Philadelphia Health & Education Corporation – Drexel University College of Medicine and Subsidiary

FINANCIAL REPORT
June 30, 2009

Drexel

DREXEL UNIVERSITY
COLLEGE OF MEDICINE

Deloitte.

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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, 2009 and 2008, 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, 2009 and 2008, 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 17, 2009

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

CONSOLIDATED STATEMENTS of FINANCIAL POSITION
as of JUNE 30, 2009 and 2008 (in thousands)

ASSETS	2009	2008
Cash and cash equivalents:		
Operating cash	$ 7,195	$ 10,411
Risk Retention Group cash	4,398	3,354
Accounts receivable, net:		
Patients	6,081	6,194
Grants, contracts and other	10,391	10,840
Drexel University, tuition and other	9,252	1,665
Tenet HealthSystem	1,530	801
Total accounts receivable, net	27,254	19,500
Contributions receivable, net	704	1,107
Other assets	7,207	6,355
Deposits with bond trustees	9,752	12,972
Beneficial interests in trusts	15,585	20,390
Investments	129,062	173,832
Student loans receivable, net	17,384	16,646
Buildings, property and equipment, net	49,817	49,919
Total assets	**$ 268,358**	**$ 314,486**
LIABILITIES		
Accounts payable	$ 11,749	$ 10,565
Accrued expenses	36,504	36,762
Note payable to Drexel University		1,250
Deposits and deferred revenue	14,525	8,890
Capital leases, affiliate	2,999	3,157
Government advances for student loans	12,892	12,765
Bonds payable	22,817	22,847
Total liabilities	**101,486**	**96,236**
NET ASSETS		
Unrestricted	11,850	32,233
Temporarily restricted	50,097	79,006
Permanently restricted	104,925	107,011
Total net assets	**166,872**	**218,250**
Total liabilities and net assets	**$ 268,358**	**$ 314,486**

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, 2009 (in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
OPERATING REVENUE				
Patient care activities	$ 86,543			$ 86,543
Affiliate tuition and fees (net of discounts of $4,045)	55,322			55,322
Government grants and contracts	20,854			20,854
Private grants and contracts	3,717			3,717
State appropriations	10,123			10,123
Contributions	5,374	$ 4,080		9,454
Endowment payout under spending formula	761	6,460	$ 58	7,279
Investment income, net	1,923	108		2,031
Other revenue	7,907			7,907
Net assets released from restrictions	10,584	(10,432)	(152)	
Total operating revenue	**203,108**	**216**	**(94)**	**203,230**
OPERATING EXPENSE				
Patient care activities	104,499			104,499
Educational and general:				
Instruction	15,367			15,367
Research and public service	21,387			21,387
Academic support	9,618			9,618
Student services	2,025			2,025
Institutional support	24,337			24,337
Scholarships and fellowships	5,173			5,173
Total educational and general	**77,907**			**77,907**
Depreciation and amortization	6,658			6,658
Operation and maintenance	15,480			15,480
Interest	1,057			1,057
Total operating expense	**205,601**			**205,601**
Change in net assets from operating activities	**(2,493)**	**216**	**(94)**	**(2,371)**
NON-OPERATING ACTIVITY				
Contributions			3,043	3,043
Realized/unrealized loss on investments, including endowment payout	(17,839)	(29,125)	(5,035)	(51,999)
Other non-operating expense	(51)			(51)
Change in net assets from non-operating activities	**(17,890)**	**(29,125)**	**(1,992)**	**(49,007)**
Change in net assets	**(20,383)**	**(28,909)**	**(2,086)**	**(51,378)**
Net assets at beginning of year	**32,233**	**79,006**	**107,011**	**218,250**
Net assets at end of year	**$ 11,850**	**$ 50,097**	**$ 104,925**	**$ 166,872**

