# PHILADELPHIA HEALTH & EDUCATION CORPORATION - DREXEL UNIVERSITY COLLEGE OF MEDICINE AND SUBSIDIARY

FINANCIAL REPORT
June 30, 2011

Drexel
UNIVERSITY

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## INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Philadelphia Health & Education Corporation
Philadelphia, Pennsylvania

We have audited the accompanying consolidated statements of financial position of Philadelphia Health & Education Corporation, doing business as Drexel University College of Medicine, and its subsidiary (the "College") as of June 30, 2011 and 2010, and the related consolidated statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the College's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the College's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the College at June 30, 2011 and 2010, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

September 15, 2011

# PHILADELPHIA HEALTH & EDUCATION CORPORATION - DREXEL UNIVERSITY COLLEGE OF MEDICINE and SUBSIDIARY

**CONSOLIDATED STATEMENTS of FINANCIAL POSITION**
**as of JUNE 30, 2011 and 2010 (in thousands)**

| ASSETS | 2011 | 2010 |
|---|---|---|
| Cash and cash equivalents: | | |
| Operating cash | $ 19,822 | $ 8,057 |
| Risk Retention Group cash | 4,773 | 4,507 |
| Accounts receivable, net: | | |
| Patients | 6,890 | 7,268 |
| Grants, contracts and other | 8,368 | 7,551 |
| Drexel University, tuition and other | 5,507 | 4,285 |
| Tenet Healthcare Corporation | 981 | 2,175 |
| Total accounts receivable, net | 21,746 | 21,279 |
| Contributions receivable, net | 2,125 | 983 |
| Other assets | 3,119 | 4,834 |
| Deposits with bond trustees | 2,178 | 4,275 |
| Beneficial interests in trusts | 19,495 | 16,762 |
| Investments | 163,510 | 140,131 |
| Student loans receivable, net | 14,426 | 16,099 |
| Buildings, property and equipment, net | 59,857 | 55,010 |
| **Total assets** | **$ 311,051** | **$ 271,937** |
| **LIABILITIES** | | |
| Accounts payable | $ 10,227 | $ 10,209 |
| Accrued expenses | 44,127 | 39,457 |
| Deposits and deferred revenue | 15,421 | 5,520 |
| Capital lease, affiliate | 2,683 | 2,841 |
| Government advances for student loans | 13,018 | 12,721 |
| Bonds payable | 21,913 | 22,372 |
| **Total liabilities** | **107,389** | **93,120** |
| **NET ASSETS** | | |
| Unrestricted | 29,590 | 17,052 |
| Temporarily restricted | 61,694 | 54,666 |
| Permanently restricted | 112,378 | 107,099 |
| **Total net assets** | **203,662** | **178,817** |
| **Total liabilities and net assets** | **$ 311,051** | **$ 271,937** |

See notes to consolidated financial statements.

# PHILADELPHIA HEALTH & EDUCATION CORPORATION - DREXEL UNIVERSITY COLLEGE OF MEDICINE and SUBSIDIARY

**CONSOLIDATED STATEMENT of ACTIVITIES for the year ended JUNE 30, 2011 (in thousands)**

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| **OPERATING REVENUE** | | | | |
| Patient care activities | $ 95,595 | | | $ 95,595 |
| Affiliate tuition and fees (net of discounts of $4,222) | 62,174 | | | 62,174 |
| Government grants and contracts | 24,515 | | | 24,515 |
| Private grants and contracts | 5,038 | | | 5,038 |
| State appropriations | 10,622 | | | 10,622 |
| Contributions | 680 | $ 2,917 | | 3,597 |
| Endowment payout under spending formula | 572 | 5,054 | $ 42 | 5,668 |
| Investment income, net | 1,987 | 74 | | 2,061 |
| Other revenue | 18,016 | | | 18,016 |
| Net assets released from restrictions | 10,303 | (10,301) | (2) | |
| **Total operating revenue** | **229,502** | **(2,256)** | **40** | **227,286** |
| **OPERATING EXPENSE** | | | | |
| Patient care activities | 110,959 | | | 110,959 |
| Education and general: | | | | |
| Instruction | 23,032 | | | 23,032 |
| Research and public service | 27,122 | | | 27,122 |
| Academic support | 6,885 | | | 6,885 |
| Student services | 2,247 | | | 2,247 |
| Institutional support | 28,877 | | | 28,877 |
| Scholarships and fellowships | 3,684 | | | 3,684 |
| **Total education and general** | **91,847** | | | **91,847** |
| Depreciation and amortization | 7,199 | | | 7,199 |
| Operation and maintenance | 15,729 | | | 15,729 |
| Interest | 998 | | | 998 |
| **Total operating expense** | **226,732** | | | **226,732** |
| **Change in net assets from operating activities** | **2,770** | **(2,256)** | **40** | **554** |
| **NON-OPERATING ACTIVITY** | | | | |
| Contributions | | | 1,849 | 1,849 |
| Realized/unrealized gain on investments, net of endowment payout | 9,844 | 9,284 | 3,390 | 22,518 |
| Other non-operating expense | (76) | | | (76) |
| **Change in net assets from non-operating activities** | **9,768** | **9,284** | **5,239** | **24,291** |
| **Change in net assets** | **12,538** | **7,028** | **5,279** | **24,845** |
| **Net assets at beginning of year** | **17,052** | **54,666** | **107,099** | **178,817** |
| **Net assets at end of year** | **$ 29,590** | **$ 61,694** | **$ 112,378** | **$ 203,662** |

See notes to consolidated financial statements.

# PHILADELPHIA HEALTH & EDUCATION CORPORATION - DREXEL UNIVERSITY COLLEGE OF MEDICINE and SUBSIDIARY

**CONSOLIDATED STATEMENT of ACTIVITIES for the year ended JUNE 30, 2010 (in thousands)**

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|---|---|---|---|
| **OPERATING REVENUE** | | | | |
| Patient care activities | $ 91,118 | | | $ 91,118 |
| Affiliate tuition and fees (net of discounts of $4,523) | 59,719 | | | 59,719 |
| Government grants and contracts | 22,254 | | | 22,254 |
| Private grants and contracts | 5,208 | | | 5,208 |
| State appropriations | 10,483 | | | 10,483 |
| Contributions | 407 | $ 4,438 | | 4,845 |
| Endowment payout under spending formula | 661 | 5,727 | $ 49 | 6,437 |
| Investment income, net | 1,575 | 67 | | 1,642 |
| Other revenue | 17,249 | | | 17,249 |
| Net assets released from restrictions | 10,819 | (10,819) | | |
| **Total operating revenue** | **219,493** | **(587)** | **49** | **218,955** |
| **OPERATING EXPENSE** | | | | |
| Patient care activities | 108,875 | | | 108,875 |
| Education and general: | | | | |
| Instruction | 18,924 | | | 18,924 |
| Research and public service | 24,913 | | | 24,913 |
| Academic support | 9,030 | | | 9,030 |
| Student services | 2,095 | | | 2,095 |
| Institutional support | 24,545 | | | 24,545 |
| Scholarships and fellowships | 4,799 | | | 4,799 |
| **Total education and general** | **84,306** | | | **84,306** |
| Depreciation and amortization | 7,498 | | | 7,498 |
| Operation and maintenance | 15,153 | | | 15,153 |
| Interest | 883 | | | 883 |
| **Total operating expense** | **216,715** | | | **216,715** |
| **Change in net assets from operating activities** | **2,778** | **(587)** | **49** | **2,240** |
| **NON-OPERATING ACTIVITY** | | | | |
| Contributions | | | 513 | 513 |
| Realized/unrealized gain on investments, net of endowment payout | 1,057 | 5,156 | 1,612 | 7,825 |
| Other non-operating expense | (88) | | | (88) |
| **Change in net assets from non-operating activities** | **969** | **5,156** | **2,125** | **8,250** |
| **Change in net assets** | **3,747** | **4,569** | **2,174** | **10,490** |
| **Cumulative effect of accounting change (Note 1)** | **1,455** | | | **1,455** |
| **Net assets at beginning of year** | **11,850** | **50,097** | **104,925** | **166,872** |
| **Net assets at end of year** | **$ 17,052** | **$ 54,666** | **$ 107,099** | **$ 178,817** |

See notes to consolidated financial statements.

