

**The Johns Hopkins Hospital**  
**Financial Statements**  
**June 30, 2012 and 2011**

**The Johns Hopkins Hospital**  
**Index**  
**June 30, 2012 and 2011**

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## REPORT OF INDEPENDENT AUDITORS

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To the Board of Trustees of  
The Johns Hopkins Hospital:

In our opinion, the accompanying balance sheets and the related statements of operations and changes in net assets and cash flows present fairly, in all material respects, the financial position of The Johns Hopkins Hospital ("JHH") at June 30, 2012 and 2011, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of JHH's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

A handwritten signature in cursive script that reads "PricewaterhouseCoopers LLP".

September 28, 2012

**The Johns Hopkins Hospital**  
**Balance Sheets**  
**June 30, 2012 and 2011**  
**(in thousands)**

	<u>2012</u>	<u>2011</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 41,074	\$ 153,388
Short-term investments	8,950	89,230
Assets whose use is limited for current liabilities	12,152	9,370
Patient accounts receivable, net of estimated uncollectibles of \$29,636 and \$47,114 at June 30, 2012 and 2011, respectively	210,413	167,573
Due from others	29,362	21,302
Due from affiliates - current portion	31,015	2,876
Inventories of supplies	45,272	36,281
Prepaid expenses and other current assets	28,815	5,484
Total current assets	<u>407,053</u>	<u>485,504</u>
Assets whose use is limited, net of current		
By donors or grantors for:		
Future campus development	644	7,516
Pledges receivable	15,079	25,614
By Board of Trustees	63,382	61,758
Other	7,705	6,549
Total assets whose use is limited, net of current	<u>86,810</u>	<u>101,437</u>
Investments	459,589	587,003
Property, plant and equipment	2,072,864	1,850,549
Less: accumulated depreciation and amortization	(552,048)	(514,360)
Total property, plant and equipment, net	<u>1,520,816</u>	<u>1,336,189</u>
Due from affiliates, net of current portion	264,213	54,641
Net pension asset	-	1,878
Other assets	31,367	4,648
Total assets	<u>\$ 2,769,848</u>	<u>\$ 2,571,300</u>

The accompanying notes are an integral part of these financial statements.

**The Johns Hopkins Hospital**  
**Balance Sheets, continued**  
**June 30, 2012 and 2011**  
**(in thousands)**

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	<u>2012</u>	<u>2011</u>
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term debt	\$ 162,625	\$ 124,995
Accounts payable and accrued liabilities	197,090	199,077
Accrued vacation	18,240	16,755
Due to affiliates	19,725	8,782
Advances from third-party payors	80,257	66,903
Current portion of estimated malpractice costs	<u>21,846</u>	<u>1,235</u>
Total current liabilities	499,783	417,747
Long-term debt, net of current portion	708,198	643,252
Estimated malpractice costs, net of current portion	64,121	39,943
Net pension liability	290,783	133,270
Other long-term liabilities	<u>235,495</u>	<u>127,166</u>
Total liabilities	<u>1,798,380</u>	<u>1,361,378</u>
Net assets:		
Unrestricted	952,208	748,394
Temporarily restricted	<u>19,260</u>	<u>461,528</u>
Total net assets	<u>971,468</u>	<u>1,209,922</u>
Total liabilities and net assets	<u>\$ 2,769,848</u>	<u>\$ 2,571,300</u>

The accompanying notes are an integral part of these financial statements.

**The Johns Hopkins Hospital**  
**Statements of Operations and Changes in Net Assets**  
**For the years ended June 30, 2012 and 2011**  
**(in thousands)**

	<u>2012</u>	<u>2011</u>
Operating revenues:		
Net patient service revenue	\$ 1,634,266	\$ 1,585,310
Other revenue	143,362	130,577
Investment income	14,042	14,145
Net assets released from restrictions used for operations	229	245
Total operating revenues	<u>1,791,899</u>	<u>1,730,277</u>
Operating expenses:		
Salaries, wages and benefits	698,118	667,347
Purchased services	505,647	497,833
Supplies and other	374,736	346,880
Interest	8,349	9,861
Provision for bad debts	34,930	38,243
Depreciation and amortization	84,892	69,357
Total operating expenses	<u>1,706,672</u>	<u>1,629,521</u>
Income from operations	85,227	100,756
Non-operating revenues and expenses:		
Interest expense on swap agreements	(19,115)	(19,078)
Change in market value of swap agreements	(107,608)	24,207
Realized and unrealized (losses) gains on investments	(5,469)	27,049
Loss on advance refunding of debt	(363)	-
Non-operating services	(8,073)	-
(Deficiency) excess of revenues over expenses	<u>(55,401)</u>	<u>132,934</u>
Contributions from affiliates	-	31,200
Unrealized (losses) gains on investments	-	(1,145)
Change in funded status of defined benefit plans	(188,442)	49,240
Net assets released from restrictions used for purchases of property and equipment	447,657	3,397
Increase in unrestricted net assets	<u>203,814</u>	<u>215,626</u>
Changes in temporarily restricted net assets:		
Gifts, grants and bequests	16,235	66,666
Net assets released from restrictions used for purchase of property, plant and equipment	(447,657)	(3,397)
Net assets released from restrictions used for operations	(229)	(245)
Other	(10,617)	-
(Decrease) increase in temporarily restricted net assets	<u>(442,268)</u>	<u>63,024</u>
(Decrease) increase in net assets	(238,454)	278,650
Net assets at beginning of year	<u>1,209,922</u>	<u>931,272</u>
Net assets at end of year	<u>\$ 971,468</u>	<u>\$ 1,209,922</u>

The accompanying notes are an integral part of these financial statements.

**The Johns Hopkins Hospital**  
**Statements of Cash Flows**  
**For the years ended June 30, 2012 and 2011**  
**(in thousands)**

	<u>2012</u>	<u>2011</u>
Operating activities:		
Change in net assets	\$ (238,454)	\$ 278,650
Adjustments to reconcile change in net assets to net cash and cash equivalents (used in) provided by operating activities:		
Depreciation, amortization, and accretion	87,215	73,635
Provisions for bad debts	34,930	38,243
Net realized and unrealized losses (gains) on investments	5,469	(25,905)
Change in market value on swap agreements	107,608	(24,207)
Change in funded status of defined benefit plans	188,442	(49,240)
Restricted contributions and investment income received	(26,770)	(64,882)
Contributions from affiliates	-	(31,200)
Refunding of debt	21,170	-
Changes in assets and liabilities:		
Patient receivable and due from others	(85,830)	(83,759)
Inventories of supplies, prepaid expenses and other current assets	(11,652)	(1,612)
Due (to) from affiliates	(75,853)	13,592
Pledges receivable	10,535	(1,783)
Other assets	(5,058)	5,836
Accounts payable, accrued liabilities and accrued vacation	15,128	15,294
Advances from third-party payors	13,354	(6,161)
Accrued pension benefit costs	(29,051)	8,421
Other long-term liabilities	721	1,795
Estimated malpractice costs	(1,976)	2,556
Net cash and cash equivalents (used in) provided by operating activities	<u>9,928</u>	<u>149,273</u>
Investing activities:		
Purchases of property, plant, and equipment	(284,697)	(216,404)
Purchases of investment securities	(338,006)	(1,379,696)
Sales of investment securities	544,319	1,265,159
Net cash and cash equivalents used in investing activities	<u>(78,384)</u>	<u>(330,941)</u>
Financing activities:		
Proceeds from restricted contributions and investment income received	26,770	64,882
Proceeds from long-term borrowing	284,587	-
Repayment of long-term debt	(204,300)	(13,415)
Contributions from affiliates	-	31,200
Advances to affiliates note payable	(150,915)	-
Net cash and cash equivalents (used in) provided by financing activities	<u>(43,858)</u>	<u>82,667</u>
Decrease in cash and cash equivalents	(112,314)	(99,001)
Cash and cash equivalents at beginning of year	<u>153,388</u>	<u>252,389</u>
Cash and cash equivalents at end of year	<u>\$ 41,074</u>	<u>\$ 153,388</u>
Supplemental disclosure of noncash transactions		
Construction costs incurred but not paid	<u>\$ 33,996</u>	<u>\$ 49,626</u>

The accompanying notes are an integral part of these financial statements.

# The Johns Hopkins Hospital

## Notes to the Financial Statements

### For the years ended June 30, 2012 and 2011

(in thousands)

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#### 1. Organization and Summary of Significant Accounting Policies

*Organization.* The Johns Hopkins Health System (“JHHS”) is the sole member of The Johns Hopkins Hospital (“JHH”). JHHS is a not-for-profit organization incorporated in the State of Maryland to formulate policy among and provide centralized management for JHHS and its Affiliates. In addition, JHHS provides certain shared services including purchasing, legal, coordination of marketing, and other functions for which JHH is charged separately (see Note 13).