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, 2008 (in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
OPERATING REVENUE				
Patient care activities	$ 83,415			$ 83,415
Affiliate tuition and fees (net of discounts of $4,124)	53,628			53,628
Government grants and contracts	24,902			24,902
Private grants and contracts	3,973			3,973
State appropriations	10,077			10,077
Contributions	5,522	$ 11,321		16,843
Endowment payout under spending formula	728	6,131	$ 56	6,915
Investment income, net	2,312	2,049		4,361
Other revenue	7,975			7,975
Net assets released from restrictions	12,411	(12,411)		
Total operating revenue	**204,943**	**7,090**	**56**	**212,089**
OPERATING EXPENSE				
Patient care activities	97,141			97,141
Educational and general:				
Instruction	19,427			19,427
Research and public service	23,990			23,990
Academic support	9,789			9,789
Student services	1,936			1,936
Institutional support	25,600			25,600
Scholarships and fellowships	4,976			4,976
Total educational and general	**85,718**			**85,718**
Depreciation and amortization	6,352			6,352
Operation and maintenance	12,947			12,947
Interest	1,177			1,177
Total operating expense	**203,335**			**203,335**
Change in net assets from operating activities	**1,608**	**7,090**	**56**	**8,754**
NON-OPERATING ACTIVITY				
Contributions			1,444	1,444
Realized/unrealized loss on investments, including endowment payout	(3,420)	(27,560)	(2,239)	(33,219)
Other non-operating expense	(46)			(46)
Change in net assets from non-operating activities	**(3,466)**	**(27,560)**	**(795)**	**(31,821)**
Change in net assets	**(1,858)**	**(20,470)**	**(739)**	**(23,067)**
Net assets at beginning of year	**34,091**	**99,476**	**107,750**	**241,317**
Net assets at end of year	**$ 32,233**	**$ 79,006**	**$ 107,011**	**$ 218,250**

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, 2009 and 2008 (in thousands)

	2009	2008
CASH FLOW FROM OPERATING ACTIVITIES		
Decrease in net assets	$ (51,378)	$ (23,067)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	6,500	6,194
Disposals of property and equipment	2	35
Contributions for long-term investment	(3,043)	(1,444)
Actuarial change on annuity liabilities	(244)	(406)
Realized/unrealized loss on investments	51,999	33,219
Changes in operating assets and liabilities:		
Accounts and contributions receivable	(7,351)	356
Other assets	(852)	(678)
Accounts payable and accrued expenses	1,672	7,065
Deposits and deferred revenue	5,635	(2,949)
Net cash provided by operating activities	**2,940**	**18,325**
CASH FLOW FROM INVESTING ACTIVITIES		
Purchase of investments	(228,123)	(152,135)
Proceeds from sales and maturities of investments	225,699	148,520
Proceeds from student loan collections	1,450	1,262
Student loans issued	(2,188)	(2,841)
Purchase of property and equipment	(6,901)	(8,388)
Deposits placed with bond trustees		(21,985)
Use of deposits with bond trustees	3,220	8,990
Net cash used in investing activities	**(6,843)**	**(26,577)**
CASH FLOW FROM FINANCING ACTIVITIES		
Contributions restricted for endowments	3,043	1,444
Payments on annuity obligations	(159)	(188)
Government advances (refunds) for student loans	127	(77)
Proceeds from short-term borrowings		1,250
Proceeds from long-term borrowings		22,870
Repayment of short-term debt	(1,250)	(5,000)
Repayment of long-term debt	(30)	(6,341)
Net cash provided by financing activities	**1,731**	**13,958**
Net (decrease) increase in cash and cash equivalents	**(2,172)**	**5,706**
Cash and cash equivalents at beginning of period	**13,765**	**8,059**
Cash and cash equivalents at end of period	**$ 11,593**	**$ 13,765**
SUPPLEMENTAL INFORMATION:		
Cash paid for interest	$ 1,058	$ 1,051
Amortization of capital lease	$ 158	$ 158

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 is split 87%/13% between the College and Drexel.