# PHILADELPHIA HEALTH & EDUCATION CORPORATION - DREXEL UNIVERSITY COLLEGE OF MEDICINE and SUBSIDIARY

## CONSOLIDATED STATEMENTS of CASH FLOWS

**for the years ended JUNE 30, 2011 and 2010 (in thousands)**

| | 2011 | 2010 |
|---|---|---|
| **CASH FLOW FROM OPERATING ACTIVITIES** | | |
| Increase in net assets | $ 24,845 | $ 10,490 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization on property | 7,041 | 7,340 |
| Provision for uncollectible accounts | 363 | 705 |
| Loss on disposal of equipment | 4 | |
| Contributions for long-term investment | (1,849) | (513) |
| Actuarial change on annuity liabilities | 270 | 266 |
| Realized/unrealized gain on investments | (27,196) | (13,092) |
| Changes in operating assets and liabilities: | | |
| Accounts and contributions receivable | (1,990) | 5,335 |
| Other assets | 1,715 | 3,828 |
| Accounts payable and accrued expenses | 4,052 | 826 |
| Deposits and deferred revenue | 9,901 | (9,005) |
| **Net cash provided by operating activities** | **17,156** | **6,180** |
| **CASH FLOW FROM INVESTING ACTIVITIES** | | |
| Purchase of investments | (98,536) | (50,835) |
| Proceeds from sales and maturities of investments | 99,620 | 51,681 |
| Proceeds from student loan collections | 2,414 | 2,135 |
| Student loans issued | (723) | (1,194) |
| Purchase of buildings, property and equipment | (11,547) | (12,224) |
| Use of deposits with bond trustees | 2,097 | 5,477 |
| **Net cash used in investing activities** | **(6,675)** | **(4,960)** |
| **CASH FLOW FROM FINANCING ACTIVITIES** | | |
| Contributions restricted for endowments | 1,849 | 513 |
| Payments on annuity obligations | (137) | (146) |
| Government advances (refunds) for student loans | 297 | (171) |
| Repayment of long-term debt | (459) | (445) |
| **Net cash provided by (used in) financing activities** | **1,550** | **(249)** |
| **Net increase in cash and cash equivalents** | **12,031** | **971** |
| **Cash and cash equivalents at beginning of year** | **12,564** | **11,593** |
| **Cash and cash equivalents at end of year** | **$ 24,595** | **$ 12,564** |
| **SUPPLEMENTAL INFORMATION:** | | |
| Cash paid for interest | $ 1,044 | $ 1,093 |
| Amortization of capital lease | $ 158 | $ 158 |
| Amounts accrued for purchase of buildings, property and equipment | $ 1,358 | $ 855 |

See notes to consolidated financial statements.

## 1. Organization and Summary of Significant Accounting Policies

**Organization:**

The Philadelphia Health & Education Corporation, doing business as Drexel University College of Medicine (the "College" or "Corporation"), is a research university concentrating in medical and related education located in Philadelphia, Pennsylvania. On July 1, 2002, the Corporation became a non-profit affiliate of Drexel University ("Drexel"), a Philadelphia non-profit corporation. The Corporation is an exempt organization under Section 501 (c) (3) of the Internal Revenue Code.

*Schuylkill Crossing Reciprocal Risk Retention Group* - The Schuylkill Crossing Reciprocal Risk Retention Group (the "RRRG"), a majority-owned subsidiary of the College, operates to provide primary coverage for claims-made medical professional liability insurance for health care professionals employed by the College. Ownership of the RRRG was split 87% and 13% between the College and Drexel, respectively, through November 9, 2010. Effective November 10, 2010, the ownership allocation was adjusted to 85% for the College and 15% for Drexel (see Note 12).

At June 30, 2011, total assets and ownership equity of the RRRG amounted to $32,671,000 and $5,138,000, respectively, and were $32,290,000 and $4,446,000, respectively, at June 30, 2010. The balances and activities of the RRRG, including the noncontrolling interest, are included in the accompanying consolidated financial statements. Changes in unrestricted net assets attributable to the controlling and noncontrolling interests for the years ended June 30, 2011 and 2010 were as follows:

| | (in thousands) | | |
|---|---|---|---|
| **2011** | **Total** | **Controlling Interest** | **Noncontrolling Interest** |
| **Beginning balance** | $ 4,446 | $ 2,991 | $ 1,455 |
| Revenue | 1,173 | 1,008 | 165 |
| Expense | (481) | (403) | (78) |
| **Ending balance** | **$ 5,138** | **$ 3,596** | **$ 1,542** |
| **2010** | | | |
| **Beginning balance** | $ 3,052 | $ 1,691 | $ 1,361 |
| Revenue | 1,008 | 877 | 131 |
| Expense | (1,251) | (1,088) | (163) |
| Contributions | 1,637 | 1,511 | 126 |
| **Ending balance** | **$ 4,446** | **$ 2,991** | **$ 1,455** |

*Affiliations and Agreements* - The College is party to an Academic Affiliation Agreement with Tenet Healthcare Corporation ("Tenet") intended to establish a relationship to foster continued coordination and integration between the College and Tenet hospitals. This agreement, dated November 10, 1998 and subsequently amended on April 25, 2002, is effective until June 30, 2022 and may be renewed thereafter for separate and successive five-year terms. Under the terms of the agreement, the College commits to furnish administrative, supervisory, and teaching services to Tenet at budgeted levels through June 30, 2022 (see Note 14).

The College is party to an agreement to provide teaching and administrative services to Drexel for the education of Drexel's medical students and students in the health professions. The agreement, which automatically renews annually, is effective until June 30, 2012. In addition, the College has engaged Drexel to provide service and personnel for its administrative and academic operations (see Note 14).

**Significant Accounting Policies:**

*Basis of Accounting* – The financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America for not-for-profit organizations. Net assets, revenues, gains, expenses and losses are classified as unrestricted, temporarily restricted or permanently restricted based on the existence or absence of donor-imposed restrictions as follows:

*Permanently Restricted* – Net assets subject to donor-imposed stipulations that they be maintained permanently by the College. Generally, donors of these assets permit the use of all or part of the income earned on these assets.

*Temporarily Restricted* – Net assets subject to donor-imposed restrictions that can be fulfilled by actions of the College in accordance with those stipulations or by the passage of time. The College classifies gifts to acquire long-lived assets as temporarily restricted net assets. The release of restriction occurs when the asset is placed in service.

