                 | 346,480                           | —                                  | —                  | 346,480          |
| Pension liability                                      | 552,097                           | —                                  | —                  | 552,097          |
| Other long-term liabilities                            | 21,695                            | —                                  | —                  | 21,695           |
| Total liabilities                                      | <u>1,012,179</u>                  | <u>673</u>                         | <u>(22)</u>        | <u>1,012,830</u> |
| Deferred inflows of resources                          | <u>—</u>                          | <u>—</u>                           | <u>—</u>           | <u>—</u>         |
| Total liabilities and deferred<br>inflows of resources | <u>1,012,179</u>                  | <u>673</u>                         | <u>(22)</u>        | <u>1,012,830</u> |
| <b>Net position:</b>                                   |                                   |                                    |                    |                  |
| Net investment in capital assets                       | 12,558                            | 2,716                              | —                  | 15,274           |
| Unrestricted   | (338,919)                         | 4,200                              | —                  | (334,719)        |
| Total net position                                     | <u>(326,361)</u>                  | <u>6,916</u>                       | <u>—</u>           | <u>(319,445)</u> |
| Total liabilities and net position \$                  | <u>\$ 685,818</u>                 | <u>7,589</u>                       | <u>(22)</u>        | <u>693,385</u>   |



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

Notes to Financial Statements

June 30, 2018 and 2017

The condensed combining statement of revenues, expenses, and changes in net position at June 30, 2018 is as follows (in thousands):

|   | UH<br>June 30, 2018 | BHCC<br>December 31,<br>2017 | Elimination | Total            |
|---|---------------------|------------------------------|-------------|------------------|
| Operating revenues:                                 |                     |                              |             |                  |
| Net patient service revenue                         | \$ 508,310          | 8,479                        | —           | 516,789          |
| Grants revenue                                      | 5,380               | 223                          | —           | 5,603            |
| Other revenue                                       | 19,875              | 1                            | —           | 19,876           |
| Total operating revenues                            | <u>533,565</u>      | <u>8,703</u>                 | <u>—</u>    | <u>542,268</u>   |
| Operating expenses:                                 |                     |                              |             |                  |
| Personnel services                                  | 257,402             | 3,379                        | —           | 260,781          |
| Contracted physician and resident fees              | 80,109              | —                            | —           | 80,109           |
| Fringe benefits                                     | 89,290              | 608                          | —           | 89,898           |
| Other postretirement benefits                       | 36,409              | —                            | —           | 36,409           |
| Pension   | 55,814              | —                            | —           | 55,814           |
| Supplies and other expenses                         | 219,602             | 5,718                        | —           | 225,320          |
| Depreciation  | 20,469              | 327                          | —           | 20,796           |
| Total operating expenses                            | <u>759,095</u>      | <u>10,032</u>                | <u>—</u>    | <u>769,127</u>   |
| Operating loss                                      | (225,530)           | (1,329)                      | —           | (226,859)        |
| Nonoperating income (expenses):                     |                     |                              |             |                  |
| Appropriations from the State of NJ                 | 141,786             | —                            | —           | 141,786          |
| Other postemployment benefits                       | 36,409              | —                            | —           | 36,409           |
| Contributions and special events                    | —                   | 108                          | —           | 108              |
| Fundraising expenses                                | —                   | (117)                        | —           | (117)            |
| Interest income                                     | 1,077               | 14                           | —           | 1,091            |
| Interest expense                                    | (15,167)            | —                            | —           | (15,167)         |
| Loss before other changes in net position           | <u>(61,425)</u>     | <u>(1,324)</u>               | <u>—</u>    | <u>(62,749)</u>  |
| Other changes in net position:                      |                     |                              |             |                  |
| Capital contributions funded by grantors and donors | 3,082               | —                            | —           | 3,082            |
| Total other changes in net position                 | <u>3,082</u>        | <u>—</u>                     | <u>—</u>    | <u>3,082</u>     |
| Decrease in net position                            | (58,343)            | (1,324)                      | —           | (59,667)         |
| Net position at beginning of year                   | <u>(326,361)</u>    | <u>6,916</u>                 | <u>—</u>    | <u>(319,445)</u> |
| Net position at end of year                         | <u>\$ (384,704)</u> | <u>5,592</u>                 | <u>—</u>    | <u>(379,112)</u> |