At June 30, 2009, the assets and ownership equity of the RRRG amounted to $38,683,000 and $3,052,000 respectively; and the College's proportional interest in the RRRG's revenues and expenses were $891,000 and $2,091,000, respectively. At June 30, 2008, the assets and ownership equity of the RRRG amounted to $31,205,000 and $2,747,000, respectively; and the College's proportional interest in its revenues and expenses were $916,000 and $903,000, respectively. The balances and activities of the RRRG are included in the accompanying consolidated financial statements. The minority interest in the equity of the RRRG of $1,360,000 and $1,321,000 at June 30, 2009 and 2008, respectively, is included in accrued expenses.

Affiliations and Agreements - The College is party to an Academic Affiliation Agreement with Tenet HealthSystem Philadelphia, Inc. ("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 12).

The College is party to an agreement to provide teaching and administrative services to Drexel for the education of Drexel's medical students. The agreement, which automatically renews annually, is effective until June 30, 2010. In addition, the College has engaged Drexel to provide service and personnel for its administrative and academic operations (see Note 12).

Significant Accounting Policies:

Basis of Accounting – The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for not-for-profit organizations. Under these principles, contributions or unconditional promises to give are recognized as revenues in the period received at their net present value, less an allowance for uncollectible pledges. 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. Contributions and income from endowments for which restrictions have been met in the same fiscal year as their receipt are combined and reported with unrestricted revenues. 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. 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 and 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 2009 and 2008, revenue from Medicare and Medicaid programs combined and from managed care payors accounted for 18% and 54%, respectively, and 18% and 53%, 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.

Beneficial Interests in Trusts – These are funds over which the College has neither possession nor control, but is a beneficiary of their income and are therefore recorded at the present value of expected future cash flows. See Note 2 for the fair value of beneficial interests in trusts.

Fair Value of Financial Instruments – 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 Notes 2, 4 and 8 for additional fair value disclosures.

Non-operating Activities – Non-operating activities include permanently restricted contributions, loss on the disposal of equipment, loss 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.

Reclassifications – Certain scholarships and information technology expenses in the 2008 consolidated statement of activities have been reclassified from instruction and institutional support to scholarships and patient care activities to conform to the 2009 classifications and comply with regulatory filing requirements.

Adoption of New Accounting Pronouncements – In February 2007, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* which permits organizations to measure certain financial instruments and certain other items at fair value. SFAS No. 159 was effective for the College on July 1, 2008. The College has adopted the fair value option for contributions receivable under the provisions of SFAS No. 159. See Note 2 for the fair value of investments.

In March 2008, the FASB issued SFAS No. 161, "*Disclosures about Derivative Instruments and Hedging Activities*". SFAS No. 161 requires organizations with derivative instruments to disclose how and why derivative instruments are used, how derivative instruments and related hedged items are accounted for under SFAS No. 133 "*Accounting for Derivative Instruments and Hedging Activities,*" and how derivative instruments and related hedged items affect an organization's financial statements. SFAS No. 161 is effective for financial statements issued for the College as of June 30, 2010. The College does not anticipate that the adoption of this statement will have a material impact on its consolidated financial statements.

2. Investments

Effective July 1, 2008, the College implemented SFAS No. 157, *Fair Value Measurements* that defines fair value 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. SFAS No. 157 clarifies that fair value should be based on assumptions about risk, risks inherent in valuation techniques and the inputs to valuations. SFAS No. 157 also requires fair value measurements to assume that the transaction occurs in the principal market for the asset or liability (the market with the most volume and activity for the asset or liability from the perspective of the reporting entity), or in the absence of a principal market, the most advantageous market for the asset or liability (the market in which the reporting entity would be able to maximize the amount received or minimize the amount paid). The College applies fair value measurements to contributions receivable, beneficial interests in trusts, endowment investments and self-insurance escrow funds.

In accordance with SFAS No. 157, the College maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. Fair value is based on actively-quoted market prices, if available. 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.