*Unrestricted* – Net assets not subject to donor-imposed restrictions. These net assets may be designated for specific purposes by action of the Board of Trustees or may otherwise be limited by contractual agreements with outside parties. Expenses are shown as decreases in unrestricted net assets. Expirations of donor-imposed stipulations are reported as net assets released from restrictions. Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless explicit donor stipulation or law restricts their use.

*Patient Care Activities* – Faculty physicians participate in several physician practice plans that are managed by the College. Revenue and expenses related to these practice plans are recorded by the College as patient care activities.

Patient care activities represent amounts received and the estimated net realizable amounts due from patients and third-party payors for services rendered. The College provides care to patients under various reimbursement arrangements, including Medicare and Medicaid. These arrangements provide for payment for covered services at agreed-upon rates under certain fee schedules and various discounts from charges. Provisions have been made in the consolidated financial statements for estimated contractual adjustments, representing the difference between the customary charges for services rendered and related reimbursement. In 2011 and 2010, revenue from Medicare and Medicaid programs combined and from managed care payors accounted for 20% and 53%, respectively, and 17% and 54%, respectively, of the College's gross patient service revenue.

*Cash and Cash Equivalents* – These are bank deposits and other investments with original maturities of 90 days or less.

*Contributions Receivable* – Contributions and unconditional pledges are recognized at fair value.

*Beneficial Interests in Trusts* – The College is the beneficiary of the income of these funds but has neither possession nor control of the investments. Beneficial interests in trusts are recorded at the present value of their expected future cash flows (see Note 3).

*Fair Value of Financial Instruments* – The College applies fair value measurements to contributions receivable, beneficial interests in trusts, endowment investments, self-insurance escrow funds, deposits with bond trustees and annuities. A reasonable estimate of the fair value of student loans receivable under government loan programs and refundable federal student loans could not be made because the loans are not readily saleable. These loans are recorded at cost, less an allowance for doubtful accounts (see Note 5). See Notes 2, 3, 6 and 10 for additional fair value disclosures.

*Non-operating Activities* – Non-operating activities include permanently restricted contributions, loss on the disposal of equipment, gain on investments in excess of the endowment spending rule and claims associated with the Allegheny Health, Education and Research Foundation.

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

*Recent Accounting Pronouncements* – In September 2009, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2009-12 *Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)*. ASU 2009-12 amends Accounting Standards Codification ("ASC") Topic 820 for Fair Value Measurements and Disclosures to: (1) permit a reporting entity, in certain situations as a practical expedient, to measure the fair value of an alternative investment on the basis of the net asset value per share of the investment and (2) require additional disclosures for such investments. The changes related to this update are effective for periods ending after December 15, 2009. The College adopted this guidance for the year ended June 30, 2010 (see Note 3).

Effective July 1, 2010, the College adopted ASC 810, *Not-for-Profit Entities: Mergers and Acquisitions* that provides guidance on the combination of not-for-profit entities and identifies certain presentation and disclosure requirements for entities with noncontrolling (formerly minority) interests in consolidated subsidiaries. The noncontrolling interest in the RRRG of $1,542,000 and $1,455,000 at June 20, 2011 and 2010, respectively, is incorporated in the College's consolidated financial statements (see Notes 1 and 11).

Effective July 1, 2010, the College adopted ASU No. 2010-06, *Fair Value Measurements and Disclosures*, which amends ASC 820, adding new disclosure requirements for Levels 1 and 2; separate disclosures of purchases, sales, issuances, and settlements relating to Level 3 measurements and clarification of existing fair value disclosures. The impact of ASU 2010-06 is limited to these additional disclosures (see Note 3).

On July 21, 2010, the FASB issued ASU 2010-20, *Disclosures About the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, which amends ASC 310, *Receivables*, by requiring more robust and disaggregated disclosures about the credit quality of an entity's financing receivables and its allowance for credit losses. The objective of enhancing these disclosures is to improve financial statement users' understanding of (1) the nature of an entity's credit risk associated with its financing receivables and (2) the entity's assessment of that risk in estimating its allowance for credit losses as well as changes in the allowance and the reasons for those changes. ASU 2010-20 was adopted by the College on June 30, 2011 and the required disclosures related to student loans receivable are included in Note 5 to the financial statements.

## 2. Investments and Investment Return

At June 30, the carrying value of investments included the following:

| | (in thousands) 2011 | 2010 |
|---|---|---|
| Equity securities | $ 77,755 | $ 68,581 |
| Fixed income securities and bond funds | 14,737 | 14,270 |
| Mutual funds | 2,785 | |
| Alternative investments | 23,683 | 19,052 |
| Real estate and real assets | 12,089 | 7,121 |
| Money market funds | 4,141 | 6,228 |
| **Total endowment investments** | **135,190** | **115,252** |
| Self-insurance escrow funds (Note 12) | 10,320 | 8,879 |
| RRRG guaranteed investment contract (Note 12) | 18,000 | 16,000 |
| **Total investments** | **$ 163,510** | **$ 140,131** |

The following summarizes the College's total investment return and its classification in the financial statements for the years ended June 30, 2011 and 2010:

| | (in thousands) | | | |
|---|---|---|---|---|
| **2011** | **Unrestricted** | **Temporarily Restricted** | **Permanently Restricted** | **Total** |
| Dividends and interest | $ 572 | $ 418 | | $ 990 |
| Net realized and unrealized gain | 9,844 | 13,920 | $ 3,432 | 27,196 |
| Return on endowment investments | 10,416 | 14,338 | 3,432 | 28,186 |
| Interest on other investments | 1,987 | 74 | | 2,061 |
| Total return on investments | 12,403 | 14,412 | 3,432 | 30,247 |
| Investment return designated for current operations | (2,559) | (5,128) | (42) | (7,729) |
| **Investment return in excess of amounts designated for current operations** | **$ 9,844** | **$ 9,284** | **$ 3,390** | **$ 22,518** |
| **2010** | | | | |
| Dividends and interest | $ 661 | $ 576 | | $ 1,237 |
| Net realized and unrealized gain | 1,057 | 10,374 | $ 1,661 | 13,092 |
| Return on endowment investments | 1,718 | 10,950 | 1,661 | 14,329 |
| Interest on other investments | 1,575 | | | 1,575 |
| Total return on investments | 3,293 | 10,950 | 1,661 | 15,904 |
| Investment return designated for current operations | (2,236) | (5,794) | (49) | (8,079) |
| **Investment return in excess of amounts designated for current operations** | **$ 1,057** | **$ 5,156** | **$ 1,612** | **$ 7,825** |

## 3. Fair Value of Financial Instruments

The three-level hierarchy for fair value measurements is based on observable inputs to the valuation of an asset or liability at the measurement date. It prioritizes the inputs to the valuation techniques used to measure fair value by giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). Fair value is defined 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.

The College maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. When available, fair value is based on actively-quoted market prices. In the absence of actively-quoted market prices, price information from external sources, including broker quotes and industry publications, is used. If pricing information from external sources is not available, or if observable pricing is not indicative of fair value, judgment is required to develop the estimates of fair value. In those cases, prices are estimated based on available historical financial data or comparable investment vehicles that reflect widely accepted market valuation practices.

