

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, 2012 and 2011, 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 as of June 30, 2012 and 2011, 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 18, 2012

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

CONSOLIDATED STATEMENTS of FINANCIAL POSITION

as of JUNE 30, 2012 and 2011 (in thousands)

ASSETS	<u>2012</u>	<u>2011</u>
Cash and cash equivalents:		
Operating cash	\$ 11,539	\$ 19,822
Risk Retention Group cash	3,961	4,773
Accounts receivable, net:		
Patients	6,281	6,890
Grants, contracts and other	14,915	8,368
Drexel University, tuition and other	7,373	5,507
Tenet Healthcare Corporation	3,105	981
Total accounts receivable, net	<u>31,674</u>	<u>21,746</u>
Contributions receivable, net	1,949	2,125
Other assets	3,811	3,119
Deposits with bond trustees	1,491	2,178
Beneficial interests in trusts	18,256	19,495
Investments	159,024	163,510
Student loans receivable, net	12,563	14,426
Buildings, property and equipment, net	<u>58,247</u>	<u>59,857</u>
Total assets	<u>\$ 302,515</u>	<u>\$ 311,051</u>
 LIABILITIES		
Accounts payable	\$ 11,226	\$ 10,227
Accrued expenses	45,011	44,127
Deposits and deferred revenue	8,433	15,421
Capital lease, affiliate	2,526	2,683
Government advances for student loans	13,453	13,018
Bonds payable	<u>21,438</u>	<u>21,913</u>
Total liabilities	<u>102,087</u>	<u>107,389</u>
 NET ASSETS		
Unrestricted	25,626	28,048
Unrestricted - noncontrolling interest	1,987	1,542
Temporarily restricted	59,869	61,694
Permanently restricted	<u>112,946</u>	<u>112,378</u>
Total net assets	<u>200,428</u>	<u>203,662</u>
 Total liabilities and net assets	<u>\$ 302,515</u>	<u>\$ 311,051</u>

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, 2012 (in thousands)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
OPERATING REVENUE				
Patient care activities	\$ 96,538			\$ 96,538
Affiliate tuition and fees (net of discounts of \$4,573)	63,617			63,617
Government grants and contracts	22,145			22,145
Private grants and contracts	5,009			5,009
State appropriations	2,457			2,457
Contributions	1,122	\$ 3,262		4,384
Endowment payout under spending formula	576	5,404	\$ 44	6,024
Investment income, net	2,211	155		2,366
Other revenue	26,261			26,261
Net assets released from restrictions	6,636	(6,636)		
Total operating revenue	<u>226,572</u>	<u>2,185</u>	<u>44</u>	<u>228,801</u>
OPERATING EXPENSE				
Patient care activities	110,182			110,182
Education and general:				
Instruction	19,235			19,235
Research and public service	28,141			28,141
Academic support	6,338			6,338
Student services	2,071			2,071
Institutional support	29,098			29,098
Scholarships and fellowships	3,733			3,733
Total education and general	<u>88,616</u>			<u>88,616</u>
Depreciation and amortization	7,570			7,570
Operation and maintenance	15,828			15,828
Interest	983			983
Total operating expense	<u>223,179</u>			<u>223,179</u>
Change in net assets from operating activities	<u>3,393</u>	<u>2,185</u>	<u>44</u>	<u>5,622</u>
NON-OPERATING ACTIVITY				
Contributions			1,579	1,579
Realized/unrealized net loss on investments, net of endowment payout	(4,231)	(4,010)	(1,055)	(9,296)
Other non-operating expense	(1,139)			(1,139)
Change in net assets from non-operating activities	<u>(5,370)</u>	<u>(4,010)</u>	<u>524</u>	<u>(8,856)</u>
Change in net assets (including noncontrolling interest of \$445)	(1,977)	(1,825)	568	(3,234)
Net assets at beginning of year	<u>29,590</u>	<u>61,694</u>	<u>112,378</u>	<u>203,662</u>
Net assets at end of year	<u>\$ 27,613</u>	<u>\$ 59,869</u>	<u>\$ 112,946</u>	<u>\$ 200,428</u>