SFAS No. 157 requires fair value measurements to be disclosed by level within the fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable data (Level 3). 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 change in net assets in the Level 3 category is a required disclosure and is shown below. 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.

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 and certain bond investments.

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 and alternative and private equities.

As of June 30, 2009, the investments measured at fair value for each hierarchy level are as follows:

		Fair Value Measurements (in thousands) Using		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Investments at Fair Value:				
Beneficial interests in trusts	$ 15,585	$ 15,585		
Investments held in endowment	108,108	90,262	$ 1,758	$ 16,088
Self-insurance escrow funds (Note 10)	6,954	6,954		
	130,647	$ 112,801	$ 1,758	$ 16,088
Investments at Cost:				
RRRG guaranteed investment contract (Note 10)	14,000			
Total investments	**$ 144,647**			

The net change in the assets included in the Level 3 fair value category using significant unobservable inputs for the year ended June 30, 2009 is as follows:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)
	Investments Held in Endowment
Balance at June 30, 2008	**$ 11,354**
Total losses (realized/unrealized) included in changes in net assets	(2,839)
Purchases	7,573
Balance at June 30, 2009	**$ 16,088**
The amount of total losses for the period included in changes in net assets that are attributable to the change in unrealized losses relating to assets still held at the reporting date	**$ (2,783)**

Endowment – Effective June 30, 2009, the College adopted FASB Staff Position ("FSP") No. 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"), and Enhanced Disclosures for All Endowment Funds.* This FSP provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization whether or not it is subject to an enacted version of the UPMIFA for the purpose of improving disclosures about both donor-restricted and board-designated endowment funds. The Commonwealth of Pennsylvania has not enacted UPMIFA as of the date of this report.

Funds with Deficiencies – From time to time due to unfavorable market fluctuations, 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 are unaffected to the same extent and maintain or exceed the level required. In accordance with generally accepted accounting principles, the aggregate amount of deficiencies at June 30, 2009 was $12,411,000, 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 as of June 30, 2008 amounted to $176,000.

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 organization in a manner consistent with the standard of prudence prescribed by PA Act 141.

Endowment net asset composition by type of fund as of June 30, 2009 and 2008 is as follows:

	(in thousands)			
2009	**Unrestricted**	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Donor-restricted endowment funds	$ (12,411)	$ 10,938	$ 85,446	$ 83,973
Board-designated endowment funds	5,091	16,083		21,174
Total Net Assets	**$ (7,320)**	**$ 27,021**	**$ 85,446**	**$ 105,147**
2008				
Donor-restricted endowment funds	$ 6	$ 40,063	$ 82,880	$ 122,949
Board-designated endowment funds	9,167	15,223		24,390
Total Net Assets	**$ 9,173**	**$ 55,286**	**$ 82,880**	**$ 147,339**

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.

Changes in endowment net assets for the years ended June 30, 2009 and 2008 are as follows:

	(in thousands)			
2009	**Unrestricted**	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Endowment net assets, beginning of year	**$ 9,173**	**$ 55,286**	**$ 82,880**	**$ 147,339**
Investment return:				
Investment income, net of fees	128	1,332		1,460
Net realized loss	(988)	(10,246)	(404)	(11,638)
Net unrealized loss	(2,457)	(26,082)	(114)	(28,653)
Reclassification for funds with deficiencies	(12,411)	12,411		-
Total investment return	(15,728)	(22,585)	(518)	(38,831)
Contributions		1,003	3,043	4,046
Use of endowment assets:				
Annual transfer for operations	(761)	(6,518)		(7,279)
Other transfers	(4)	(165)	41	(128)
Total uses	(765)	(6,683)	41	(7,407)
Endowment net assets, end of year	**$ (7,320)**	**$ 27,021**	**$ 85,446**	**$ 105,147**