In some cases, the inputs used to measure fair value might fall in different levels of the fair value hierarchy. In those cases, the lowest level input that is significant to a fair value measurement in its entirety determines the applicable level in the fair value hierarchy. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment and consideration of factors specific to the asset. Fair value measurements are categorized as Level 3 when a significant amount of price or other inputs, considered to be unobservable, are used in their valuations. The fair value hierarchy and inputs to valuation techniques are as follows:

*Level 1* - Quoted prices (unadjusted) in active markets for identical assets and liabilities at the measurement date. Instruments categorized in Level 1 primarily consist of a broadly-traded range of equity and debt securities and funds held by bond trustees.

*Level 2* - Inputs other than quoted prices included within Level 1 that are either directly or indirectly observable for the asset or liability, including quoted prices for similar assets or liabilities in active markets, inputs other than quoted prices that are observable for the asset or liability and inputs that are derived from observable market data by correlation or other means. Instruments categorized in Level 2 primarily include non-exchange-traded fixed income securities, structured products, certain bond investments and mutual funds.

*Level 3* - Unobservable inputs for the asset or liability including situations where there is little, if any, market activity for the asset or liability. Instruments categorized in Level 3 consist of partnership investments in hedge funds, alternative and private equities, annuity liabilities and contributions receivable (see Note 6).

The College assesses the valuation hierarchy for each asset or liability measured on an annual basis. From time to time, assets or liabilities will be transferred within hierarchy levels as a result of changes in the valuation methodologies. At June 30, 2011, one investment transferred from Level 3 to Level 2 as a result of an increase in liquidity due to the release of restrictions for redemption. The College's policy is to recognize such transfers at the end of the reporting period.

As of June 30, the assets and liabilities measured at fair value for each hierarchy level were as follows:

| | (in thousands) | | | |
|---|---|---|---|---|
| 2011 | Total | Level 1 | Level 2 | Level 3 |
| **Assets at Fair Value:** | | | | |
| Deposits with bond trustees | $ 2,178 | $ 2,178 | | |
| Beneficial interests in trusts | 19,495 | 19,495 | | |
| **Investments:** | | | | |
| Equity securities | 77,755 | 77,755 | | |
| Fixed income securities and bond funds | 14,737 | 9,809 | $ 4,928 | |
| Mutual funds | 2,785 | | 2,785 | |
| Alternative investments | 23,683 | | 3,124 | $ 20,559 |
| Real estate and real assets | 12,089 | 6,378 | | 5,711 |
| Money market funds | 4,141 | 4,141 | | |
| Investments held in endowment | 135,190 | 98,083 | 10,837 | 26,270 |
| Self-insurance escrow funds (Note 12) | 10,320 | 10,320 | | |
| **Total investments at fair value** | 145,510 | $ 108,403 | $10,837 | $ 26,270 |
| **Investments at Cost:** | | | | |
| RRRG guaranteed investment contract (Note 12) | 18,000 | | | |
| **Total investments** | 163,510 | | | |
| **Total assets** | $ 185,183 | | | |
| **Liabilities at Fair Value:** | | | | |
| Annuities | $ 1,376 | | | $ 1,376 |

| 2010 | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| | (in thousands) | | | |
| **Assets at Fair Value:** | | | | |
| Deposits with bond trustees | $ 4,275 | $ 4,275 | | |
| Beneficial interests in trusts | 16,762 | 16,762 | | |
| **Investments:** | | | | |
| Equity securities | 68,581 | 68,581 | | |
| Fixed income securities and bond funds | 14,270 | 9,114 | $ 5,156 | |
| Alternative investments | 19,052 | | | $ 19,052 |
| Real estate and real assets | 7,121 | 5,136 | | 1,985 |
| Money market funds | 6,228 | 6,228 | | |
| Investments held in endowment | 115,252 | 89,059 | 5,156 | 21,037 |
| Self-insurance escrow funds (Note 12) | 8,879 | 8,879 | | |
| **Total investments at fair value** | 124,131 | $ 97,938 | $ 5,156 | $ 21,037 |
| **Investments at Cost:** | | | | |
| RRRG guaranteed investment contract (Note 12) | 16,000 | | | |
| **Total investments** | 140,131 | | | |
| **Total assets** | $161,168 | | | |
| **Liabilities at Fair Value:** | | | | |
| Annuities | $ 1,243 | | | $ 1,243 |

Detail related to the fair value of the investments that have been estimated using a net asset value equivalent (e.g. ownership interest in partners' capital to which a proportionate share of net assets is attributable) was as follows:

| 2011 | Fair Value (in thousands) | Unfunded Commitments (in thousands) | Redemption Frequency (if currently eligible) | Redemption Notice Period (if applicable) |
|---|---|---|---|---|
| Multi-Strategy Hedge Funds (a) | $ 4,215 | | Quarterly | 65 days |
| Distressed Debt Hedge Funds (b) | 6,807 | | Quarterly/Annually | 90 days |
| Fixed Income Hedge Funds (c) | 3,124 | | Monthly | 60 days |
| Private Capital Funds - Secondaries (d) | 1,844 | $ 1,488 | | |
| Private Capital Funds - Venture Capital (e) | 1,858 | | | |
| Private Capital Funds - Distressed Debt (f) | 1,558 | 1,219 | | |
| Real Asset Funds (g) | 2,509 | 2,907 | | |
| Real Estate Funds (h) | 1,614 | 931 | | |
| Long/Short Equity Hedge Funds (i) | 4,993 | | Quarterly | 45 days |
| Private Capital Funds - Hedge Fund Seeder (j) | 727 | 1,775 | | |
| Private Capital Funds - Mezzanine Debt (k) | 145 | 1,452 | | |
| Total | $ 29,394 | $ 9,772 | | |

| 2010 | (in thousands) Fair Value | Unfunded Commitments | Redemption Frequency (if currently eligible) | Redemption Notice Period (if applicable) |
|---|---|---|---|---|
| Multi-Strategy Hedge Funds (a) | $ 5,938 | | Quarterly | 65 days |
| Distressed Debt Hedge Funds (b) | 6,263 | | Quarterly/Annually | 90 days |
| Fixed Income Hedge Funds (c) | 2,967 | | Monthly | 60 days |
| Private Capital Funds - Secondaries (d) | 384 | $ 2,809 | | |
| Private Capital Funds - Venture Capital (e) | 1,998 | 50 | | |
| Private Capital Funds - Distressed Debt (f) | 1,502 | 1,539 | | |
| Real Asset Funds (g) | 1,029 | 2,745 | | |
| Real Estate Funds (h) | 956 | 1,461 | | |
| **Total** | $ 21,037 | $ 8,604 | | |

(a) This category invests in hedge funds that pursue multiple strategies to diversify risks and reduce volatility. The composite portfolio includes approximately 57% in distressed investments with a liquidation period of 1 to 3 years, 21% arbitrage opportunities, 9% cash, 7% long/short equity and 6% in private equity investments which can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets in the portfolio. If these investments were held, it is estimated that the underlying assets would be liquidated over the next 1 to 3 years. As of June 30, 2010, this category included investments of approximately 57% in credit and distressed credit (with a liquidation period of 1 to 3 years), 19% arbitrage opportunities, 9% cash, 6% long/short equity and 9% private equity. If the private equity investments were held, it is estimated that the underlying assets would have been liquidated over the next 1 to 4 years.