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

Notes to Financial Statements

June 30, 2018 and 2017

The condensed combining statement of revenues, expenses, and changes in net position at June 30, 2017 is as follows (in thousands):

|   | UH<br>June 30, 2017 | BHCC<br>December 31,<br>2016 | Elimination | Total            |
|---|---------------------|------------------------------|-------------|------------------|
| Operating revenues:                                 |                     |                              |             |                  |
| Net patient service revenue                         | \$ 487,131          | 9,413                        | —           | 496,544          |
| Grants revenue                                      | 5,016               | 319                          | —           | 5,335            |
| Other revenue                                       | 26,580              | 7                            | —           | 26,587           |
| Total operating revenues                            | <u>518,727</u>      | <u>9,739</u>                 | <u>—</u>    | <u>528,466</u>   |
| Operating expenses:                                 |                     |                              |             |                  |
| Personnel services                                  | 242,172             | 3,351                        | —           | 245,523          |
| Contracted physician and resident fees              | 75,679              | —                            | —           | 75,679           |
| Fringe benefits                                     | 91,170              | 595                          | —           | 91,765           |
| Pension   | 56,116              | —                            | —           | 56,116           |
| Supplies and other expenses                         | 211,357             | 5,756                        | —           | 217,113          |
| Depreciation  | 20,174              | 319                          | —           | 20,493           |
| Total operating expenses                            | <u>696,668</u>      | <u>10,021</u>                | <u>—</u>    | <u>706,689</u>   |
| Operating loss                                      | (177,941)           | (282)                        | —           | (178,223)        |
| Nonoperating income (expenses):                     |                     |                              |             |                  |
| Appropriations from the State of New Jersey         | 129,843             | —                            | —           | 129,843          |
| Interest income                                     | 445                 | 18                           | —           | 463              |
| Interest expense                                    | (15,190)            | —                            | —           | (15,190)         |
| Loss before other changes in net position           | <u>(62,843)</u>     | <u>(264)</u>                 | <u>—</u>    | <u>(63,107)</u>  |
| Other changes in net position:                      |                     |                              |             |                  |
| Capital contributions funded by grantors and donors | 989                 | —                            | —           | 989              |
| Total other changes in net position                 | <u>989</u>          | <u>—</u>                     | <u>—</u>    | <u>989</u>       |
| Decrease in net position                            | (61,854)            | (264)                        | —           | (62,118)         |
| Net position at beginning of year                   | <u>(264,507)</u>    | <u>7,180</u>                 | <u>—</u>    | <u>(257,327)</u> |
| Net position at end of year                         | <u>\$ (326,361)</u> | <u>6,916</u>                 | <u>—</u>    | <u>(319,445)</u> |

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

Notes to Financial Statements

June 30, 2018 and 2017

The condensed combining statement of cash flows for the year ended June 30, 2018 is as follows (in thousands):