2008				
Endowment net assets, beginning of year	**$ 11,948**	**$ 82,581**	**$ 81,692**	**$ 176,221**
Investment return:				
Investment income, net of fees	179	1,841		2,020
Net realized gain (loss)	(235)	(2,452)	162	(2,525)
Net unrealized loss	(1,986)	(20,760)	(396)	(23,142)
Total investment return	(2,042)	(21,371)	(234)	(23,647)
Contributions		839	1,444	2,283
Use of endowment assets:				
Annual transfer for operations	(728)	(6,187)		(6,915)
Other transfers	(5)	(576)	(22)	(603)
Total uses	(733)	(6,763)	(22)	(7,518)
Endowment net assets, end of year	**$ 9,173**	**$ 55,286**	**$ 82,880**	**$ 147,339**

For 2009, investment income, net realized losses and net unrealized losses on unendowed investments amounted to $1,978,000, $1,590,000, and $4,246,000, respectively. For 2008, investment income, net realized gains and net unrealized losses on unendowed investments amounted to $4,353,000, $915,000 and $3,565,000, respectively.

Investment Policies - 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 long-term, 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 primary asset classes are stocks, bonds, cash and real estate.

For the years ended June 30, 2009 and 2008, the College had an endowment spending rule that limited the spending of endowment resources to 5% of the average market 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.

At June 30, 2009 and 2008, investments included the following:

	(in thousands)			
	2009		2008	
	Market	Cost	Market	Cost
Equity securities	$ 59,777	$ 69,080	$ 103,427	$ 96,466
Fixed income securities and bond funds	28,604	31,226	42,421	43,190
Real estate	5,422	6,170	2,324	1,932
Money market funds	14,305	14,305	3,614	3,614
Total endowment investments	**108,108**	**120,781**	**151,786**	**145,202**
Self-insurance escrow funds (Note 10)	6,954	6,635	8,046	6,635
RRRG guaranteed investment contract (Note 10)	14,000	14,000	14,000	14,000
Total investments	**$ 129,062**	**$ 141,416**	**$ 173,832**	**$ 165,837**

3. Accounts and Loans Receivable

Accounts and loans receivable, net of allowances, as of June 30 are as follows:

	(in thousands)	
	2009	2008
Accounts receivable		
Patient, net of contractual allowances	$ 11,000	$ 12,544
Grants, contracts and other	10,962	11,454
Tenet HealthSystem	1,530	801
Drexel University tuition and other	9,252	1,665
	32,744	26,464
Less allowance for doubtful accounts	(5,490)	(6,964)
Net accounts receivable	**$ 27,254**	**$ 19,500**
Student loans receivable	$ 18,696	$ 17,927
Less allowance for doubtful accounts	(1,312)	(1,281)
Net student loans receivable	**$ 17,384**	**$ 16,646**

4. Contributions Receivable

Net contributions receivable as of June 30 are as follows:

	(in thousands)	
	2009	2008
Amounts due in:		
Less than one year	$ 444	$ 457
One to five years	208	677
Greater than five years	80	54
Gross contributions receivable	732	1,188
Less discount to present value	(28)	(81)
Total contributions receivable, net	**$ 704**	**$ 1,107**

The current yields for two-to ten year U.S. Treasury notes are used to discount contributions receivable, which averaged 2.292% and 3.375% for the fiscal years ended June 30, 2009 and 2008, respectively. The College considers these discount rates to be a Level 3 input in the context of the SFAS No. 157 hierarchy (see Note 2).

Outstanding conditional promises to give to the College totaled $2,499,000 and $2,750,000 at June 30, 2009 and 2008, respectively, which are dependent upon the fulfillment of certain conditions and, therefore, are not included in the consolidated financial statements.

The following table summarizes the change in net contributions receivable for the year ended June 30, 2009:

	(in thousands)
Balance, beginning of year	**$ 1,107**
New pledges	462
Collections on pledges	(918)
Decrease in discount to present value	53
Balance, end of year	**$ 704**

5. 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, 2009 and 2008, the College contributed $7,734,000 and $6,915,000 respectively, to the Retirement Plan, reported as institutional support in the consolidated statements of activities.