(b) This category includes investments in hedge funds that invest in debt of companies that are in or facing bankruptcy. The investment managers seek to liquidate these investments in 1 to 3 years. The fair value has been estimated using the net asset value per share of the investments. As of June 30, 2010, the liquidation period would have been the same (1 to 3 years) as the investment horizon was still 1 to 3 years.

(c) This category includes investments in hedge funds that invest in publicly traded corporate bonds, sovereign debt and currency forward contracts of emerging market countries. The fair value has been estimated using the net asset value per share of the investments. There were no changes in this category from June 30, 2010.

(d) This category includes investments in private equity funds that invest in the secondary market. The private equity secondary market refers to the buying and selling of pre-existing investor commitments to private equity and other alternative investment funds. These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If the investments were held, it is estimated that the underlying assets of the fund would be liquidated over 3 to 5 years. As of June 30, 2010, the estimated liquidation period would have been 3 to 6 years.

(e) This category includes investments in private equity funds that invest primarily in technology and healthcare companies in the U.S. These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If these investments were held, it is estimated that the underlying assets of the funds would be liquidated over 2 to 5 years. As of June 30, 2010, if these investments were held, it is estimated that the underlying assets would be liquidated over 3 to 6 years.

(f) This category includes investments in private equity funds that invest in legacy loans and securities which banks are otherwise unable to remove from their balance sheets. These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If these investments were held, it is estimated that the underlying assets of the fund would be liquidated over 1 to 6 years. As of June 30, 2010, if these investments were held, it is estimated that the underlying assets would be liquidated over 1 to 7 years.

(g) This category includes investments in private equity funds that invest primarily in real assets (e.g. investments with intrinsic value, such as real estate or commodities). These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If these investments were held, it is estimated that the underlying assets of the fund would be liquidated over 6 to 10 years. As of June 30, 2010, if these investments were held, it is estimated that the underlying assets would be liquidated over 7 to 11 years.

(h) This category includes investments in private equity funds that invest primarily in U.S. commercial real estate. These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If these investments were held, it is estimated that the underlying assets of the fund would be liquidated over the following time frames: approximately 12% in 2 to 4 years, 71% in 6 to 8 years and 17% in 9 to 11 years. As of June 30, 2010, if these investments were held, it is estimated that the underlying assets would be liquidated over the following time frames: approximately 12% in 2 to 5 years and approximately 88% in 7 to 9 years.

(i) This category includes investments in hedge funds that invest both long and short primarily in U.S. common stocks. Management of the hedge funds has the ability to shift investments from value to growth strategies, from small to large capitalization stocks and from a net long position to a net short position. The fair values of the investments have been estimated using the net asset value per share of the investments. Investments representing approximately 50% of the value of the investments cannot be redeemed because the investments include restrictions that do not allow for redemption in the first 12 months after acquisition. The remaining restriction period for these investments was three months at June 30, 2011.

(j) This category includes investments in private equity funds that invest in newly started hedge funds that pursue multiple strategies. The fund provides start-up funding to hedge funds of various strategies with the potential to share in the appreciation of the investment, as well as to share in the management fees gathered by the underlying start-up hedge funds. As of June 30, 2011, the fund's underlying investments were 62% long/short global equity, 21% macro and commodity trading and 17% in global event-driven opportunities. These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If these investments were held, it is estimated that the underlying assets would be liquidated in 5 to 8 years.

(k) This category includes investments in private equity funds that provide mezzanine debt financing to middle market firms. Mezzanine debt differs from mortgage debt in that the mezzanine debt is backed by equity interests in the borrowing firm, versus mortgage financing which is backed by the asset. These investments can never be redeemed with the funds. Instead, distributions are received through the liquidation of the underlying assets of the fund. If these investments were held, it is estimated that the underlying assets would be liquidated over 5 to 8 years.

The net change in the assets included in the Level 3 fair value category using significant unobservable inputs as of June 30 is as follows:

| | (in thousands) 2011 | 2010 |
|---|---|---|
| **Asset balance, beginning of year** | $ 21,037 | $ 16,088 |
| Net unrealized gain | 2,241 | 1,811 |
| Net realized loss | (344) | (385) |
| Purchases | 10,457 | 4,938 |
| Sales | (3,997) | (1,415) |
| Funds transferred to level 2 | (3,124) | |
| **Asset balance, end of year** | $ 26,270 | $ 21,037 |
| **Liability balance, beginning of year** | $ 1,243 | $ 1,123 |
| Actuarial change on annuity liabilities | 270 | 266 |
| Payment on annuity liabilities | (137) | (146) |
| **Liability balance, end of year** | $ 1,376 | $ 1,243 |

## 4. Endowment Funds

The College has an investment policy for endowment assets designed to maximize the total return on the assets invested within an acceptable level of risk consistent with long-term preservation of the real value of the funds. The goal is to manage the portfolio for risk as well as total return, consistent with fiduciary standards of the prudent investor rule.

To satisfy its rate-of-return objectives, the College relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). Endowment assets are invested in several asset classes and subclasses thereof to moderate the volatility of the returns of the total portfolio.

The College's endowment funds include both donor-restricted funds and funds designated by the Board of Trustees to function as endowments (quasi endowments). Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions. Board-designated temporarily restricted endowment funds represent donor-restricted funds which the Board has earmarked for endowment purposes. The earnings on these funds are utilized by the College in a manner consistent with specific donor restrictions on the original contributions.

For the years ended June 30, 2011 and 2010, the College had an endowment spending rule that limited the spending of endowment resources to 5% of the average fair value of the pooled endowment portfolio for the prior three fiscal years. To the extent that current yield is inadequate to meet the spending rule, a portion of cumulative realized net gains is available for current use.

*Interpretation of Relevant Law* – The Board of Trustees of the College has interpreted Pennsylvania Act 141 ("PA Act 141") as requiring the preservation of the fair value of the original gift as specified in the individual trust instruments. As a result of this interpretation, the College classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instruments at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the College in a manner consistent with the standard of prudence prescribed by PA Act 141.

Endowment net asset composition by type of fund is as follows:

| | (in thousands) | | | |
|---|---|---|---|---|
| **2011** | **Unrestricted** | **Temporarily Restricted** | **Permanently Restricted** | **Total** |
| Donor-restricted endowment funds | $ (2,919) | $ 23,107 | $ 88,574 | $ 108,762 |
| Board-designated endowment funds | 7,397 | 15,700 | | 23,097 |
| **Total net assets** | **$ 4,478** | **$ 38,807** | **$ 88,574** | **$ 131,859** |
| **2010** | | | | |
| Donor-restricted endowment funds | $ (10,130) | $ 13,824 | $ 86,356 | $ 90,050 |
| Board-designated endowment funds | 5,897 | 15,920 | | 21,817 |
| **Total net assets** | **$ (4,233)** | **$ 29,744** | **$ 86,356** | **$ 111,867** |