|   | UH<br>June 30, 2018 | BHCC<br>December 31,<br>2017 | Elimination | Total     |
|---|---------------------|------------------------------|-------------|-----------|
| Cash flows from operating activities:                           |                     |                              |             |           |
| Cash received from patients and third-party payors              | \$ 495,055          | 8,363                        | —           | 503,418   |
| Receipts from grants  | 2,550               | 293                          | —           | 2,843     |
| Other receipts  | 19,874              | 1                            | —           | 19,875    |
| Cash paid for personnel services                                | (252,884)           | (3,379)                      | —           | (256,263) |
| Cash paid for contracted physician and resident fees            | (72,369)            | —                            | —           | (72,369)  |
| Cash paid for fringe benefits                                   | (12,336)            | (615)                        | —           | (12,951)  |
| Cash paid for supplies and other expenses                       | (213,483)           | (5,575)                      | —           | (219,058) |
| Net cash used in operating activities                           | (33,593)            | (912)                        | —           | (34,505)  |
| Cash flows from noncapital financing activities:                |                     |                              |             |           |
| Cash appropriations received from State of New Jersey and other | 43,839              | (9)                          | —           | 43,830    |
| Net cash provided by noncapital financing activities            | 43,839              | (9)                          | —           | 43,830    |
| Cash flows from capital and related financing activities:       |                     |                              |             |           |
| Purchase of capital assets                                      | (28,206)            | (114)                        | —           | (28,320)  |
| Capital contributions by grantors                               | 3,082               | —                            | —           | 3,082     |
| Payments of capital lease obligations                           | (118)               | —                            | —           | (118)     |
| Payments of long-term debt                                      | (89)                | —                            | —           | (89)      |
| Interest paid   | (15,405)            | —                            | —           | (15,405)  |
| Net cash used in capital and related financing activities       | (40,736)            | (114)                        | —           | (40,850)  |

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

Notes to Financial Statements

June 30, 2018 and 2017

|  | UH<br>June 30, 2018 | December 31,<br>2017 | Elimination | Total    |
|--|---------------------|----------------------|-------------|----------|
| Cash flows from investing activities:                                |                     |                      |             |          |
| Purchases of investments   | \$ —                | (785)                | —           | (785)    |
| Sales of investments   | 15,769              | 39                   | —           | 15,808   |
| Interest received  | 1,077               | 14                   | —           | 1,091    |
| Net cash provided by investing activities                            | 16,846              | (732)                | —           | 16,114   |
| Net decrease in cash   | (13,644)            | (1,767)              | —           | (15,411) |
| Cash at beginning of year  | 76,211              | 3,189                | —           | 79,400   |
| Cash at end of year  | \$ 62,567           | 1,422                | —           | 63,989   |
| Supplemental disclosure:   |                     |                      |             |          |
| Appropriation paid on behalf of the Hospital                         | \$ 97,947           | —                    | —           | 97,947   |
| Other postemployment benefits paid on behalf of the Hospital         | 36,407              | —                    | —           | 36,407   |
| Capital assets included within accounts payable and accrued expenses | 3,185               | —                    | —           | 3,185    |
| Re-evaluation of capital lease obligation                            | 2,647               | —                    | —           | 2,647    |

The condensed combining statement of cash flows for the year ended June 30, 2017 is as follows (in thousands):

|   | UH<br>June 30, 2017 | BHCC<br>December 31,<br>2016 | Elimination | Total     |
|---|---------------------|------------------------------|-------------|-----------|
| Cash flows from operating activities:                 |                     |                              |             |           |
| Cash received from patients and third-party payors    | \$ 480,285          | 10,047                       | —           | 490,332   |
| Receipts from grants                                  | 6,390               | 319                          | —           | 6,709     |
| Other receipts  | 26,580              | 7                            | —           | 26,587    |
| Cash paid for personnel services                      | (259,654)           | (3,325)                      | —           | (262,979) |
| Cash paid for contracted physician and resident fees  | (79,570)            | (2,876)                      | —           | (82,446)  |
| Cash paid for fringe benefits                         | (6,582)             | (798)                        | —           | (7,380)   |
| Cash paid for supplies and other expense              | (214,626)           | (2,632)                      | —           | (217,258) |
| Net cash (used in) provided by operating activities   | (47,177)            | 742                          | —           | (46,435)  |
| Cash flows from noncapital financing activity:        |                     |                              |             |           |
| Cash appropriations received from State of New Jersey | 33,841              | —                            | —           | 33,841    |
| Net cash provided by noncapital financing activity    | 33,841              | —                            | —           | 33,841    |