JHHS appoints JHH’s Board of Trustees. JHH’s Articles of Incorporation provide that JHHS’ Board of Trustees will approve JHH’s annual operating and capital budgets, significant programmatic changes at JHH, and other significant changes to JHH including amendments of its articles of incorporation or bylaws, mergers, or dissolutions.

JHH’s mission is to provide patient care in the treatment and prevention of human illness which compares favorably with that rendered by any other institution in the United States or abroad.

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

*Basis of Presentation.* The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

*Cash and Cash Equivalents.* Cash and cash equivalents include amounts invested in accounts with depository institutions which are readily convertible to cash, with original maturities of three months or less. Total deposits maintained at these institutions at times exceed the amount insured by federal agencies and therefore, bear a risk of loss. JHH has not experienced such losses on these funds.

*Inventories of Supplies.* Inventories of supplies are composed of medical supplies, drugs, linen, and parts inventory for repairs. Inventories of supplies are recorded at lower of cost or market using a first in, first out method.

*Assets Whose Use is Limited.* Assets whose use is limited or restricted by donor are recorded at fair value at the date of donation, which is then considered cost. Investment income or losses on investments of temporarily restricted assets is recorded as an increase or decrease in temporarily restricted net assets to the extent restricted by the donor or law. The cost of securities sold is based on the specific identification method.

Assets whose use is limited include assets set aside for future capital improvements, assets held by trustees under debt agreements, assets restricted by the board of trustees, and assets held for malpractice funding. These assets consist of cash and short term investments, accrued interest and pledges receivable. The carrying amounts reported in the balance sheets approximate fair value.

**The Johns Hopkins Hospital**  
**Notes to the Financial Statements**  
**For the years ended June 30, 2012 and 2011**  
**(in thousands)**

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*Valuation of Investments.* Investments in equity securities with readily determinable fair values and all investments in debt securities are recorded at fair value in the Balance Sheets (see Note 4). Debt and equity securities traded on a national securities and international exchange are valued as of the last reported sales price on the last business day of the fiscal year; investments traded on the over-the-counter market and listed securities for which no sale was reported on that date are valued at the average of the last reported bid and ask prices.

Investments include equity method investments in managed funds, which include hedge funds, private partnerships and other investments which do not have readily ascertainable fair values and may be subject to withdrawal restrictions. Investments in hedge funds, private partnerships, and other investments (collectively "alternative investments"), are accounted for under the equity method, which approximates fair value. The equity method income or loss from these alternative investments is included in the Statement of Operations and Changes in Net Assets as an unrealized gain or loss within excess of revenues over expenses.

Alternative investments are less liquid than JHHs' other investments. These instruments may contain elements of both credit and market risk. Such risks include, but are not limited to, limited liquidity, absence of oversight, dependence upon key individuals, emphasis on speculative investments, and nondisclosure of portfolio composition.

Investment income earned on cash balances (interest and dividends) is reported in the operating income section of the Statements of Operations and Changes in Net Assets under "Investment income." Realized gains or losses related to the sale of investments, other than temporary impairments, and unrealized gains or losses on alternative investments are included in the non-operating section of the Statement of Operations and Changes in Net Assets included in excess of revenues over expenses unless the income or loss is restricted by donor or law. Prior to April 1, 2011, unrealized gains or losses on investments other than alternative investments are excluded from excess of revenues over expenses.

On April 1, 2011, JHH changed the classification of certain investments to a trading portfolio from available for sale. Accordingly, cumulative unrealized gains of \$12.1 million were reclassified from unrestricted net assets to non-operating income included in the realized and unrealized gains (losses) on investments within the Statement of Operations and Changes in Net Assets. This change was made as management's intent with respect to the nature of the investment portfolios has changed.

Investments in companies in which JHH does not have control, but has the ability to exercise significant influence over operating and financial policies are accounted for using the equity method of accounting, and operating results flow through the investment income on the Statements of Operations and Changes in Net Assets. Dividends paid are recorded as a reduction of the carrying amount of the investment.

Investments in companies in which JHH does not have control, nor has the ability to exercise significant influence over operating and financial policies are accounted for using the cost method of accounting. Investments are originally recorded at cost, with dividends received being recorded as investment income.

**The Johns Hopkins Hospital**  
**Notes to the Financial Statements**  
**For the years ended June 30, 2012 and 2011**  
**(in thousands)**

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*Property, Plant and Equipment.* Property, plant and equipment acquisitions are recorded at cost. Equipment is recorded as an asset if the individual cost is at least \$5 thousand and the useful life is at least three years. Renovation projects of \$5 thousand or greater are capitalized in total even though individual components are less than the capital limit. The amount capitalized for equipment, buildings, and renovation projects financed by debt would include the interest costs incurred on borrowed funds, net of income earned, during the period of construction of capital assets and is capitalized as a component of the cost of acquiring those assets. Depreciation and amortization are determined by use of the straight-line method over an estimated useful life of the asset or the remaining life of the lease, whichever is shorter. Estimated useful lives assigned by JHH range from 5 to 25 years for land improvements, 3 to 40 years for buildings and improvements, 3 to 25 years for fixed and movable equipment, and 5 to 10 years for leasehold improvements. Maintenance and repair costs are expensed as incurred. When property, plant and equipment are retired, sold or otherwise disposed of, the asset's carrying amount and related accumulated depreciation are removed from the accounts and any gain or loss is included in operations.

The cost of software is capitalized provided the cost of the project is at least \$100 thousand and the expected life is at least two years. Costs include payment to vendors for the purchase of software and assistance in its installation, payroll costs of employees directly involved in the software installation, and the interest costs of the software project if financed by debt. Preliminary costs to document system requirements, vendor selection, and any costs before software purchase are expensed. Capitalization of costs will generally end when the project is completed and the software is ready to be used. Where implementation of the project is in phases, only those costs incurred which further the development of the project will be capitalized. Costs incurred to maintain the system are expensed.

Gifts of long-lived assets such as land, buildings or equipment are reported as unrestricted support, and are excluded from the excess of revenues over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expiration of donor restrictions are reported when the donated or acquired long-lived assets are placed into service.

*Impairment of Long-Lived Assets.* Long-lived assets are reviewed for impairment when events and circumstances indicate that the carrying amount of an asset may not be recoverable. JHH's policy is to record an impairment loss when it is determined that the carrying amount of the asset exceeds the sum of the expected undiscounted future cash flows resulting from use of the asset and its eventual disposition. Impairment losses are measured as the amount by which the carrying amount of the asset exceeds its fair value. Long-lived assets to be disposed of are reported at the lower of the carrying amount or fair value less cost to sell. There were no impairment charges for the years ended June 30, 2012 and 2011.

*Financing Expenses.* Financing expenses incurred in connection with the issuance by the Maryland Health and Higher Educational Facilities Authority ("MHHEFA") of long-term debt have been capitalized and are included in other assets in the Balance Sheet. Unamortized financing expenses were \$4.9 million and \$4.3 million at June 30, 2012 and 2011, respectively. These expenses are being amortized over the term of the related bond issues using the effective interest method. Amortization expense for the years ended June 30, 2012 and 2011 was \$.5 million and \$.2 million, respectively.

**The Johns Hopkins Hospital**  
**Notes to the Financial Statements**  
**For the years ended June 30, 2012 and 2011**  
**(in thousands)**

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*Accrued Vacation.* JHH records a liability for amounts due to employees for future absences which are attributable to services performed in the current and prior periods.

*Estimated Malpractice Costs.* The provision for estimated medical malpractice claims includes estimates of the ultimate gross costs for both reported claims and claims incurred but not reported. Additionally, an insurance recovery has been recorded representing the amount expected to be recovered from the self insured captive insurance company.

*Swap Agreements.* The value of the interest rate swap agreements entered into by JHH are adjusted to market value monthly at the close of each accounting period based upon quotations from market makers. The change in market value, if any, is recorded in the Statement of Operations and Changes in Net Assets. Entering into interest rate swap agreements involves, to varying degrees, elements of credit, default, prepayment, market and documentation risk in excess of the amounts recognized on the Balance Sheets. Such risks involve the possibility that there will be no liquid market for these agreements, the counterparty to these agreements may default on its obligation to perform and there may be unfavorable changes in interest rates.