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)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
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	<u>229,502</u>	<u>(2,256)</u>	<u>40</u>	<u>227,286</u>
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	<u>91,847</u>			<u>91,847</u>
Depreciation and amortization	7,199			7,199
Operation and maintenance	15,729			15,729
Interest	998			998
Total operating expense	<u>226,732</u>			<u>226,732</u>
Change in net assets from operating activities	<u>2,770</u>	<u>(2,256)</u>	<u>40</u>	<u>554</u>
NON-OPERATING ACTIVITY				
Contributions			1,849	1,849
Realized/unrealized net 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	<u>9,768</u>	<u>9,284</u>	<u>5,239</u>	<u>24,291</u>
Change in net assets (including noncontrolling interest of \$87)	<u>12,538</u>	<u>7,028</u>	<u>5,279</u>	<u>24,845</u>
Net assets at beginning of year	<u>17,052</u>	<u>54,666</u>	<u>107,099</u>	<u>178,817</u>
Net assets at end of year	<u>\$ 29,590</u>	<u>\$ 61,694</u>	<u>\$ 112,378</u>	<u>\$ 203,662</u>

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, 2012 and 2011 (in thousands)

	<u>2012</u>	<u>2011</u>
CASH FLOW FROM OPERATING ACTIVITIES		
(Decrease) increase in net assets	\$ (3,234)	\$ 24,845
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation and amortization on property	7,413	7,041
Provision for uncollectible accounts	(573)	363
Loss on disposal of equipment	23	4
Contributions for long-term investment	(1,579)	(1,849)
Actuarial change on annuity liabilities	(355)	270
Realized/unrealized net loss (gain) on investments	3,922	(27,196)
Changes in operating assets and liabilities:		
Accounts and contributions receivable	(9,270)	(1,990)
Other assets	(692)	1,715
Accounts payable and accrued expenses	2,076	4,052
Deposits and deferred revenue	<u>(6,988)</u>	<u>9,901</u>
Net cash (used in) provided by operating activities	<u>(9,257)</u>	<u>17,156</u>
CASH FLOW FROM INVESTING ACTIVITIES		
Purchase of investments	(72,623)	(98,536)
Proceeds from sales and maturities of investments	74,426	99,620
Proceeds from student loan collections	2,280	2,414
Student loans issued	(326)	(723)
Purchase of buildings, property and equipment	(5,674)	(11,547)
Use of deposits with bond trustees	<u>687</u>	<u>2,097</u>
Net cash used in investing activities	<u>(1,230)</u>	<u>(6,675)</u>
CASH FLOW FROM FINANCING ACTIVITIES		
Contributions restricted for endowments	1,579	1,849
Payments on annuity obligations	(147)	(137)
Government advances (refunds) for student loans	435	297
Repayment of long-term debt	<u>(475)</u>	<u>(459)</u>
Net cash provided by financing activities	<u>1,392</u>	<u>1,550</u>
Change in cash and cash equivalents	<u>(9,095)</u>	<u>12,031</u>
Cash and cash equivalents at beginning of year	<u>24,595</u>	<u>12,564</u>
Cash and cash equivalents at end of year	<u><u>\$ 15,500</u></u>	<u><u>\$ 24,595</u></u>
SUPPLEMENTAL INFORMATION:		
Cash paid for interest	\$ 1,015	\$ 1,044
Amortization of capital lease	\$ 158	\$ 158
Amounts accrued for purchase of buildings, property and equipment	\$ 1,944	\$ 1,358

See notes to consolidated financial statements.

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

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
for the years ended June 30, 2012 and 2011**

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, 2012 and 2011, total assets of the RRRG totaled \$35,654,000 and \$32,671,000, respectively, and ownership equity was \$8,109,000 and \$5,138,000, respectively. 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, 2012 and 2011 were as follows:

	(in thousands)		
	<u>Total</u>	<u>Controlling Interest</u>	<u>Noncontrolling Interest</u>
Unrestricted net assets - July 1, 2010	\$ 17,052	\$ 15,597	\$ 1,455
Change in net assets attributable to the RRRG	692	605	87
Change in net assets attributable to the College (excluding RRRG)	<u>11,846</u>	<u>11,846</u>	<u> </u>
Total change in net assets	<u>12,538</u>	<u>12,451</u>	<u>87</u>
Unrestricted net assets - June 30, 2011	<u>29,590</u>	<u>28,048</u>	<u>1,542</u>
Change in net assets attributable to the RRRG	2,971	2,526	445
Change in net assets attributable to the College (excluding RRRG)	<u>(4,948)</u>	<u>(4,948)</u>	<u> </u>
Total change in net assets	<u>(1,977)</u>	<u>(2,422)</u>	<u>445</u>
Unrestricted net assets - June 30, 2012	<u>\$ 27,613</u>	<u>\$ 25,626</u>	<u>\$ 1,987</u>

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, 2013. 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 2012 and 2011, revenue from Medicare and Medicaid programs combined and from managed care payors accounted for 21% and 52%, respectively, and 20% 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.