6. Buildings, Property and Equipment

Buildings, property, equipment and artwork 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 or depreciated over the lesser of their useful lives, the term of the lease or 25 to 30 years.

The College determined that it had legal obligations to retire certain facilities and equipment. Total asset retirement cost and the related obligation amounted to $94,000 and $211,000 at June 30, 2009 and $97,000 and $201,000 at June 30, 2008, respectively, and are included in buildings and improvements and accrued expenses, respectively. In 2009 and 2008, depreciation and accretion expenses were $4,000 and $10,000, respectively, and $7,000 and $17,000, respectively.

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

	(in thousands)	
	2009	**2008**
Art collection	$ 1,659	$ 1,659
Leasehold improvements	24,842	24,189
Buildings and improvements	16,163	16,006
Equipment and software	49,556	46,393
Construction in progress	3,845	1,333
	96,065	89,580
Less accumulated depreciation and amortization	(46,248)	(39,661)
Buildings, property and equipment, net	**$ 49,817**	**$ 49,919**

7. 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)
2010	$ 11,675
2011	11,505
2012	11,294
2013	10,933
2014	10,933
Thereafter	77,570
Total minimum lease payments	**$ 133,910**

Total rent expense for operating leases amounted to $12,031,000 and $11,817,000 for the years ended June 30, 2009 and 2008, respectively.

Under the terms of a twenty-year operating lease with Tenet ending June 30, 2022, payments until November 11, 2008 shall equal $22.38 per rentable square foot per annum for all space located within such premises except for special use space, defined as certain research space, which shall equal $27.38 per rentable square foot per annum. Payments were reduced to a blended rate of $19.50 per rentable square foot for the remainder of the lease effective November 12, 2008. The future minimum payments are included in the table above.

In fiscal year 2004, 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 $2,999,000 and $3,157,000 respectively, at June 30, 2009 and 2008. A capital lease liability has been recorded for the same amount.

8. Bonds and Notes Payable

The Pennsylvania Higher Educational Facilities Authority, Drexel University College of Medicine Revenue Bonds, Series of 2007, were 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 College-owned facilities and (3) funded capitalized interest, a debt service reserve fund and other costs associated with issuing the bonds. Interest accrues at fixed rates from 3.75% to 5%, and the bonds mature beginning in 2010 through 2037. 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 in accordance with the loan agreement. At June 30, 2009, the bonds outstanding, including premium, amounted to $22,817,000 and had a market value of $18,669,000.

In fiscal year 2008, the College 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 August 5, 2010, 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 was no amount outstanding at June 30, 2009 and 2008.

In addition, the College maintains an unsecured $10,000,000 Revolving Credit Facility (the "Facility") that accrues interest based on Libor plus .25% and matures on January 1, 2010. It can be extended annually based upon the mutual agreement of the College and the bank maintaining the Facility. At June 30, 2009 and 2008, the Facility accrued interest at .54% and 2.72%, respectively; and there were no amounts outstanding.

For the year ended June 30, 2008, the College received an unsecured loan from Drexel for working capital in the amount of $1,250,000. The loan accrued interest at 2.61% and was paid in full in July 2008.