*Asset Retirement Obligations.* The Financial Accounting Standards Board's ("FASB") guidance on accounting for asset retirement obligations provides for the recognition of an estimated liability for legal obligations associated with the retirement of tangible long-lived assets, including obligations that are conditional upon a future event. JHH measures asset retirement obligations at fair value when incurred and capitalizes a corresponding amount as part of the book value of the related long-lived assets. The increase in the capitalized cost is included in determining depreciation expense over the estimated useful life of these assets. Since the fair value of the asset retirement obligation is determined using a present value approach, accretion of the obligation due to the passage of time until its settlement is recognized each year as part of depreciation and amortization expense in JHH's Statements of Operations and Changes in Net Assets.

*Temporarily Restricted Net Assets.* Temporarily restricted net assets are those whose use has been limited by donors or law to a specific time period or purpose.

*Donor Restricted Gifts.* Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Unconditional promises to give cash to JHH greater than one year are discounted using a rate of return that a market participant would expect to receive at the date the pledge is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statements of Operations and Changes in Net Assets as net assets released from restrictions. Donor restricted contributions, whose restrictions are met within the same year as received, are reported as unrestricted contributions in the accompanying financial statements.

*Grants.* JHH receives various grants from individuals and agencies of Federal and State Governments for the purpose of furthering its mission of providing patient care. Grants are recognized as support and the related project costs are recorded as expenses when services related to grants are incurred. Grants receivable are included in due from others, and grant income is included in other revenue in the accompanying financial statements.

**The Johns Hopkins Hospital**  
**Notes to the Financial Statements**  
**For the years ended June 30, 2012 and 2011**  
**(in thousands)**

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*Excess of revenues over expenses.* The Statements of Operations and Changes in Net Assets include "Excess of revenues over expenses." Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include, among other items, changes in unrealized gains and losses on investments other than trading securities, changes in funded status of defined benefit plans, cumulative effect of changes in accounting principle, permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets).

*Non-operating services.* JHH has entered into an agreement effective July 1, 2011 to support capital improvements to the Johns Hopkins University School of Medicine's ("JHUSOM") infrastructure at the Johns Hopkins Hospital's East Baltimore campus through annual contributions. These contributions are recognized each year as non-operating services in JHH's Statements of Operations and Changes in Net Assets.

*Income Taxes.* JHH qualifies under Section 501(c)(3) of the Internal Revenue Code and is, therefore, not subject to tax under current income tax regulations.

FASB's guidance on accounting for uncertainty in income taxes clarifies the accounting for uncertainty of income tax positions. This guidance defines the threshold for recognizing tax return positions in the financial statements as "more likely than not" that the position is sustainable, based on its technical merits. This guidance also provides guidance on the measurement, classification and disclosure of tax return positions in the financial statements. There was no impact on JHH's financial statements during the years ended June 30, 2012 and 2011 resulting from this guidance.

*New Accounting Standards.* Effective July 1, 2011, JHH adopted the provisions of ASU 2010-06, "Improving Disclosures about Fair Value Measurements", which affects entities required to make disclosures about recurring and nonrecurring fair value measurements. This ASU requires that the Level 3 fair value roll forward activity be displayed gross, breaking out the purchases, issuances, sales and settlement activity. The adoption of this ASU did not have a significant impact on JHH's disclosures.

Effective July 1, 2011, JHH adopted the provisions of ASU 2010-23, "Measuring Charity Care for Disclosure", which states that direct and indirect cost be used as the measurement basis for charity care disclosure purposes and that the method used to determine such costs also be disclosed. The adoption of this ASU had no impact on JHH's financial condition, results of operations or cash flows.

Effective July 1, 2011, JHH adopted the provisions of ASU 2010-24, "Presentation of Insurance Claims and Related Insurance Recoveries", which clarifies that health care entities should not net insurance recoveries against the related claims liabilities.

**The Johns Hopkins Hospital**  
**Notes to the Financial Statements**  
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**(in thousands)**

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In connection with JHH's adoption of ASU 2010-24, JHH recorded an increase in its assets and liabilities in the accompanying consolidated Balance Sheet as of June 30, 2012 as follows:

Caption on Balance Sheet	<u>2012</u>
Prepaid expense and other current assets	\$ 20,670
Other assets	<u>26,095</u>
Total assets	<u>\$ 46,765</u>
Current portion of estimated malpractice costs	\$ 20,670
Estimated malpractice costs, net of current portion	<u>26,095</u>
Total liabilities	<u>\$ 46,765</u>

The assets and liabilities represent JHH's estimated self-insured captive insurance recoveries for claims reserves and certain claims in excess of self-insured retention levels. The insurance recoveries and liabilities have been allocated between short-term and long-term assets and liabilities based upon the expected timing of the claims payments. The adoption had no impact on JHH's results of operations or cash flows.

**2. Net Patient Service Revenue**

JHH has agreements with third-party payors that provide for payments to JHH at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Adjustments mandated by the Health Services Cost Review Commission are also included in contractual adjustments, a portion of which are also included in established rates.

JHH has a policy of providing care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Such patients are identified based on information obtained from the patient and subsequent analysis. Because JHH does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Direct and indirect costs for these services amounted to \$29.2 million and \$26.6 million for the years ended June 30, 2012 and 2011, respectively. The costs of providing charity care services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on JHH's total expenses (less bad debt expense) divided by gross patient service revenue.

**The Johns Hopkins Hospital**  
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**(in thousands)**

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Patient accounts receivable as of June 30 consisted of the following:

	<u>2012</u>	<u>2011</u>
Medicare program	19 %	17 %
Blue Cross and Blue Shield of Maryland	17 %	19 %
Health Maintenance Organizations	17 %	16 %
Commercial	15 %	15 %
Medicaid program	10 %	13 %
Medicaid Managed Care Organizations	9 %	9 %
Other self-pay and third party-payers	13 %	13 %

**3. Pledges Receivable**

As of June 30, 2012 and 2011, the total value of pledges receivable was \$15.7 million and \$26.7 million, before discounts. These amounts have been discounted at rates ranging from 1.38% to 6.0% and consist of the following (in thousands):

	<u>2012</u>			
	<u>1 Year</u>	<u>2 –5 Years</u>	<u>5 Years or Greater</u>	<u>Totals</u>
Future campus development	\$ 7,897	\$ 7,138	\$ 44	\$ 15,079

  

	<u>2011</u>			
	<u>1 Year</u>	<u>2 –5 Years</u>	<u>5 Years or Greater</u>	<u>Totals</u>
Future campus development	\$ 16,153	\$ 9,263	\$ 198	\$ 25,614

Pledges are deemed to be fully collectable and therefore, no reserve is recorded.

**4. Fair Value Measurements**

FASB's guidance on the fair value option for financial assets and financial liabilities permits companies to choose to measure many financial assets and liabilities, and certain other items at fair value. This guidance requires a company to record unrealized gains and losses on items for which the fair value option has been elected in excess of revenues over expenses. The fair value option may be applied on an instrument by instrument basis. Once elected, the fair value option is irrevocable for that instrument. The fair value option can be applied only to entire instruments and not to portions thereof. JHH did not elect fair value accounting for any asset or liability that was not currently required to be measured at fair value.

**The Johns Hopkins Hospital**  
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**(in thousands)**

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JHH follows the guidance on fair value measurements, which 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, establishes a framework for measuring fair value, and expands disclosures about such fair value measurements. This guidance applies to other accounting pronouncements that require or permit fair value measurements and, accordingly, this guidance does not require any new fair value measurements. Adopting this guidance did not have a material impact on JHHs' financial position and results of operations.

This guidance discusses valuation techniques such as the market approach, cost approach and income approach. This guidance establishes a three-tier level hierarchy for fair value measurements based upon the transparency of inputs used to value an asset or liability as of the measurement date. The three-tier hierarchy prioritizes the inputs used in measuring fair value as follows:

- Level 1 – Observable inputs such as quoted market prices for identical assets or liabilities in active markets;
- Level 2 – Observable inputs for similar assets or liabilities in an active market, or other than quoted prices in an active market that are observable either directly or indirectly; and
- Level 3 – Unobservable inputs in which there is little or no market data that require the reporting entity to develop its own assumptions. There were no financial instruments requiring level 3 classification at June 30, 2012 or June 30, 2011.

The financial instrument's categorization within the hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Each of the financial instruments below have been valued utilizing the market approach.