Changes in endowment net assets are as follows:

| | (in thousands) | | | |
|---|---|---|---|---|
| **2011** | **Unrestricted** | **Temporarily Restricted** | **Permanently Restricted** | **Total** |
| **Endowment net assets, beginning of year** | **$ (4,233)** | **$ 29,744** | **$ 86,356** | **$ 111,867** |
| Investment return: | | | | |
| Investment income (loss), net of fees | 84 | 906 | (42) | 948 |
| Net realized gain | 207 | 2,231 | 50 | 2,488 |
| Net unrealized gain | 1,682 | 18,452 | 358 | 20,492 |
| Reclassification for funds with deficiencies | 7,211 | (7,211) | | |
| Total investment return | 9,184 | 14,378 | 366 | 23,928 |
| Contributions | | | 1,849 | 1,849 |
| Use of endowment assets: | | | | |
| Annual transfer for operations | (572) | (5,096) | | (5,668) |
| Other transfers | 99 | (219) | 3 | (117) |
| Total uses | (473) | (5,315) | 3 | (5,785) |
| **Endowment net assets, end of year** | **$ 4,478** | **$ 38,807** | **$ 88,574** | **$ 131,859** |

| 2010 | Unrestricted | Temporarily Restricted (in thousands) | Permanently Restricted | Total |
|---|---|---|---|---|
| **Endowment net assets, beginning of year** | **$ (7,320)** | **$ 27,021** | **$ 85,446** | **$ 105,147** |
| Investment return: | | | | |
| Investment income (loss), net of fees | 99 | 1,071 | (22) | 1,148 |
| Net realized (loss) gain | (3) | (29) | 31 | (1) |
| Net unrealized gain | 906 | 9,892 | 180 | 10,978 |
| Reclassification for funds with deficiencies | 2,281 | (2,281) | | |
| Total investment return | 3,283 | 8,653 | 189 | 12,125 |
| Contributions | | 140 | 513 | 653 |
| Use of endowment assets: | | | | |
| Annual transfer for operations | (661) | (5,776) | | (6,437) |
| Other transfers | 465 | (294) | 208 | 379 |
| Total uses | (196) | (6,070) | 208 | (6,058) |
| **Endowment net assets, end of year** | **$ (4,233)** | **$ 29,744** | **$ 86,356** | **$ 111,867** |

*Endowment Funds with Deficiencies* – From time to time, the fair value of some assets associated with individual donor-restricted endowment funds may fall below the level that donors require to be retained as a perpetual fund, while other assets maintain or exceed the level required. In accordance with generally accepted accounting principles, the aggregate amount of these deficiencies is reported in unrestricted net assets on the consolidated statement of activities. Subsequent investment gains will be used to restore the balances to the fair market value of the original amount of the gift. Subsequent gains above that amount will be recorded as temporarily restricted net assets. Aggregate deficiencies were $2,919,000 and $10,130,000 at June 30, 2011 and 2010, respectively.

## 5. Accounts and Loans Receivable

Accounts receivable are reported at their net realizable value. Accounts are written off against the allowance for doubtful accounts when they are determined to be uncollectible based upon management's assessment of individual accounts. The allowance for doubtful accounts is estimated based on the College's historical losses and periodic review of individual accounts. Interest is not accrued on the balances. Accounts receivable, net of allowances, were as follows:

| | 2011 (in thousands) | 2010 |
|---|---|---|
| Accounts receivable: | | |
| Patient, net of contractual allowances | $ 12,780 | $ 12,592 |
| Grants, contracts and other | 8,710 | 8,078 |
| Drexel University tuition and other | 5,507 | 4,285 |
| Tenet Healthcare Corporation | 981 | 2,175 |
| | 27,978 | 27,130 |
| Less allowance for doubtful accounts | (6,232) | (5,851) |
| **Accounts receivable, net** | **$ 21,746** | **$ 21,279** |

Student loans are disbursed based on financial need and include loans granted by the College from institutional resources and under federal government loan programs. Students have a grace period until repayment is required based upon the earlier of graduation or no longer achieving full-time status. The grace period varies depending on the type of loan. Loans accrue interest after the grace period and are repaid directly to the College. Student loans are uncollateralized and carry default risk. At June 30, 2011 and 2010, student loans represented 5% and 6% of total assets, respectively.

The availability of funds for loans under federal government revolving loan programs is dependent on reimbursements to the pool from repayments of outstanding loans. Funds advanced by the federal government of $13,018,000 and $12,721,000 at June 30, 2011 and 2010, respectively, are ultimately refundable to the government and are classified as liabilities in the statements of financial position. Outstanding loans cancelled under the program result in a reduction of the funds available for loans and a decrease in the liability to the government. Student loans consisted of the following:

| | (in thousands) | |
|---|---|---|
| | **2011** | **2010** |
| Student loans: | | |
| Federal government loan programs: | | |
| Perkins loan program | $ 7,743 | $ 9,348 |
| Health Professions Student Loans and Loans for Disadvantaged Students | 5,593 | 5,613 |
| Federal government loan programs | 13,336 | 14,961 |
| Institutional loan programs | 2,728 | 2,794 |
| | 16,064 | 17,755 |
| Less allowance for doubtful accounts: | | |
| Balance, beginning of year | (1,656) | (1,312) |
| (Decrease) increase in provision for doubtful accounts | 18 | (344) |
| Balance, end of year | (1,638) | (1,656) |
| **Student loans receivable, net** | **$14,426** | **$16,099** |

Allowances for doubtful accounts are established based on prior collection experience and current economic factors which, in management's judgment, could influence the ability of loan recipients to repay the amounts according to the terms of the loan. Further, the College does not evaluate the credit quality of student loans receivable after the initial approval of the loan. Student loans are considered past due when payment is not received within 30 days of the due date, and interest continues to accrue until the loan is paid in full or written off. When student loans receivable are deemed uncollectible, an allowance for doubtful accounts is established.

The College considers the age of the amounts outstanding in determining the collectibility of student loans receivable. The aging of student loans receivable based on days delinquent and the related allowance for doubtful accounts at June 30, 2011 and 2010 is as follows:

| | (in thousands) | | | | |
|---|---|---|---|---|---|
| | < 30 Days | 30-60 Days | 61-90 Days | >= 91 Days | Total |
| **2011** | | | | | |
| Student loans receivable: | | | | | |
| Federal government loan programs | $ 10,858 | $ 449 | $ 113 | $ 1,916 | $ 13,336 |
| Institutional loan programs | 1,740 | 30 | 10 | 948 | 2,728 |
| Total student loans receivable | 12,598 | 479 | 123 | 2,864 | 16,064 |
| Allowance for doubtful accounts: | | | | | |
| Federal government loan programs | | | (11) | (988) | (999) |
| Institutional loan programs | | | (1) | (638) | (639) |
| Total allowance for doubful accounts | | | (12) | (1,626) | (1,638) |
| **Student loans receivable, net** | **$ 12,598** | **$ 479** | **$ 111** | **$ 1,238** | **$ 14,426** |
| **2010** | | | | | |
| Student loans receivable: | | | | | |
| Federal government loan programs | $ 12,404 | $ 432 | $ 77 | $ 2,049 | $ 14,962 |
| Institutional loan programs | 1,749 | 66 | 17 | 961 | 2,793 |
| Total student loans receivable | 14,153 | 498 | 94 | 3,010 | 17,755 |
| Allowance for doubtful accounts: | | | | | |
| Federal government loan programs | | | (8) | (991) | (999) |
| Institutional loan programs | | | (2) | (655) | (657) |
| Total allowance for doubful accounts | | | (10) | (1,646) | (1,656) |
| **Student loans receivable, net** | **$ 14,153** | **$ 498** | **$ 84** | **$ 1,364** | **$ 16,099** |

## 6. Contributions Receivable

Unconditional pledges are reported as contributions receivable and revenue in the appropriate net asset category. Contributions receivable are recorded net of a discount based on current yields for two-to-ten year U.S. Treasury notes, which averaged 1.7% and 2.0% for the years ended June 30, 2011 and 2010, respectively. The College considers these discount rates to be a Level 3 input in the context of FASB ASC 820-10 (see Note 3).