9. Net Assets

Net assets as of June 30 are as follows:	(in thousands) 2009	2008
Unrestricted:		
Undesignated	$ (30,701)	$ (28,815)
Designated for:		
Colleges, departments and student loans	11,390	9,828
Physical plant	38,481	42,047
Quasi-endowment funds	5,091	9,173
Reclassification for endowments with deficiencies	(12,411)	
Total unrestricted	**11,850**	**32,233**
Temporarily restricted:		
Funds for instruction, scholarships and capital expenditures		
Unexpended	39,159	38,943
Endowment realized and unrealized gain (loss)	(1,473)	40,063
Reclassification for endowments with deficiencies	12,411	
Total temporarily restricted	**50,097**	**79,006**
Permanently restricted:		
Endowment funds	85,446	82,880
Beneficial interests in trusts	15,653	20,348
Student loans and others	3,826	3,783
Total permanently restricted	**104,925**	**107,011**
Total net assets	**$ 166,872**	**$ 218,250**

10. 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 11, 2003, the College purchased primary and excess insurance coverage from the RRRG on a claims-made basis. In addition, the College's physicians and midwives participate in the Pennsylvania Medical Care Availability and Reduction of Error Fund ("Mcare"). The College self insures a layer of excess of up to $2,000,000 above the Mcare Fund and provides an additional $9,000,000 for excess layer coverage from reinsurance.

For self-insured retention amounts for both reported claims and claims incurred but not reported at June 30, 2009 and 2008, respectively, the College recorded reserves of $27,080,000 and $24,183,000, net of estimated recoveries from purchased reinsurance of $15,451,000 and $8,978,000, respectively. In fiscal 2008, the reserves were discounted at 7%. In fiscal 2009, the discount was 7% for the RRRG coverage and 4% for the self-insured layer. Such reserves are included in accrued expenses on the accompanying consolidated statements of financial position. During 2008, based on updated claims information, the College increased its reserve for liability insurance which was offset by a comparable increase in reinsurance recoverable. Self-insurance escrow funds of $6,954,000 and $8,046,000 at June 30, 2009 and 2008, respectively, plus the RRRG guaranteed investment contract, which amounted to $14,000,000 in each year, are available to fund these liabilities when they become due (see Note 2).

11. 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 $50,000 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, 2010 and March 15, 2010, respectively, and are renewed annually. There were no amounts outstanding under these letters of credit as of June 30, 2009 or 2008.

The College also maintains a letter of credit in the amount of $1,125,000 as required by the U.S. Nuclear Regulatory Commission, in connection with the disposal of nuclear medical waste. It expires on May 15, 2010 and is renewed annually. There was no amount outstanding under the letter of credit as of June 30, 2009 or 2008.

Subsequent Events - The College has evaluated subsequent events through September 17, 2009 and determined that there were no subsequent events requiring adjustment or disclosure in the consolidated financial statements.

12. 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, 2009 and 2008 were $15,045,000 and $15,271,000, respectively. These services include charges for various personnel, administrative and support services related to operating the College and rent.

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, 2010. For the years ended June 30, 2009 and 2008, Drexel provided services under this agreement valued at approximately $11,214,000 and $11,689,000, respectively, for which the College paid $6,577,000 annually. Drexel and the College have agreed to a payment methodology which considers, among other things, the incremental costs as opposed to the full cost of services received by the College. The excess in value of services received compared to the payments made by the College of approximately $4,637,000 and $5,112,000 is reported as contribution revenue from Drexel and institutional support expense in the accompanying consolidated statements of activities in 2009 and 2008, respectively.

Separately, Drexel funded $2,663,000 and $2,381,000 of the College's Retirement Plan in fiscal years 2009 and 2008, respectively, and $837,000 of the College's merit-increase program in 2009, both of which are reported as other revenue in the accompanying consolidated statements of activities.

The College provided various administrative, supervisory and teaching services to Tenet in connection with faculty physician and residency programs. Total charges to Tenet for these services were $20,657,000 and $20,815,000 for the years ended June 30, 2009 and 2008, respectively, and are mainly included in patient care activities revenue in the accompanying consolidated statements of activities.

13. Operating Expenses

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

	(in thousands)	
	2009	**2008**
Patient care activities	$ 2,812	$ 2,439
Instruction	6,218	4,783
Research and public service	9,847	8,797
Academic support	3,240	2,714
Student services	973	1,178
Institutional support	105	565
Total	**$ 23,195**	**$ 20,476**

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