The following table presents the financial instruments carried at fair value as of June 30, 2012 grouped by hierarchy level (in thousands):

<u>Assets</u>	<u>Total Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>
Cash equivalents (1)	\$ 28,457	\$ -	\$ 28,457
U.S. treasury notes (2)	56,392	-	56,392
Corporate bonds (2)	88,946	-	88,946
Asset backed securities (2)	39,604	-	39,604
Equities and equity funds (3)	136,881	-	136,881
Fixed Income Funds (4)	44,967	-	44,967
Totals	<u>\$ 395,247</u>	<u>\$ -</u>	<u>\$ 395,247</u>
<u>Liabilities</u>			
Interest rate swap agreements (5)	<u>\$ 206,703</u>	<u>\$ -</u>	<u>\$ 206,703</u>

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The following table presents the financial instruments carried at fair value as of June 30, 2011 grouped by hierarchy level (in thousands):

<u>Assets</u>	<u>Total Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>
Cash equivalents (1)	\$ 124,831	\$ -	\$ 124,831
U.S. treasury notes (2)	123,515	-	123,515
Corporate bonds (2)	182,775	-	182,775
Asset backed securities (2)	141,164	-	141,164
Equities and equity funds (3)	128,516	-	128,516
Fixed Income Funds (4)	39,507	-	39,507
Totals	<u>\$ 740,308</u>	<u>\$ -</u>	<u>\$ 740,308</u>
<u>Liabilities</u>			
Interest rate swap agreements (5)	<u>\$ 99,095</u>	<u>\$ -</u>	<u>\$ 99,095</u>

- (1) Cash equivalents include investments with original maturities of three months or less, including certificates of deposit, commercial paper, money-market funds and overnight investments. Certificates of deposit and commercial paper are carried at amortized cost, which approximates fair value which renders them level 2. Money-market funds are valued based on the net asset value and are classified as level 2.
- (2) For investments in U.S. Treasuries (notes, bonds, and bills), corporate bonds, and asset backed securities, fair value is based on the average of the last reported bid and ask price; therefore these investments are rendered level 2. These investments fluctuate in value based upon changes in interest rates. Until April 1, 2011, significant changes in the credit quality of the underlying entity were analyzed and any other than temporary impairments was recorded upon that determination, if any.
- (3) Equities include individual equities and investments in mutual funds, commingled trusts and hedge funds. The ability to liquidate these funds is not limited except for the small percentage of each securities lending fund that is on loan. The commingled trusts and hedge funds are valued regularly within each month utilizing NAV per unit and are rendered level 2.
- (4) Fixed income funds are investments in mutual funds and commingled trusts investing in fixed income instruments. The underlying fixed investments are principally U.S. Treasuries, corporate bonds, commercial paper, and mortgage backed securities. The commingled trusts are valued regularly within each month utilizing NAV per unit and are rendered level 2.
- (5) The interest rate swap agreements are valued using a pricing service at net present value. These evaluated prices render these instruments level 2. The volatility in the fair value of the swap agreements change as long-term interest rates change. See footnote 8.

During 2012 and 2011, there were no transfers between level 1 and 2.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair value. Furthermore, while JHH believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value as of the reporting date.

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The estimated total fair value of long-term debt based on quoted market prices for the same or similar issues, was \$901.2 million and \$785.4 million as of June 30, 2012 and 2011, respectively.

JHH holds alternative investments which are accounted for on the equity method of accounting which approximates fair value, that are not traded on national exchanges or over-the counter markets. JHH is provided a net asset value per share for these alternative investments that has been calculated in accordance investment company rules, which among other requirements, indicates that the underlying investments be measured at fair value. There are no unfunded commitments related to JHH's alternative investments.

The following table displays information by major alternative investment category as of June 30, 2012:

<b>Description</b>	<b>Market Value</b>	<b>Liquidity</b>	<b>Notice Period</b>	<b>Receipt of Proceeds</b>
Global asset allocation	\$ 71,847	Monthly	5 days	(1)
Fund of funds	40,367	Monthly, quarterly or terminated	25 - 70 days	(2)
Hedge funds	3,552	Quarterly	60 days	(3)

- (1) At least 95% within 15 days, remaining within 30 days of redemption date  
(2) At least 90% within 60 days, remaining received after the audit or as SPV shares  
(3) 95% within 30 days, 5% within 120 days

The following table displays information by major alternative investment category as of June 30, 2011:

<b>Description</b>	<b>Market Value</b>	<b>Liquidity</b>	<b>Notice Period</b>	<b>Receipt of Proceeds</b>
Global asset allocation	\$ 55,050	Monthly	5 - 14 days	(1)
Fund of funds	29,000	Monthly, quarterly or terminated	30 - 60 days	(2)
Hedge funds	3,275	Quarterly	60 days	(3)

- (1) Within 15 days, or 95% within 1 business days of the redemption date; 5% after the 12<sup>th</sup> business day of the month  
(2) Within 5 days, or 95% in 1 - 30 days, 5% within 60 days or after annual audit  
(3) 95% within 30 days of redemption date; 5% within 120 days of redemption date

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Financial instruments are reflected in the Combined Balance Sheets as of June 30, 2012 and 2011 as follows (in thousands):

	<u>2012</u>	<u>2011</u>
Cash equivalents measured at fair value	\$ 25,804	\$ 119,491
Cash	15,270	33,897
Total cash and cash equivalents	<u>\$ 41,074</u>	<u>\$ 153,388</u>
Short and long-term investments measured at fair value	\$ 300,180	\$ 554,336
Investments accounted for under equity/cost method	168,359	121,897
Total short and long-term investments	<u>\$ 468,539</u>	<u>\$ 676,233</u>
Assets whose use is limited measured at fair value	\$ 69,262	\$ 66,482
Pledges receivable	15,079	25,613
Beneficial interest remainder trust	584	7,457
Deposit with bond trustees	14,037	11,255
Total assets whose use is limited	<u>\$ 98,962</u>	<u>\$ 110,807</u>

**5. Investments and Assets Whose Use is Limited**

Investments (short and long-term) are pooled together with other JHHS affiliates and consisted of the following as of June 30 (in thousands):

	<u>2012</u>	<u>2011</u>
	<u>Carrying</u>	<u>Carrying</u>
	<u>Amount</u>	<u>Amount</u>
U.S. treasury notes	\$ 35,801	\$ 105,722
Corporate bonds	57,183	156,643
Asset backed securities	25,349	123,948
Equities and equity funds	136,881	128,516
Fixed Income funds	44,967	39,507
Alternative investments	115,766	87,325
Other equity/cost investments	52,592	34,572
	<u>\$ 468,539</u>	<u>\$ 676,233</u>

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Assets whose use is limited as of June 30 consisted of the following (in thousands):

	<u>2012</u>	<u>2011</u>
	<u>Carrying</u>	<u>Carrying</u>
	<u>Amount</u>	<u>Amount</u>
Cash and cash equivalents	\$ 16,691	\$ 16,595
U.S. treasury notes	20,590	17,793
Asset backed securities	14,256	17,217
Corporate bonds	31,762	26,132
Beneficial interest remainder trust	584	7,457
Pledges receivable	<u>15,079</u>	<u>25,613</u>
	<u>\$ 98,962</u>	<u>\$ 110,807</u>

Included in assets whose use is limited as of June 30, 2012 and 2011 are \$62.5 million and \$60.9 million, respectively, of investments pooled together with other JHHS affiliates.

Realized and unrealized losses on investments for the years ended June 30, included in non-operating revenues and expenses section of the Statement of Operations consisted of the following (in thousands):

	<u>2012</u>	<u>2011</u>
Realized gains on investments	\$ 2,282	\$ 4,528
Unrealized (losses) gains on investments	<u>(7,751)</u>	<u>22,521</u>
Total	<u>\$ (5,469)</u>	<u>\$ 27,049</u>

Investments recorded under the cost or equity method as of June 30 consisted of the following (in thousands):

<u>Entity</u>	<u>Cost/Equity</u>	<u>%</u>	<u>2012</u>	<u>2011</u>
JHMI Utilities, LLC	Equity	50.0 %	\$ 5,666	\$ 3,862
MCIC Bermuda	Cost	10.0 %	45,381	29,635
MCIC Vermont	Cost	16.0 %	1,000	1,000
Other	Cost		<u>545</u>	<u>75</u>
			<u>\$ 52,592</u>	<u>\$ 34,572</u>

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**6. Property, Plant and Equipment**

Property, plant and equipment and accumulated depreciation and amortization consisted of the following as of June 30 (in thousands):

	2012		2011	
	Cost	Accumulated Depreciation	Cost	Accumulated Depreciation
Land and land improvements	\$ 29,277	\$ 4,206	\$ 14,421	\$ 3,884
Buildings and improvements	974,926	247,454	432,866	213,500
Fixed and moveable equipment	992,797	273,969	451,093	279,212
Construction in-progress	21,667	-	905,607	-
Capitalized software	54,197	26,419	46,562	17,764
	\$ 2,072,864	\$ 552,048	\$ 1,850,549	\$ 514,360

Accruals for purchases of property, plant and equipment at June 30, 2012 and 2011 amounted to \$33.9 million and \$49.6 million, respectively, and are included in accounts payable and accrued liabilities in the Balance Sheet. Depreciation expense for the years ended June 30, 2012 and 2011 amounted to \$84.4 and \$69.1 million, respectively. Amortization expense for the years ended June 30, 2012 and 2011 amounted to \$484 and \$200 thousand, respectively.