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

|   | UH<br>June 30, 2017 | BHCC<br>December 31,<br>2016 | Elimination | Total           |
|---|---------------------|------------------------------|-------------|-----------------|
| Cash flows from capital and related financing activities: |                     |                              |             |                 |
| Purchase of capital assets                                | \$ (14,117)         | (162)                        | —           | (14,279)        |
| Capital contributions by grantors                         | 989                 | —                            | —           | 989             |
| Payments of capital lease obligation                      | (112)               | —                            | —           | (112)           |
| Payments of long-term debt                                | (83)                | —                            | —           | (83)            |
| Interest paid   | (16,252)            | —                            | —           | (16,252)        |
| Net cash used in capital and related financing activities | <u>(29,575)</u>     | <u>(162)</u>                 | <u>—</u>    | <u>(29,737)</u> |
| Cash flows from investing activities:                     |                     |                              |             |                 |
| Sales of investments                                      | 20,756              | —                            | —           | 20,756          |
| Interest received   | 446                 | 17                           | —           | 463             |
| Net cash provided by investing activities                 | <u>21,202</u>       | <u>17</u>                    | <u>—</u>    | <u>21,219</u>   |
| Net (decrease) increase in cash                           | (21,709)            | 597                          | —           | (21,112)        |
| Cash at beginning of year                                 | <u>97,920</u>       | <u>2,592</u>                 | <u>—</u>    | <u>100,512</u>  |
| Cash at end of year                                       | <u>\$ 76,211</u>    | <u>3,189</u>                 | <u>—</u>    | <u>79,400</u>   |
| Supplemental disclosures:                                 |                     |                              |             |                 |
| Appropriation paid on behalf of the Hospital              | \$ 96,002           | —                            | —           | 96,002          |

**UNIVERSITY HOSPITAL**  
(A Component Unit of the State of New Jersey)  
Notes to Financial Statements  
June 30, 2018 and 2017

The condensed combining statement of cash flows for the year ended June 30, 2018 and 2017 is as follows (in thousands):

|  | <b>UH</b><br><b>June 30, 2018</b> | <b>BHCC</b><br><b>December 31,</b><br><b>2017</b> | <b>Elimination</b> | <b>Total</b>     |
|--|-----------------------------------|---|--------------------|------------------|
| Reconciliation of operating loss to net cash used in operating activities:           |                                   |   |                    |                  |
| Operating loss   | \$ (225,530)                      | (1,329)   | —                  | (226,859)        |
| Adjustments to reconcile operating loss to net cash provided by operating activities | 327,152                           | 1,578   | —                  | 328,730          |
| Net change in assets and liabilities   | <u>(135,215)</u>                  | <u>(1,161)</u>                                    | <u>—</u>           | <u>(136,376)</u> |
| Net cash used in operating activities  | <u>\$ (33,593)</u>                | <u>(912)</u>                                      | <u>—</u>           | <u>(34,505)</u>  |
|  |                                   |   |                    |                  |
|  | <b>UH</b><br><b>June 30, 2017</b> | <b>BHCC</b><br><b>December 31,</b><br><b>2016</b> | <b>Elimination</b> | <b>Total</b>     |
| Reconciliation of operating loss to net cash used in operating activities:           |                                   |   |                    |                  |
| Operating loss   | \$ (177,942)                      | (281)   | —                  | (178,223)        |
| Adjustments to reconcile operating loss to net cash provided by operating activities | 258,997                           | 1,177   | —                  | 260,174          |
| Net change in assets and liabilities   | <u>(128,232)</u>                  | <u>(154)</u>                                      | <u>—</u>           | <u>(128,386)</u> |
| Net cash (used in) provided by operating activities                                  | <u>\$ (47,177)</u>                | <u>742</u>  | <u>—</u>           | <u>(46,435)</u>  |

**(13) Subsequent Event**

Management evaluated all events and transactions that occurred after June 30, 2018 and through March 29, 2019. The Hospital did not have any material recognizable subsequent events during the period.