Contributions Receivable – Contributions and unconditional pledges are recorded at the present value of their expected future cash flows.

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, (loss)gain on investments net of the endowment spending rule and severances.

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 – Effective July 1, 2010, the College adopted Accounting Standards Codification (ASC) 810, *Not-for-Profit Entities: Mergers and Acquisitions*, which provides guidance on the combination of not-for-profit entities and identifies certain presentation and disclosure requirements for entities with noncontrolling interests in consolidated subsidiaries. The noncontrolling interest in the RRRG of \$1,987,000 and \$1,542,000 at June 30, 2012 and 2011, respectively, is incorporated in the College's consolidated financial statements (see Notes 1 and 11).

Effective July 1, 2010, the College adopted Accounting Standards Update (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 Financial Accounting Standards Board (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.

In August 2010, the FASB issued ASU 2010-24, *Presentation of Insurance Claims and Related Insurance Recoveries*, which clarifies that entities should not net insurance recoveries against a related claim liability. Further, such entities should determine the claim liability without considering insurance recoveries. ASU 2010-24 was adopted by the College on July 1, 2011. The malpractice liability and related receivables from unaffiliated insurers are recorded in accrued expenses and grants, contracts and other receivables, respectively, in the June 30, 2012 consolidated statement of financial position (see Note 12).

In May 2011, the FASB issued ASU No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*, to improve the comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with U.S. GAAP and International Financial Reporting Standards. The amendments, including expanded disclosures about Level 3 measurements, are effective for interim and annual periods beginning after December 15, 2011 and are to be applied prospectively. On adoption, the College does not expect a material effect to its financial statements.

2. Investments and Investment Return

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

	(in thousands)	
	2012	2011
Equity securities	\$ 70,893	\$ 77,755
Fixed income securities and bond funds	15,522	14,737
Mutual funds	2,669	2,785
Alternative investments	22,000	23,683
Real estate and real assets	16,158	12,089
Money market funds	645	4,141
Total endowment investments	127,887	135,190
Self-insurance escrow funds (Note 12)	9,137	10,320
RRRG guaranteed investment contract (Note 12)	22,000	18,000
Total investments	\$ 159,024	\$ 163,510

The following summarizes the College's total investment return and its classification in the financial statements for the years ended June 30, 2012 and 2011:

	(in thousands)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
2012				
Dividends and interest	\$ 576	\$ 74		\$ 650
Net realized and unrealized (loss) gain	(4,231)	1,320	\$ (1,011)	(3,922)
Return on endowment investments	(3,655)	1,394	(1,011)	(3,272)
Interest on other investments	2,211	156		2,367
Total return on investments	(1,444)	1,550	(1,011)	(905)
Investment return designated for current operations	(2,787)	(5,560)	(44)	(8,391)
Investment return net of amounts designated for current operations	\$ (4,231)	\$ (4,010)	\$ (1,055)	\$ (9,296)
2011				
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 net of amounts designated for current operations	\$ 9,844	\$ 9,284	\$ 3,390	\$ 22,518

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 fair values of alternative investments represent the College's ownership interest in the net asset value (NAV) of the respective fund. Investments held by the fund consist of marketable securities as well as securities that do not have readily determinable fair values. The fair values of the securities held that do not have readily determinable fair values are based on historical cost, appraisals, or other estimates that require varying degrees of judgment. If no public market exists for the investment securities, the fair value is determined by taking into consideration, among other things, the cost of the securities, prices of recent significant placements of securities of the same issue, and subsequent developments concerning the companies to which the securities relate.