JHH and The Johns Hopkins University (“JHU”) share various facilities, equipment and services. The costs related to these facilities, equipment and services are generally paid for in their entirety by one institution. Under the provisions of a Joint Administrative Agreement and a lease agreement between JHH and JHU, these costs are allocated to both institutions on the basis of usage. JHU leases approximately 20% and 26.6% of the net square footage within JHH’s buildings at June 30, 2012 and 2011, respectively. During the years ended June 30, 2012 and 2011, JHH retired long-lived, fully depreciated assets determined to have no future value. The original cost and corresponding accumulated depreciation of these long-lived assets was \$46.7 million and \$85.3 million in 2012 and 2011, respectively. No proceeds from retirement were received.

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**7. Debt**

Debt as of June 30 is summarized as follows (in thousands):

	2012		2011	
	Current Portion	Long-Term Portion	Current Portion	Long-Term Portion
MHHEFA bonds and notes:				
1990 Series--Revenue Bonds	\$ 9,370	\$ 49,589	\$ 9,370	\$ 54,850
2001 Series--Revenue Bonds - net of original issue discount of \$790 as of June 30, 2011	-	-	2,755	78,514
2004 - Commercial Paper Series A	-	-	54,625	-
2004 - Commercial Paper Series C	60,000	-	10,000	50,000
2007 - Commercial Paper Series D	40,000	-	-	40,000
2008 - Commercial Paper Series E	325	83,775	-	84,100
2008 - Commercial Paper Series F	400	84,150	-	84,550
2008 Series Revenue Bonds – including premium of \$2,108 and \$4,806 as of June 30, 2012 and 2011, respectively	48,250	50,353	48,245	101,301
2010 Series Revenue Bonds - including net original issue premium of \$1,679 and \$1,742 at June 30, 2012 and 2011, respectively.	-	149,874	-	149,937
2011 Series A Revenue Bonds - including premium of \$7,083 as of June 30, 2012	2,260	79,438	-	-
2011 Series B Revenue Bonds	-	48,245	-	-
2012 Series A Note	1,320	52,190	-	-
2012 Series B Revenue Bonds - including premium of \$13,724 at June 30, 2012	700	110,584	-	-
	<u>\$ 162,625</u>	<u>\$ 708,198</u>	<u>\$ 124,995</u>	<u>\$ 643,252</u>

**Obligated Group**

The Johns Hopkins Health System's Obligated Group ("JHHS Obligated Group") consists of JHH, Johns Hopkins Bayview Medical Center, Inc., ("JHBMC"), Suburban Hospital Healthcare System, Inc. ("SHHS"), Suburban Hospital, Inc. ("SHI") and Howard County General Hospital ("HCGH"). JHBMC was admitted into the JHHS Obligated Group in 2004 as part of a plan of debt refinancing. SHHS and SHI were admitted into the JHHS Obligated Group in 2010 as part of the JHH 2010 Series Revenue Bonds issuance and HCGH was admitted into the JHHS Obligated Group in 2012 as part of the JHH 2012 Series B Revenue Bond issuance. All debt of these entities are parity debt, and as such are collateralized equally and ratably by a claim on and a security interest in all of JHH's, JHBMC's, SHI's, SHHS' and HCGH's receipts as defined in the Master Loan Agreement with MHHEFA. JHH, JHBMC, SHI, SHHS and HCGH are required to achieve a defined minimum debt service coverage ratio each year, maintain adequate insurance coverage and comply with certain restrictions on their ability to incur additional debt. As of

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June 30, 2012 and 2011 all parties are in compliance with these requirements. As of June 30, 2012 the outstanding JHH, JHBMC, SHI, SHHS and HCGH parity debt was \$1.1 billion. As of June 30, 2011, the outstanding JHH, JHBMC, SHI and SHHS parity debt was \$946.0 million.

#### **1990 Series - Revenue Bonds**

Portions of the Series 1990 Revenue Bonds have been advance refunded by the 1993 Series - Refunding Revenue Bonds.

The bonds outstanding consist of Capital Appreciation Bonds. Interest on the Capital Appreciation Bonds accrues from the date of delivery, is compounded semi-annually on each July 1, and January 1, and is to be paid at maturity or redemption. Serial Capital Appreciation Bonds of \$33.7 million and \$40.8 million as of June 30, 2012 and 2011, respectively, bearing interest at rates ranging from 7.30% to 7.35% per annum, are due each July 1 in the amount of \$9.4 million from 2010 to 2015. Term Capital Appreciation Bonds of \$25.2 million and \$23.4 million as of June 30, 2012 and 2011, respectively, are due July 1, 2019 and bear interest, compounded semi-annually at a rate of 7.4%. Annual sinking fund installments for the Term Capital Appreciation Bonds in the amount of \$9.4 million are due on July 1, 2016 through 2019.

#### **2001 Series - Revenue Bonds**

The outstanding 2001 bonds consisted of Serial Bonds of \$14.6 million and Term Bonds of \$67.5 million as of June 30, 2011. The Serial Bonds bore interest at rates ranging from 4.06% to 5.00% and the Term Bonds paid interest semi-annually at a rate of 5.0%. In November 2011 these bonds were refinanced through the issuance of the 2011 Series A Revenue Bonds described below.

#### **2004 Commercial Paper Revenue Notes – Series A**

The Series A Notes paid interest as the notes matured at a variable rate based on the commercial paper sold by a designated re-marketing agent for terms ranging from 1 to 270 days. The rates for the years ended June 30, 2012 and 2011 were approximately 0.17% and 0.31%, respectively. In February 2012 this commercial paper was refinanced through the issuance of the 2012 Series A Note described below.

#### **2004 Commercial Paper Revenue Notes – Series C**

The Series C Notes pay interest as the notes mature at a variable rate based on the commercial paper sold by a designated re-marketing agent for terms ranging from 1 to 270 days. The rates for the years ended June 30, 2012 and 2011 were approximately .37% and 0.46%, respectively.

In connection with the 2004 Commercial Paper Revenue Series C, JHH entered into a \$60.0 million line of credit agreement dated March 1, 2004 with Suntrust Bank to provide for payment of such commercial paper at maturity subject to certain conditions described therein. This agreement expires on November 1, 2012 subject to extension or earlier termination. In connection with the expiration of this line of credit, JHH plans to refinance this commercial paper series through a variable interest rate debt issuance. Accordingly, \$60.0 million of commercial paper notes have been reclassified as short-term in the balance sheet.

Amounts advanced under the line of credit agreement bear interest at a variable rate based upon the higher of the prime rate and the Federal funds rate plus 0.50% for the first 60 days outstanding and the higher of these two rates plus 2.00% thereafter. The advances are

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repayable on the earliest date that is 360 days from the date of such advance, the date of termination, the date of receipts by JHH of proceeds of any subsequent issuances of notes or the final date. No amounts were outstanding as of June 30, 2012 or 2011. Since this liquidity facility must be repaid within 360 days, \$10.0 million of commercial paper notes that were scheduled for remarketing during the period July 1 through July 6, 2011 were reclassified as short-term in the June 30, 2011 balance sheet. This commercial paper was successfully remarketed subsequent to June 30, 2011.

On July 1, 2011, JHH made \$10.0 million of aggregate principal payments on the notes. In connection with the payment of these maturities, JHH issued an additional \$10.0 million of commercial paper notes to replace the matured notes. The additional notes are subject to the same terms and conditions as the original notes except for the inclusion of the additional maturities.

**2007 Commercial Paper Revenue Notes – Series D**

The Series D Notes pay interest monthly at a variable rate based on the commercial paper sold by a designated re-marketing agent for terms ranging from 1 to 270 days. The rates for the years ended June 30, 2012 and 2011 were approximately .33% and 0.43%, respectively.