**UNIVERSITY HOSPITAL**  
Required Supplementary Information  
Schedules of the Hospital's Contributions  
(Unaudited)  
June 30, 2018  
(Dollar amounts in thousands)

|  | <u>2018</u>     | <u>2017</u>    | <u>2016</u>    | <u>2015</u>    |
|--|-----------------|----------------|----------------|----------------|
| Contractually required contribution                                  | \$ 13,638       | 9,174          | 7,233          | 3,906          |
| Contributions in relation to the contractually required contribution | <u>(13,638)</u> | <u>(9,174)</u> | <u>(7,233)</u> | <u>(3,906)</u> |
| Contribution deficiency (excess)                                     | <u>\$ —</u>     | <u>—</u>       | <u>—</u>       | <u>—</u>       |
| Covered-employee payroll   | \$ 120,783      | 114,464        | 95,926         | 88,210         |
| Contributions as a percentage of covered-employee payroll            | 11.3 %          | 8.0 %          | 7.5 %          | 4.4 %          |

Note: Contributed by State on behalf of the Hospital

See accompanying independent auditors' report.

**Notes:**

- 1) Information provided for Required Supplementary Information will be provided for ten years as the information becomes available in subsequent years.
- 2) There were no significant changes in benefits for any of the actuarial valuations used to determine required contributions.

**UNIVERSITY HOSPITAL**  
Required Supplementary Information

Schedules of the Hospital's Proportionate Share of the Net Pension Liability

(Unaudited)

June 30, 2018

(Dollar amounts in thousands)

|   | <u>2018</u> | <u>2017</u> | <u>2016</u> | <u>2015</u> |
|---|-------------|-------------|-------------|-------------|
| Hospital's proportion of the net pension liability  | 2.112 %     | 1.878 %     | 1.732 %     | 1.722 %     |
| Hospital's proportionate share of the net pension liability   | \$ 541,572  | 552,097     | 410,860     | 346,611     |
| Hospital's covered-employee payroll   | 114,464     | 95,926      | 88,210      | 79,796      |
| Hospital's proportionate share of the net pension liability as a percentage of its covered-employee payroll | 473.26 %    | 575.55 %    | 465.77 %    | 434.37 %    |
| Plan fiduciary net position as a percentage of the total pension liability                                  | 36.78 %     | 31.20 %     | 38.21 %     | 42.74 %     |

See accompanying independent auditors' report.

**Notes:**

- 1) Information provided for Required Supplementary Information will be provided for ten years as the information becomes available in subsequent years.
- 2) There were no significant changes in benefits for any of the actuarial valuations used to determine required contributions.



**UNIVERSITY HOSPITAL**  
Required Supplementary Information

Schedule of the Hospital's Proportionate Share of the Other Postemployment  
Benefit (OPEB) Liability

(Unaudited)

June 30, 2018

(Dollar amounts in thousands)

|   |                          |
|---|--------------------------|
| Hospital's proportion of the collective total OPEB liability  | — %                      |
| Hospital's proportionate share of the collective total OPEB liability   | — %                      |
| State of New Jersey's proportionate share of the collective total<br>OPEB liability associated with the Hospital                    | \$ <u>618,890</u>        |
| Total proportionate share of the collective OPEB liability  | \$ <u><u>618,890</u></u> |
| Hospital's covered-employee payroll   | \$ 193,083               |
| Hospital's proportionate share of the collective total OPEB liability as a<br>percentage of the Hospital's covered-employee payroll | — %                      |

See accompanying independent auditor's report.

**Notes:**

- 1) Information provided for Required Supplementary Information will be provided for ten years as the information becomes available in subsequent years.
- 2) For the State Health Benefit State Retired Employees Plan, there are no assets accumulated in a trust that meets the criteria in paragraph 4 of GASB 75.