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. During 2012, the College determined that its beneficial interests in trusts were more appropriately classified as level 2 in the fair value hierarchy. On June 30, 2012, the College transferred these assets totaling \$18,256,000, from level 1 to level 2. At June 30, 2011, one investment was transferred from level 3 to level 2 as a result of an increase in liquidity due to the release of restrictions for redemption (see level 3 activity below). 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)			
	Total	Level 1	Level 2	Level 3
2012				
Assets at Fair Value:				
Deposits with bond trustees	\$ 1,491	\$ 1,491		
Beneficial interests in trusts	18,256		\$ 18,256	
Investments:				
Equity securities	70,893	70,893		
Fixed income securities and bond funds	15,522	10,387	5,135	
Mutual funds	2,669		2,669	
Alternative investments	21,957		3,035	\$ 18,922
Real estate and real assets	16,201	9,794		6,407
Money market funds	645	645		
Investments held in endowment	127,887	91,719	10,839	25,329
Self-insurance escrow funds (Note 12)	9,137	9,137		
Total investments at fair value	137,024	\$ 100,856	\$ 10,839	\$ 25,329
Investments at Cost:				
RRRG guaranteed investment contract (Note 12)	22,000			
Total investments	159,024			
Total assets	\$ 178,771			
Liabilities at Fair Value:				
Annuities	\$ 874			\$ 874
2011				
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

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:

	<u>(in thousands)</u>		Redemption Frequency (if currently eligible)	Redemption Notice Period (if applicable)
	Fair Value	Unfunded Commitments		
2012				
Long/Short Equity Hedge Funds (a)	\$ 2,251		Quarterly	45 days
Multi-Strategy Hedge Funds (b)	3,554		Quarterly	65 days
Distressed Debt Hedge Funds (c)	3,462		Quarterly	90 days
Fixed Income Hedge Funds (d)	7,295		Monthly/Quarterly	60/65 days
Private Capital Funds - Secondaries (e)	2,619	\$ 953		
Private Capital Funds - Venture Capital (f)	1,048			
Private Capital Funds - Distressed Debt (g)	1,136	195		
Private Capital Funds - Hedge Fund Seeder (h)	1,171	1,265		
Private Capital Funds - Mezzanine Debt (i)	558	990		
Real Asset Funds (j)	3,498	5,005		
Real Estate Funds (k)	1,772	783		
Total	\$ 28,364	\$ 9,191		
2011				
Long/Short Equity Hedge Funds (a)	\$ 4,993		Quarterly	45 days
Multi-Strategy Hedge Funds (b)	4,215		Quarterly	65 days
Distressed Debt Hedge Funds (c)	6,807		Quarterly/Annually	90 days
Fixed Income Hedge Funds (d)	3,124		Monthly	60 days
Private Capital Funds - Secondaries (e)	1,844	\$ 1,488		
Private Capital Funds - Venture Capital (f)	1,858			
Private Capital Funds - Distressed Debt (g)	1,558	1,219		
Private Capital Funds - Hedge Fund Seeder (h)	727	1,775		
Private Capital Funds - Mezzanine Debt (i)	145	1,452		
Real Asset Funds (j)	2,509	2,907		
Real Estate Funds (k)	1,614	931		
Total	\$ 29,394	\$ 9,772		

- (a) This category includes investments in hedge funds that invest primarily in U.S. common stocks with both long and short strategies. 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.
- (b) This category invests in hedge funds that pursue multiple strategies to diversify risks and reduce volatility. At June 30, 2012 and 2011, respectively, the composite portfolio includes approximately 45% and 57% in distressed investments with a liquidation period of 1 to 3 years, 17% and 21% in arbitrage opportunities, 29% and 9% in cash, 3% and 7% in long/short equity and 6% in both years 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.

- (c) 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.
- (d) This category includes investment in hedge funds that invest in: U.S. mortgage backed securities, publicly traded corporate bonds, and 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.
- (e) 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 2 to 5 years at June 30, 2012 (3 to 5 years at June 30, 2011).
- (f) 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 1 to 4 years at June 30, 2012 (2 to 5 years at June 30, 2011).
- (g) 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 5 years at June 30, 2012 (1 to 6 years at June 30, 2011).
- (h) 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, 2012 and 2011, respectively, the fund's underlying investments were 56% and 62% in long/short global equity, 11% and 21% in macro and commodity trading, 15% and 0% in diversified credit, 10% and 0% in arbitrage opportunities, and 8% 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 3 to 7 years at June 30, 2012 (5 to 8 years at June 30, 2011).