In connection with the 2007 Commercial Paper Revenue Series D, JHH entered into a \$40.0 million line of credit agreement dated November 1, 2007 with Suntrust Bank to provide for payment of such commercial paper at maturity subject to certain conditions described therein. This agreement expires on November 1, 2012 subject to extension or earlier termination. In connection with the expiration of this line of credit, JHH plans to refinance this commercial paper series through a variable interest rate debt issuance. Accordingly, \$40.0 million of commercial paper notes have been reclassified as short-term in the balance sheet.

Amounts advanced under the line of credit agreement bear interest at a variable rate based upon the higher of the prime rate and the Federal funds rate plus 0.50% for the first 60 days outstanding and the higher of these two rates plus 2.00% thereafter. The advances are repayable on the earliest date that is 360 days from the date of such advance, the date of termination, the date of receipts by JHH of proceeds of any subsequent issuances of notes or the final date. No amounts were outstanding as of June 30, 2012. There were no commercial paper notes that were required to be reclassified as short-term in the June 30, 2011 balance sheet.

**2008 Commercial Paper Revenue Notes - Series E and Series F**

In April 2008 JHH issued \$84.1 million and \$84.6 million 2008 Commercial Paper Revenue Notes Series E and Series F, respectively. Notes are due May 15, 2038 and pay interest as they mature at a variable rate based on the commercial paper sold by a designated remarketing agent for terms ranging from 1 to 270 days. The interest rates for the years ended June 30, 2012 and 2011 were approximately .21% and 0.28% for the Series E notes and 0.21% and 0.29% for the Series F notes, respectively.

In connection with the 2008 Commercial Paper Revenue Notes Series E and Series F, JHH entered into a \$170.5 million letter of credit agreement dated April 1, 2008 with Bank of America, N.A. equal to the principal amount of the Notes plus thirty-four days of interest at the maximum rate of 12.0%. This agreement was extended on June 30, 2010 to expire on June 30, 2015.

Amounts advanced under the line of credit agreements bear interest at the prime rate for the first 90 days outstanding and the prime rate plus 1.00% thereafter. The advances are repayable on

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the earliest date that is 366 days from the date of the advance or the date of receipt by JHH of proceeds of subsequent issuances of notes in excess of the principal of notes maturing or the expiration date. No amounts were outstanding as of June 30, 2012 or 2011.

**2008 Series Revenue Bonds**

In June 2008 JHH issued \$144.7 million of Revenue Bonds to finance construction of two new clinical care buildings. The bonds are term bonds that were sold in three tranches of approximately \$48.2 million each that have final maturities in 2042, 2046 and 2048. The payment terms require sinking fund deposits in 2036 through 2048 in amounts ranging from \$2.3 million to \$20.2 million. The interest rates on the bonds are based on initial term rate periods of three, five and seven years and currently range between 3.65% and 5.0%. Interest is payable semi-annually.

At the end of the initial term rate periods on November 15, 2011, May 15, 2013 and May 15, 2015 \$48.2 million of the bonds are subject to mandatory purchase by JHH. Accordingly, \$48.2 million of debt has been reclassified to current in the June 30, 2012 and 2011 balance sheets. The first tranche of term bonds was purchased by JHH on November 14, 2011 through the issuance of the 2011 Series B Revenue Bonds (see below). JHH plans to refinance the second tranche of term bonds through a tax-exempt floating rate note issuance. JHH has the option at the end of each term period to change the length of the term periods or extend the fixed rate period to the final maturity of the bonds. JHH also has the right to retire the bonds at par value at the end of each term period. The bonds were sold at a premium of \$5.3 million which is being accounted for using the bond outstanding method.

**2010 Series Revenue Bonds**

In June 2010 JHH issued \$148.2 million of Revenue Bonds to further finance construction of the two new clinical buildings. \$29.8 million of the bonds are serial bonds that mature in 2031 through 2035 and pay interest semi-annually at rates ranging from 4.38% to 4.63%. The remaining 2010 Bonds are Term Bonds amounting to \$118.4 million paying interest semi-annually at a rate of 5.0% and maturing in 2040. The payment terms for the Term Bonds require sinking fund deposits in 2036 through 2040 in amounts ranging from \$21.0 million to \$26.3 million. The Serial Bonds were sold at a discount of \$.5 million and the Term Bonds were sold at a premium of \$2.3 million both of which are being accounted for using the bond outstanding method.

**2011 Series A Revenue Bonds**

In November 2011, JHH issued \$74.6 million of Revenue Bonds to refinance the existing JHH 2001 Series Revenue Bonds. The 2011 Series A Bonds are serial bonds with maturities from 2013 through 2026 and pay a fixed rate of interest ranging from 2.00% to 5.00%. The repayment terms require semi-annual interest payments on May 15<sup>th</sup> and November 15<sup>th</sup>. Principal payments range from \$100 thousand to \$13.5 million, and are due upon maturity, beginning May 15, 2013. The bonds were sold at a premium of \$7.6 million.

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**2011 Series B Revenue Bonds**

In November 2011, JHH issued \$48.2 million of Revenue Bonds to refinance a portion of its existing 2008 Series Revenue Bonds (see above). The 2011 Series B Revenue Bonds are variable rate bonds that were issued with a five year term, and a mandatory purchase date of November 15, 2016. The 2011 Bonds pay interest monthly based on 67% of LIBOR plus 1.15%. The LIBOR rate is reset on the first business day of each month. The interest rates for the year ended June 30, 2012 were approximately 1.32%.

**2012 Series A Note**

In February 2012, JHH issued a \$53.5 million Floating Rate Note in a private placement to refinance its Series 2004 A Commercial Paper that had a balance of \$53.5 million. The 2012 Series A Note has a term of five years, carries a variable rate of interest at 67% of the one-month LIBOR rate plus a spread of .44% that resets and is payable monthly. The interest rates for the year ended June 30, 2012 were approximately 0.60%.

**2012 Series B Revenue Bonds**

In May 2012, JHH issued \$97.6 million of Revenue Bonds to further finance the construction of its two new clinical buildings. The Bonds are serial bonds and mature annually from 2012 through 2033 in installments that range from \$700 thousand in 2012 to \$7.1 million in 2033, and pay interest semi-annually at rates ranging from 2.00% to 5.00%. The 2012 Series B Revenue Bonds were sold at a premium of \$13.9 million.

Total maturities of debt and sinking fund requirements during the next five fiscal years and thereafter are as follows as of June 30, 2012 (in thousands):

2013	\$	162,625
2014		16,860
2015		65,340
2016		14,225
2017		55,075
Thereafter		<u>532,104</u>
	\$	<u>846,229</u>

Interest costs incurred, paid and capitalized in the years ended June 30 are as follows (in thousands):

	<u>2012</u>	<u>2011</u>
Net interest costs:		
Capitalized	\$ 15,095	\$ 16,507
Charged to operations	<u>27,464</u>	<u>28,939</u>
	<u>\$ 42,559</u>	<u>\$ 45,446</u>
Interest costs paid	<u>\$ 38,891</u>	<u>\$ 39,172</u>

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**8. Derivative Financial Instruments**

JHH's primary objective for holding derivative financial instruments is to manage interest rate risk. Derivative financial instruments are recorded at fair value and are included in other long-term liabilities. The total notional amount of interest rate swap agreements was \$522.2 million and \$523.3 million as of June 30, 2012 and 2011, respectively.

JHH follows accounting guidance on derivative financial instruments that is based on whether the derivative instrument meets the criteria for designation as cash flow or fair value hedges. The criteria for designating a derivative as a hedge include the assessment of the instrument's effectiveness in risk reduction, matching of the derivative instrument to its underlying transaction, and the assessment of the probability that the underlying transaction will occur. All of JHH's derivative financial instruments are interest rate swap agreements without hedge accounting designation.

The value of interest rate swap agreements entered into by JHH are adjusted to market value monthly at the close of each accounting period based upon quotations from market makers. Entering into interest rate swap agreements involves, to varying degrees, elements of credit, default, prepayment, market and documentation risk in excess of the amounts recognized on the Balance Sheets. Such risks involve the possibility that there will be no liquid market for these agreements, the counterparty to these agreements may default on its obligation to perform and there may be unfavorable changes in interest rates. JHH does not hold derivative instruments for the purpose of managing credit risk and limits the amount of credit exposure to any one counterparty and enters into derivative transactions with high quality counterparties. JHH recognizes gains and losses from changes in fair values of interest rate swap agreements as a non-operating revenue or expense within excess of revenues over expenses in the Statement of Operations and Changes in Net Assets.