Net contributions receivable as of June 30 were as follows:

| | (in thousands) | |
|---|---|---|
| | 2011 | 2010 |
| Amounts due in: | | |
| Less than one year | $ 1,170 | $ 235 |
| One to five years | 885 | 662 |
| Greater than five years | 135 | 138 |
| Gross contributions receivable | 2,190 | 1,035 |
| Less discount to present value | (65) | (52) |
| **Total contributions receivable, net** | **$ 2,125** | **$ 983** |

Outstanding conditional pledges are dependent upon the fulfillment of certain conditions and amounted to $5,802,000 and $2,996,000 at June 30, 2011 and 2010, respectively. Conditional pledges are not included in the consolidated financial statements.

The following table summarizes the changes in net contributions receivable as of June 30:

| | (in thousands) | |
|---|---|---|
| | 2011 | 2010 |
| **Balance, beginning of year** | **$ 983** | **$ 704** |
| New pledges | 1,668 | 554 |
| Collections on pledges | (513) | (251) |
| Increase in discount to present value | (13) | (24) |
| **Balance, end of year** | **$ 2,125** | **$ 983** |

## 7. Retirement Plan

All eligible employees of the College are offered retirement plan benefits through an IRS Section 403 (b) savings plan. The plan is the Philadelphia Health & Education Corporation Defined Contribution Retirement Plan ("Retirement Plan") and is administered by Teachers Insurance Annuity Association, Fidelity Investments and the Vanguard Group.

For the years ended June 30, 2011 and 2010, the College contributed $8,254,000 and $7,923,000 respectively, to the Retirement Plan, reported as institutional support in the consolidated statements of activities.

## 8. Buildings, Property and Equipment

Buildings, property and equipment owned by the College are stated at cost or, if acquired by gift, at the fair market value on the date of acquisition. The College has received the majority of its artwork through gifts. Artwork items received by gift prior to 1996 are carried at their 1996 appraised (insured) value. Depreciation and amortization is recorded using the straight-line method. Estimated useful lives are as follows: furniture, fixtures and medical equipment, between 5 and 10 years; computer equipment, 3 years; and software, 5 years. Leasehold improvements and buildings and improvements are amortized over the lesser of their useful lives or the term of the lease or depreciated over 25 to 30 years.

The College determined that it has legal obligations to retire certain facilities and equipment. Total asset retirement cost and the related obligation amounted to $76,000 and $222,000 at June 30, 2011 and $78,000 and $210,000 at June 30, 2010, respectively, included in buildings and improvements and accrued expenses, respectively, in the consolidated statements of financial position.

Buildings, property and equipment as of June 30 are summarized as follows:

| | (in thousands) | |
|---|---|---|
| | 2011 | 2010 |
| Art collection | $ 1,659 | $ 1,659 |
| Land and improvements | 2,040 | |
| Leasehold improvements | 26,715 | 25,150 |
| Buildings and improvements | 20,172 | 16,154 |
| Equipment and software | 54,202 | 52,777 |
| Construction in progress | 13,796 | 11,850 |
| | 118,584 | 107,590 |
| Less accumulated depreciation and amortization | (58,727) | (52,580) |
| **Buildings, property and equipment, net** | **$ 59,857** | **$ 55,010** |

## 9. Leases

Future minimum payments by year and in the aggregate under non-cancelable, operating leases with initial or remaining terms of one year or more are as follows:

| | (in thousands) |
|---|---|
| 2012 | $ 11,641 |
| 2013 | 11,212 |
| 2014 | 11,204 |
| 2015 | 10,459 |
| 2016 | 9,599 |
| Thereafter | 57,594 |
| **Total minimum lease payments** | **$ 111,709** |

Total rent expense for operating leases amounted to $13,015,000 and $10,751,000 for the years ended June 30, 2011 and 2010, respectively.

Under the terms of a twenty-year operating lease ending June 30, 2022 with Tenet for educational and medical office space, payments equaled $22.38 per rentable square foot through November 9, 2008, for all space except for special use space, defined as certain research space, which equaled $27.38 per rentable square foot. Effective November 10, 2008, payments were reduced to a blended rate of $19.50 per rentable square foot for the remainder of the lease. The future minimum payments are included in the table above.

On July 1, 2003, the College entered into an agreement with Drexel to lease a building at 2900 Queen Lane, Philadelphia, Pennsylvania, for the sum of $1 annually for a period of 25 years. The proportional cost of the leased property, net of depreciation, has been capitalized and amounted to $2,683,000 and $2,841,000 at June 30, 2011 and 2010, respectively. A capital lease liability has been recorded for the same amount.

## 10. Bonds and Notes Payable

The Pennsylvania Higher Educational Facilities Authority, Drexel University College of Medicine Revenue Bonds, Series of 2007, was issued during fiscal 2008 in the amount of $21,985,000. The proceeds (1) refunded a mortgage loan; (2) financed capital improvements and equipment for the College's Medical Office Building located at 219 North Broad Street, Philadelphia, Pennsylvania, and other facilities used by the College and (3) funded capitalized interest, a debt service reserve fund and other associated costs. Interest accrues at fixed rates from 3.75% to 5% through the 2037 maturity date. The bonds are secured by a security interest in the College's unrestricted revenues, and Drexel has guaranteed to replenish the debt service reserve fund in the event the College fails to do so. At June 30, 2011, total bonds outstanding, including premium, were $21,913,000 with a fair value of $21,164,000. At June 30, 2010, the outstanding bonds, including premium, amounted to $22,372,000 and had a fair value of $22,198,000.

Bond maturities for the fiscal years ending June 30 are as follows:

| | (in thousands) |
|---|---|
| 2012 | $ 475 |
| 2013 | 495 |
| 2014 | 510 |
| 2015 | 530 |
| 2016 | 520 |
| Thereafter | 19,383 |
| **Total** | **$ 21,913** |

The College has entered into a term note – line of credit of $3,500,000 for equipment purchases that accrues interest based on Libor plus 1.25%. Advances are available through July 5, 2012, with equal payments of principal and interest due sixty months thereafter. The line of credit is secured by a lien and security interest in deposits or other sums held by the lender or its affiliates. There were no amounts outstanding at June 30, 2011 or 2010.

In addition, the College maintains an unsecured $10,000,000 Revolving Credit Facility (the "Facility") that accrues interest based on Libor (subject to a floor of 1.00%) plus .25% and matures on April 1, 2012. It can be extended annually based upon the mutual agreement of the College and the bank maintaining the Facility. At June 30, 2011 and 2010, the Facility accrued interest at 1.25%, and there were no amounts outstanding.