- (i) 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 of the fund would be liquidated over 4 to 8 years.
- (j) 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 5 to 12 years at June 30, 2012 (6 to 10 years at June 30, 2011).
- (k) This category includes investments in private equity funds that invest 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. At June 30, 2012, if these investments were held, it is estimated that the underlying assets of the fund would be liquidated over the following time frames: approximately 4% in 1 to 3 years, 75% in 5 to 7 years and 21% in 8 to 10 years. Liquidation time frames at June 30, 2011 were approximately 12% in 2 to 4 years, 71% in 6 to 8 years, and 17% in 9 to 11 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)	
	2012	2011
Asset balance, beginning of year	\$ 26,270	\$ 21,037
Net unrealized (loss) gain	(231)	2,241
Net realized loss	(216)	(344)
Purchases	7,713	10,457
Sales	(8,207)	(3,997)
Funds transferred to level 2		(3,124)
Asset balance, end of year	\$ 25,329	\$ 26,270
Liability balance, beginning of year	\$ 1,376	\$ 1,243
Actuarial change on annuity liabilities	(355)	270
Payment on annuity liabilities	(147)	(137)
Liability balance, end of year	\$ 874	\$ 1,376

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 year ended June 30, 2012, the College had an endowment spending rule that limited the spending of endowment resources to 4.75% of the average fair value of the pooled endowment portfolio for the prior seven fiscal years. For the year ended June 30, 2011, the College had an endowment spending rule that limited the spending of endowment resources to 5% of the average 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)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<u>2012</u>				
Donor-restricted endowment funds	\$ (6,570)	\$ 19,097	\$ 89,716	\$ 102,243
Board-designated endowment funds	6,813	15,616		22,429
Total net assets	\$ 243	\$ 34,713	\$ 89,716	\$ 124,672
<u>2011</u>				
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

Changes in endowment net assets are as follows:

	(in thousands)			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
2012				
Endowment net assets, beginning of year	\$ 4,478	\$ 38,807	\$ 88,574	\$ 131,859
Investment return:				
Investment income (loss), net of fees	57	611	(36)	632
Net realized gain	133	1,423	23	1,579
Net unrealized loss	(406)	(4,248)	(102)	(4,756)
Reclassification for funds with deficiencies	(3,651)	3,651		
Total investment return	(3,867)	1,437	(115)	(2,545)
Contributions			1,575	1,575
Use of endowment assets:				
Annual transfer for operations	(576)	(5,448)	-	(6,024)
Other transfers	208	(83)	(318)	(193)
Total uses	(368)	(5,531)	(318)	(6,217)
Endowment net assets, end of year	\$ 243	\$ 34,713	\$ 89,716	\$ 124,672
2011				
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

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 the deficiencies is reported as a reduction 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 \$6,570,000 and \$2,919,000 at June 30, 2012 and 2011, 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, as of June 30 were as follows:

	<u>(in thousands)</u>	
	<u>2012</u>	<u>2011</u>
Accounts receivable:		
Patient, net of contractual allowances	\$ 11,568	\$ 12,780
Grants, contracts and other	15,204	8,710
Drexel University tuition and other	7,373	5,507
Tenet Healthcare Corporation	3,279	981
	<u>37,424</u>	<u>27,978</u>
Less allowance for doubtful accounts	<u>(5,750)</u>	<u>(6,232)</u>
Accounts receivable, net	<u>\$ 31,674</u>	<u>\$ 21,746</u>

*2012 includes the impact of adoption of ASU 2010-24 (see Notes 1 and 12).

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, 2012 and 2011, student loans represented 4% and 5%, respectively, of total assets.

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 \$13,453,000 and \$13,018,000 at June 30, 2012 and 2011, 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:

	<u>(in thousands)</u>	
	<u>2012</u>	<u>2011</u>
Student loans:		
Federal government loan programs:		
Perkins loan program	\$ 6,101	\$ 7,743
Health Professions Student Loans and Loans for Disadvantaged Students	5,507	5,593
Federal government loan programs	11,608	13,336
Institutional loan programs	2,502	2,728
	<u>14,110</u>	<u>16,064</u>
Less allowance for doubtful accounts:		
Balance, beginning of year	(1,638)	(1,656)
Decrease in provision for doubtful accounts	91	18
Balance, end of year	<u>(1,547)</u>	<u>(1,638)</u>
Student loans receivable, net	<u>\$ 12,563</u>	<u>\$ 14,426</u>

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 collectability of student loans receivable. The aging of student loans receivable based on days delinquent and the related allowance for doubtful accounts at June 30, 2012 and 2011 is as follows:

	(in thousands)				
	<u>< 30 Days</u>	<u>30-59 Days</u>	<u>60-89 Days</u>	<u>>= 90 Days</u>	<u>Total</u>
<u>2012</u>					
Student loans receivable:					
Federal government loan programs	\$ 9,582	\$ 20	\$ 6	\$ 2,000	\$ 11,608
Institutional loan programs	<u>1,303</u>	<u>35</u>	<u> </u>	<u>1,164</u>	<u>2,502</u>
Total student loans receivable	<u>10,885</u>	<u>55</u>	<u>6</u>	<u>3,164</u>	<u>14,110</u>
Allowance for doubtful accounts:					
Federal government loan programs			(1)	(778)	(779)
Institutional loan programs			<u> </u>	<u>(768)</u>	<u>(768)</u>
Total allowance for doubtful accounts			<u>(1)</u>	<u>(1,546)</u>	<u>(1,547)</u>
Student loan receivable, net	<u>\$ 10,885</u>	<u>\$ 55</u>	<u>\$ 5</u>	<u>\$ 1,618</u>	<u>\$ 12,563</u>
<u>2011</u>					
Student loans receivable:					
Federal government loan programs	\$ 10,858	\$ 449	\$ 113	\$ 1,916	\$ 13,336
Institutional loan programs	<u>1,740</u>	<u>30</u>	<u>10</u>	<u>948</u>	<u>2,728</u>
Total student loans receivable	<u>12,598</u>	<u>479</u>	<u>123</u>	<u>2,864</u>	<u>16,064</u>
Allowance for doubtful accounts:					
Federal government loan programs			(11)	(988)	(999)
Institutional loan programs			<u>(1)</u>	<u>(638)</u>	<u>(639)</u>
Total allowance for doubtful accounts			<u>(12)</u>	<u>(1,626)</u>	<u>(1,638)</u>
Student loans receivable, net	<u>\$ 12,598</u>	<u>\$ 479</u>	<u>\$ 111</u>	<u>\$ 1,238</u>	<u>\$ 14,426</u>

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 .9% and 1.7% for the years ended June 30, 2012 and 2011, 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)	
	<u>2012</u>	<u>2011</u>
Amounts due in:		
Less than one year	\$ 1,073	\$ 1,170
One to five years	790	885
Greater than five years	<u>110</u>	<u>135</u>
Gross contributions receivable	1,973	2,190
Less discount to present value	<u>(24)</u>	<u>(65)</u>
Total contributions receivable, net	<u>\$ 1,949</u>	<u>\$ 2,125</u>

Outstanding conditional pledges are dependent upon the fulfillment of certain conditions and amounted to \$6,715,000 and \$5,802,000 at June 30, 2012 and 2011, 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)	
	<u>2012</u>	<u>2011</u>
Balance, beginning of year	\$ 2,125	\$ 983
New pledges	609	1,668
Collections on pledges	(826)	(513)
Decrease (increase) in discount to present value	<u>41</u>	<u>(13)</u>
Balance, end of year	<u>\$ 1,949</u>	<u>\$ 2,125</u>

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, 2012 and 2011, the College contributed \$8,269,000 and \$8,254,000 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 related to the retirement of certain facilities and equipment. At June 30, 2012 and 2011, the asset retirement costs totaled \$73,000 and \$76,000, respectively, and the related obligation totaled \$233,000 and \$222,000, respectively. The asset retirement costs and related obligations are 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:

	<u>(in thousands)</u>	
	<u>2012</u>	<u>2011</u>
Works of art	\$ 1,659	\$ 1,659
Land and improvements	2,040	\$ 2,040
Leasehold improvements	31,725	26,715
Buildings and improvements	24,953	20,172
Equipment and software	53,122	54,202
Construction in progress	<u>7,977</u>	<u>13,796</u>
	121,476	118,584
Less accumulated depreciation and amortization	<u>(63,229)</u>	<u>(58,727)</u>
Buildings, property and equipment, net	<u>\$ 58,247</u>	<u>\$ 59,857</u>

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:

	<u>(in thousands)</u>
2013	\$ 13,448
2014	13,360
2015	10,775
2016	9,709
2017	9,618
Thereafter	<u>47,995</u>
Total minimum lease payments	<u>\$ 104,905</u>

Total rent expense for operating leases amounted to \$12,869,000 and \$13,015,000 for the years ended June 30, 2012 and 2011, respectively.