Each swap agreement has certain collateral thresholds whereby, on a daily basis, if the market value of the swap agreement declines such that its devaluation exceeds the threshold, cash must be deposited by JHHS with the swap counterparty for the difference between the threshold amount and the market value. At June 30, 2012 and 2011, the amount of required collateral was \$140.5 million and \$54.4 million, respectively. JHH has funded the collateral payments to JHHS. JHHS makes the deposits to the counterparty. JHH has included the collateral funding in the balance of due from affiliates, net of current portion in the balance sheet.

Fair value of derivative instruments as of June 30 (in thousands):

<b>Derivatives Reported as Liabilities</b>				
<b>2012</b>		<b>2011</b>		
<b>Balance Sheet Caption</b>	<b>Fair Value</b>	<b>Balance Sheet Caption</b>	<b>Fair Value</b>	
Interest rate swaps not designated as hedging instruments	Other long-term liabilities	Other long-term liabilities	\$	(99,095)
	<u>\$ (206,703)</u>		<u>\$</u>	<u>(99,095)</u>

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Derivatives not designated as hedging instruments as of June 30 (in thousands):

Classification of Derivative Loss in Statement of Operations	<b>Amount of Loss Recognized in Change in Unrestricted Net Assets</b>	
	<b>2012</b>	<b>2011</b>
Interest rate swaps:		
Change in market value of swap agreements	<u>\$ (107,608)</u>	<u>\$ 24,207</u>

The following is a description of JHH's interest rate swap agreements:

In 2004 JHH entered into a fixed payor interest swap agreement with J.P. Morgan. The notional amount on this swap agreement is \$53.5 million and \$54.6 million as of June 30, 2012 and 2011, respectively. JHH pays J.P. Morgan a fixed annual rate of 3.329% on the outstanding loan value of the 2004 Series A Notes in return for the receipt of a floating rate of interest equal to 67% of the one Month LIBOR rate. Monthly payments began on February 1, 2004. This swap agreement has a maturity date of July 1, 2023. The floating rates as of June 30, 2012 and 2011 were 0.16% and 0.13%, respectively.

In April 2006, JHH entered into two forward start fixed payor swap agreements with Goldman Sachs Capital Markets, L.P. ("GSCM"). The notional amount on these swap agreements is \$150 million each. Payments under the first of these swap agreements began June 1, 2007 and payments under the second agreement began June 1, 2008. These agreements carry a term of 32 years. JHH pays GSCM a fixed annual rate of 3.911% on the notional value of the swap agreement in return for the receipt of a floating rate of interest equal to 67% of the one-month LIBOR rate. Under the second swap agreement JHH pays GSCM a fixed annual rate of 3.922% on the \$150.0 million notional value in return for the receipt of a floating rate of interest equal to 67% of the one month LIBOR rate. The floating rates as of June 30, 2012 and 2011 were 0.16% and 0.13%, respectively.

In July 2007, JHH entered into two additional fixed payor interest rate swap agreements. One was with GSCM in a notional amount of \$84.1 million and another was with Merrill Lynch Capital Services ("MLCS") in a notional amount of \$84.6 million. JHH will pay GSCM a fixed annual rate of 3.819% and will pay MLCS a fixed annual rate of 3.8091% on the outstanding loan values in return for the receipt of a floating rate of interest equal to 67% of the one-month LIBOR rate. Monthly payments began on November 15, 2007 for both swap agreements. Both swap agreements have a maturity date of May 15, 2038. The floating rates as of June 30, 2012 and 2011 were 0.16% and 0.13%, respectively.

**9. Temporarily Restricted Net Assets**

Temporarily restricted net assets were available for the following purposes as of June 30 (in thousands):

	<b>2012</b>	<b>2011</b>
Purchase of property, plant and equipment	\$ 17,723	\$ 459,845
Patient care	992	1,164
Education and counseling	545	519
	<u>\$ 19,260</u>	<u>\$ 461,528</u>

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**10. Pension Plans**

JHH has two defined benefit pension plans (the "Plans") covering substantially all of its employees. The plan for employees not represented by a collective bargaining unit is part of a multi-employer plan. Employees represented by Local 1999-E are covered by a noncontributory pension plan which provides for retirement income benefits based on years of service and compensation.

Employees not represented by a collective bargaining agreement are covered by a contributory pension plan which provides for retirement income based on years of service, the level of contributions and the employees' compensation. Effective July 1, 1992, the option for an employee to contribute to the pension plan was discontinued. The funding policy for both plans is to make sufficient contributions to meet the Internal Revenue Service minimum funding requirements. The assets of both plans as of June 30, 2012 and 2011 consisted of cash and cash equivalents, listed stocks, corporate bonds, government securities and alternative investments. All assets are managed by external investment managers, consistent with the plan's investment policy.

The change in benefit obligation, plan assets, and funded status of the pension plans are shown below (in thousands):

	<u>2012</u>	<u>2011</u>
<u>Change in benefit obligation</u>		
Benefit obligation as of beginning of year	\$ 669,494	\$ 614,623
Service cost	24,564	22,525
Interest cost	39,741	36,562
Actuarial loss	174,617	13,171
Benefits paid	<u>(18,396)</u>	<u>(17,387)</u>
Benefit obligation as of June 30	<u>\$ 890,020</u>	<u>\$ 669,494</u>
<u>Change in plan assets</u>		
Fair value of plan assets as of beginning of year	\$ 538,102	\$ 442,412
Actual return on plan assets	4,355	79,839
Employer contribution	75,176	33,238
Benefits paid	<u>(18,396)</u>	<u>(17,387)</u>
Fair value of plan assets as of June 30	<u>\$ 599,237</u>	<u>\$ 538,102</u>
<u>Funded Status as of June 30.</u>		
Fair value of plan assets	\$ 599,237	\$ 538,102
Projected benefit obligation	<u>(890,020)</u>	<u>(669,494)</u>
Funded status	<u>\$ (290,783)</u>	<u>\$ (131,392)</u>

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Amounts recognized in the Balance Sheets consist of (in thousands):

	<u>2012</u>	<u>2011</u>
Net pension asset	\$ -	\$ 1,878
Net pension liability	<u>(290,783)</u>	<u>(133,270)</u>
Net amount recognized	<u>\$ (290,783)</u>	<u>\$ (131,392)</u>

Amounts not yet recognized in net periodic benefit cost and included in unrestricted net assets consist of (in thousands):

	<u>2012</u>	<u>2011</u>
Actuarial net loss	\$ 443,318	\$ 253,622
Prior service cost	<u>2,053</u>	<u>3,308</u>
	<u>\$ 445,371</u>	<u>\$ 256,930</u>
Accumulated benefit obligation	<u>\$ 777,542</u>	<u>\$ 579,016</u>

**Net Periodic Cost**

Components of net periodic pension cost (in thousands):

	<u>2012</u>	<u>2011</u>
Service cost	\$ 24,564	\$ 22,525
Interest cost	39,741	36,562
Expected return on plan assets	(44,967)	(41,261)
Amortization of prior service cost	1,255	1,261
Recognized net actuarial loss	<u>25,532</u>	<u>22,572</u>
Net periodic pension benefit cost	<u>\$ 46,125</u>	<u>\$ 41,659</u>

The actuarial net loss and prior service cost for the defined benefit plans that will be amortized from unrestricted net assets into net periodic benefit costs in 2013 are \$38.7 million and \$1.1 million, respectively.

The assumptions used in determining the net periodic pension cost for the plans are as follows for the years ended June 30:

	<u>2012</u>	<u>2011</u>
Discount rate	6.03%	6.04%
Expected return on plan assets	8.25%	8.25%
Rate of compensation increase	2.50% - 3.00%	2.00% - 3.00%

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The assumptions used in determining the projected pension obligations for the plans are as follows as of July 1:

	<u>2012</u>	<u>2011</u>
Discount rate	4.66 %	6.03 %
Expected return on plan assets	8.00 %	8.25 %
Rate of compensation increase	2.00% - 3.00%	2.50% - 3.00%

The rate of compensation increase was 2.00% for fiscal 2013, 2.50% for fiscal year 2014 and 3.00% thereafter. The expected rate of return on plan assets assumption was developed based on historical returns for the major asset classes. This review also considered both current market conditions and projected future conditions.

**Plan Assets**

JHH's pension plan weighted average asset allocations as of June 30, 2012 and 2011 by asset class are as follows:

<u>Asset Class</u>	<u>2012</u>	<u>2011</u>
Cash equivalents	4.9%	4.5%
Equities and equity funds	30.2%	35.8%
Fixed income funds	26.3%	15.6%
Alternative investments	38.6%	44.1%
Total	<u>100.0%</u>	<u>100.0%</u>

The Plans assets are invested among and within various asset classes in order to achieve sufficient diversification in accordance with JHH's risk tolerance. This is achieved through the utilization of asset managers and systematic allocation to investment management style(s), providing a broad exposure to different segments of the fixed income and equity markets. The Plans strive to allocate assets between equity securities (including global asset allocation strategies) and debt securities at a target rate of approximately 75% and 25%, respectively.