## 11. Net Assets

Net assets as of June 30 were as follows:

| | (in thousands) 2011 | 2010 |
|---|---|---|
| Unrestricted: | | |
| Undesignated | $ (30,244) | $ (29,495) |
| Designated for colleges, departments and student loans | 11,150 | 11,603 |
| Physical plant | 42,664 | 37,722 |
| Quasi-endowment funds | 7,397 | 5,897 |
| Reclassification for endowments with deficiencies | (2,919) | (10,130) |
| **Total unrestricted - College** | 28,048 | 15,597 |
| Noncontrolling interest in RRRG | 1,542 | 1,455 |
| **Total unrestricted** | **29,590** | **17,052** |
| Temporarily restricted: | | |
| Funds for instruction, scholarships and capital expenditures: | | |
| Unexpended | 38,587 | 40,843 |
| Endowment realized and unrealized gain | 20,188 | 3,693 |
| Reclassification for endowments with deficiencies | 2,919 | 10,130 |
| **Total temporarily restricted** | **61,694** | **54,666** |
| Permanently restricted: | | |
| Endowment funds | 88,574 | 86,356 |
| Beneficial interests in trusts | 19,894 | 16,870 |
| Student loans and others | 3,910 | 3,873 |
| **Total permanently restricted** | **112,378** | **107,099** |
| **Total net assets** | **$ 203,662** | **$ 178,817** |

## 12. Professional Liability Insurance

The College maintained commercial, occurrence-based insurance coverage for professional liability claims that occurred from November 10, 1998 through November 10, 2003. Beginning on November 10, 2003, the College purchased primary and excess insurance coverage from the RRRG on a claims-made basis. The RRRG provides primary coverage of $500,000 for physicians and midwives and up to $1,000,000 for other health professions and entity coverage. Physicians and midwives also participate in the Pennsylvania Medical Care Availability and Reduction of Error Fund ("Mcare") that covers from $500,000 to $1,000,000. In addition, the College self insures a layer of excess of up to $2,000,000 above the Mcare Fund. The RRRG provided excess coverage above the self-insured layer of an additional $9,000,000 through January 10, 2011. Beginning January 11, 2011, the excess coverage above the self-insured layer provided by the RRRG was $5,000,000.

For self-insured retention amounts for both reported claims and claims incurred but not reported at June 30, 2011 and 2010, respectively, the College and the RRRG recorded combined reserves of $30,072,000 and $28,382,000, net of estimated recoveries from purchased reinsurance of $6,413,000 and $7,935,000, respectively. For fiscal years 2011 and 2010, the reserves were discounted at 7% for the RRRG retained layer and 2% for the self-insured layer. Such reserves are included in accrued expenses in the accompanying consolidated statements of financial position. Escrow funds of $10,320,000 and $8,879,000 at June 30, 2011 and 2010, respectively, plus the RRRG guaranteed investment contract of $18,000,000 and $16,000,000 in 2011 and 2010, respectively, are available to fund these liabilities (see Note 2).

## 13. Commitments and Contingencies

*Healthcare Legislation and Regulation* – The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements and reimbursement for patient services. Federal government activity has continued with respect to investigations and allegations concerning possible violation of billing regulations by healthcare providers. Violations of these regulations could result in the imposition of significant fines and penalties and have a significant effect on reported net income or cash flow.

Management believes that the College is in compliance with applicable government laws and regulations. While no regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

*Litigation* - The nature of the educational and healthcare industries is such that, from time to time, claims will be presented against the College on account of alleged negligence, acts of discrimination, medical malpractice, breach of contract or disagreements arising from the interpretation of laws or regulations. While some of these claims may be for substantial amounts, they are not unusual in the ordinary course of providing educational and healthcare services at a large institution. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters will not have a materially adverse effect on the College's financial condition or results of operations.

*Other Commitments and Contingencies* – The College maintains two letters of credit in the amounts of $9,000 and $260,000 for the benefit of Liberty Mutual Insurance Company and Pennsylvania Manufacturer's Association, respectively, associated with workers' compensation insurance. The letters of credit expire on February 1, 2012 and March 14, 2012, respectively, and are renewed annually. There were no amounts outstanding as of June 30, 2011 or 2010.

The College also maintains a letter of credit in the amount of $225,000 required by the Department of Environmental Protection related to the disposal of nuclear medical waste. It expires on May 14, 2012 and is renewed annually. There was no amount outstanding as of June 30, 2011 or 2010.

## 14. Related Party Transactions

The College has various operating agreements with Tenet and Drexel. Under these agreements, the College acts both as a purchaser and provider of services. Total services purchased from Tenet for the years ended June 30, 2011 and 2010 were $12,862,000 and $13,660,000, respectively. These services include charges for various personnel, administrative and support services related to operating the College and rent. Services provided to Tenet include administrative, supervisory and teaching services connected with faculty physician and residency programs. The charges to Tenet for these services amounted to $20,552,000 and $20,416,000 for the years ended June 30, 2011 and 2010, respectively, and are mainly included in patient care activities revenue in the accompanying consolidated statements of activities.

The College has entered into a General and Administrative Services Agreement engaging Drexel to provide services and personnel for administrative and academic operations. The agreement, which automatically renews annually, is effective until June 30, 2012. Under this agreement, Drexel provided services valued at approximately $12,435,000 and $11,382,000, respectively, for the years ended June 30, 2011 and 2010. The College paid the full cost of the services for each year, reported as institutional support expense in the accompanying consolidated statements of activities. In addition, Drexel provided approximately $12,000,000 and $11,000,000 to the College in fiscal years 2011 and 2010, respectively, for operations, reported as other revenue.

Separately, Drexel funded $2,928,000 and $2,774,000 of the College's Retirement Plan in fiscal years 2011 and 2010, respectively, which is reported as other revenue in the accompanying consolidated statements of activities.

In September 2004, Drexel entered into a guaranteed investment contract ("GIC") with the RRRG that accrued interest at a rate of 7% for the years ended June 30, 2011 and 2010. Drexel intends to renew the contract with interest at the rate of 6.75% effective January 2012. Principal balances of $18,000,000 and $16,000,000 at June 30, 2011 and 2010, respectively, are included in investments in the consolidated statements of financial position (see Note 2).

## 15. Operating Expenses

Expenses for the operation and maintenance of plant, depreciation and interest are not included in the College's patient care and education and general expense categories in the consolidated statements of activities. The allocation of those expenses, based on the space assigned to each, is as follows:

| | (in thousands) | |
|---|---|---|
| | 2011 | 2010 |
| Patient care activities | $ 3,089 | $ 3,074 |
| Instruction | 8,356 | 6,354 |
| Research and public service | 8,510 | 9,726 |
| Academic support | 3,308 | 3,330 |
| Student services | 561 | 948 |
| Institutional support | 102 | 102 |
| **Total** | **$ 23,926** | **$ 23,534** |

## 16. Subsequent Events

The College's President and Annenberg Dean, Richard V. Homan, M.D., announced his resignation effective October 31, 2011. John A. Fry, President of Drexel University, will assume the position of President of the College, and Daniel V. Schidlow, M.D. will assume the position of Interim Dean. Dr. Schidlow is currently the College's Professor of Pediatrics, Pharmacology and Physiology, Chair of the Department of Pediatrics and Physician in Chief at St. Christopher's Hospital for Children in Philadelphia.

The College evaluated events subsequent to June 30, 2011 through September 15, 2011 and determined that there were no additional events requiring adjustment to or disclosure in the consolidated financial statements.

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