The College leases educational and medical office space from Tenet under an operating lease expiring June 30, 2022 at a rate of \$19.50 per rentable square foot. 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 \$2,526,000 and \$2,683,000 at June 30, 2012 and 2011, 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, 2012, the outstanding bonds, including premium, amounted to \$21,438,000 and had a fair value of \$21,874,000. At June 30, 2011, total bonds outstanding, including premium, were \$21,913,000 with a fair value of \$21,164,000.

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

	<u>(in thousands)</u>
2013	\$ 495
2014	510
2015	530
2016	550
2017	565
Thereafter	<u>18,788</u>
Total	<u>\$ 21,438</u>

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, 2013, 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, 2012 or 2011.

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, 2013. It can be extended annually based upon the mutual agreement of the College and the bank maintaining the Facility. At June 30, 2012 and 2011, 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)	
	2012	2011
Unrestricted:		
Undesignated	\$ (28,055)	\$ (30,244)
Designated for colleges, departments and student loans	12,832	11,150
Physical plant	40,606	42,664
Quasi-endowment funds	6,813	7,397
Reclassification for endowments with deficiencies	(6,570)	(2,919)
Total unrestricted - College	25,626	28,048
Noncontrolling interest in RRRG	1,987	1,542
Total unrestricted	27,613	29,590
Temporarily restricted:		
Funds for instruction, scholarships and capital expenditures:		
Unexpended	40,772	38,587
Endowment realized and unrealized gain	12,527	20,188
Reclassification for endowments with deficiencies	6,570	2,919
Total temporarily restricted	59,869	61,694
Permanently restricted:		
Endowment funds	89,716	88,574
Beneficial interests in trusts	19,286	19,894
Student loans and others	3,944	3,910
Total permanently restricted	112,946	112,378
Total net assets	\$ 200,428	\$ 203,662

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 is \$5,000,000.

For self-insured retention amounts for both reported claims and claims incurred but not reported at June 30, 2012 and 2011, the College and the RRRG recorded gross combined reserves of \$34,207,000 and \$36,485,000, respectively, and related recoveries from third party insurers of \$6,164,000 and \$6,413,000, respectively. For fiscal years 2012 and 2011, the reserves were discounted at 6.25% and 7%, respectively, for the RRRG retained layer and 2% for the self-insured layer. Such reserves and reinsurance recoveries are included in accrued expenses and grants, contracts and other receivables, respectively, in the accompanying 2012 consolidated statement of financial position. In 2011, the liability, net of the reinsurance recovery, is recorded in accrued expenses (see recent accounting pronouncements above). At June 30, 2012 and 2011, escrow funds of \$9,137,000 and \$10,320,000, respectively, and the RRRG guaranteed investment contract of \$22,000,000 and \$18,000,000, respectively, are available to fund these liabilities (see Note 1).

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 changes in net assets 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, 2013 and March 15, 2013, respectively, and are renewed annually. There were no amounts outstanding as of June 30, 2012 or 2011.

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 15, 2013 and is renewed annually. There was no amount outstanding as of June 30, 2012 or 2011.

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, 2012 and 2011 were \$12,571,000 and \$12,862,000, 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 \$21,287,000 and \$20,552,000 for the years ended June 30, 2012 and 2011, 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, 2013. Under this agreement, Drexel provided services valued at approximately \$13,483,000 and \$12,435,000, respectively, for the years ended June 30, 2012 and 2011. 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 \$13,483,000 and \$12,435,000 to the College in fiscal years 2012 and 2011, respectively, for operations, reported as other revenue.

Separately, Drexel funded \$2,918,000 and \$2,928,000 of the College's Retirement Plan in fiscal years 2012 and 2011, 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 year ended June 30, 2011. Drexel renewed the contract for three additional years with interest rates of 6.75%, 6.5%, and 6.25% effective January 2012, January 2013 and January 2014, respectively. Principal balances of \$22,000,000 and \$18,000,000 at June 30, 2012 and 2011, 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)	
	2012	2011
Patient care activities	\$ 3,148	\$ 3,089
Instruction	8,515	8,356
Research and public service	8,671	8,510
Academic support	3,371	3,308
Student services	572	561
Institutional support	104	102
Total	\$ 24,381	\$ 23,926

16. Subsequent Events

The College evaluated events subsequent to June 30, 2012 through September 18, 2012 and determined that there were no additional events requiring adjustment to or disclosure in the consolidated financial statements.