**Fair Value of Plan Assets**

Fair value is the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participant at the measurement date. The three-tier hierarchy prioritizes the inputs used in measuring fair value as follows:

- Level 1 – Observable inputs such as quoted market prices for identical assets or liabilities in active markets;
- Level 2 – Observable inputs for similar assets or liabilities in an active market, or other than quoted prices in an active market that are observable either directly or indirectly; and
- Level 3 – Unobservable inputs in which there is little or no market data that require the reporting entity to develop its own assumptions. There were no financial instruments requiring Level 3 classification at June 30, 2012 and 2011.

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The following table presents the plan assets carried at fair value as of June 30, 2012 and 2011 grouped by hierarchy level (in thousands):

As of June 30, 2012:

Assets	<u>Total Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>
Cash equivalents (1)	\$ 29,477	\$ -	\$ 29,477
Equities and equity funds (2)	181,181	14,295	166,886
Fixed income funds (3)	157,563	139,116	18,447
Alternative investments (4)	<u>231,016</u>	<u>-</u>	<u>231,016</u>
Totals	<u>\$ 599,237</u>	<u>\$ 153,411</u>	<u>\$ 445,826</u>

As of June 30, 2011:

Assets	<u>Total Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>
Cash equivalents (1)	\$ 23,943	\$ -	\$ 23,943
Equities and equity funds (2)	192,793	-	192,793
Fixed income funds (3)	83,991	77,148	6,843
Alternative investments (4)	<u>237,375</u>	<u>-</u>	<u>237,375</u>
Totals	<u>\$ 538,102</u>	<u>\$ 77,148</u>	<u>\$ 460,954</u>

- (1) Cash equivalents include investments with original maturities of three months or less and overnight investments. Cash equivalents are carried at amortized cost which approximates fair value which renders them level 2.
- (2) Equities include individual equities. Equity funds include investments in mutual funds, commingled trusts and hedge funds. The individual equities and mutual funds are valued based on the closing price on the primary market and are rendered level 1. The commingled trusts and hedge funds are valued regularly within each month utilizing NAV per unit and are rendered level 2.
- (3) Fixed income funds are investments in mutual funds and commingled trusts investing in fixed income instruments. The underlying fixed investments are principally U.S. Treasuries, corporate bonds, commercial paper, and mortgage backed securities. The mutual funds are valued based on the closing price on the primary market and are rendered level 1. The commingled trusts are valued regularly within each month utilizing NAV per unit and are rendered level 2.
- (4) Alternative investments include investments that are not traded on national exchanges or over-the-counter markets. These investments are valued at using a net asset value per share that has been calculated in accordance with investment company rules, which among other things, indicates that the underlying investments be measured at fair value. This valuation technique renders these investments level 2.

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The following table displays information by major alternative investment category as of June 30, 2012 (in thousands):

<b>Description</b>	<b>Fair Value</b>	<b>Liquidity</b>	<b>Notice Period</b>	<b>Receipt of Proceeds</b>
Global asset allocation	\$106,058	Monthly	5 to 30 days	(1)
Fund of funds	47,982	Quarterly	45 days	(2)
Hedge funds	51,075	Mthly, qtrly or bi-annually	30 to 90 days	(3)
Credit funds	18,712	Annually	60 to 90 days	(4)
Distressed credit	7,189	December 31, 2013		(5)
Total	<u>\$ 231,016</u>			

- (1) At least 95% within 15 days, remaining within 30 days of redemption date
- (2) At least 90% within 60 days, remaining received after the audit or as SPV shares
- (3) 90% - 95% within 30 days, 5% - 10% after annual audit
- (4) Within 30 days, or 90% within 10 days, 10% after annual audit
- (5) Locked up until December 31, 2013

The following table displays information by major alternative investment category as of June 30, 2011 (in thousands):

<b>Description</b>	<b>Fair Value</b>	<b>Liquidity</b>	<b>Notice Period</b>	<b>Receipt of Proceeds</b>
Global asset allocation	\$103,931	Monthly	5 days	(1)
Fund of funds	74,126	Mthly, qtrly or annually	30 to 65 days	(2)
Hedge funds	27,695	Monthly or quarterly	30 to 65 days	(3)
Credit funds	21,327	Annually	60 to 90 days	(4)
Distressed credit	10,296	December 31, 2013		(5)
Total	<u>\$ 237,375</u>			

- (1) Within 15 days
- (2) Within 5 days, or 90% within 30 to 60 days, 10% after annual audit
- (3) 95% within 30 days, 5% after annual audit
- (4) Within 30 days, or 90% within 10 days, 10% after annual audit
- (5) Locked up until December 31, 2013

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**Contributions and Estimated Future Benefit Payments (Unaudited)**

JHH expects to contribute \$56.5 million to its pension plan in the fiscal year ending June 30, 2013.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid in each of the following fiscal years as of June 30, 2012 (in thousands):

2013	\$	23,509
2014		26,364
2015		29,365
2016		32,593
2017		35,872
2018 -- 2020		235,181

**11. Maryland Health Services Cost Review Commission (“Commission” or “HSCRC”)**

JHH’s charges are subject to review and approval by the Commission. JHH management has filed the required forms with the Commission and believes JHH is in compliance with Commission requirements. The total rate of reimbursement for services to patients under the Medicare and Medicaid programs is based on an agreement between the Center for Medicare and Medicaid Services and the Commission. Management believes that this program will remain in effect at least through June 30, 2013. Effective April 1, 1999, the Commission developed a methodology to control inpatient hospital charges and JHH elected to be paid under the new methodology. The methodology established a charge per admission cap for each hospital. The hospital specific charge per admission is adjusted annually to reflect cost inflation, and is also adjusted for changes in the hospital’s case mix index. Certain highly tertiary inpatient cases such as solid organ transplants, bone marrow transplants and certain oncology cases are treated as exclusions from the charge per case methodology. Effective July 1, 2011, the Commission modified this methodology in an effort to reduce readmissions at Maryland hospitals. Under a Charge per Episode (“CPE”) methodology, hospitals are allowed to retain any rate authority lost due to reductions in readmissions. Conversely, hospitals are not granted any additional rate authority for any increases to readmissions.

In addition to the HSCRC annual rate update, JHH’s management successfully negotiated a prospective rate setting agreement effective July 1, 2004 to provide annual rate increases through fiscal year 2010 for capital costs related to the planned east Baltimore campus redevelopment project. JHH received a certificate of need (“CON”) from the Maryland Health Care Commission for this project which is a condition required by the HSCRC. This capital cost rate increase will increase JHH’s annual approved rate base by approximately \$39.3 million beginning with the opening of the new hospital facilities on May 1, 2012.

In fiscal 2011, the HSCRC implemented a new methodology to establish a charge per visit (“CPV”) for certain types of outpatient services. The hospital specific charge per visit is adjusted annually to reflect cost inflation and is also adjusted for changes in case mix. This methodology is primarily focused on ambulatory surgery procedures, medical clinic visits and emergency room visits. The methodology also includes other types of outpatient services including infusion procedures, therapies, mental health and major radiology procedures. Certain types of visits such as radiation therapy, psychiatric day hospital and certain types of recurring visits will be treated as exclusions under this methodology. In March 2012, the HSCRC voted to suspend the CPV methodology for fiscal 2012. The HSCRC has not yet provided a timeline for the establishment of a replacement methodology. It is expected that some type of outpatient constraint system will be put in place sometime during fiscal 2013.

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The Commission approves hospital rates on a departmental unit rate basis. Individual unit rates are the basis for hospital reimbursement for inpatient excluded cases and for hospital outpatient services. Under the Commission rate methodology, amounts collected for services to patients under the Medicare and Medicaid programs are computed at approximately 94% of Commission approved charges. Other payors are eligible to receive up to a 2.25% discount on prompt payment of claims.

**12. Professional and General Liability Insurance**

JHU, JHHS and its affiliates participate in an agreement with four other medical institutions to provide a program of professional and general liability insurance for each member institution. As part of this program, the participating medical institutions have formed a risk retention group ("RRG") and a captive insurance company to provide self-insurance for a portion of their risk.

JHH and JHU each have a 10% ownership interest in the RRG and the captive insurance company. This ownership interest is included in investments on the Balance Sheets. The medical institutions obtain primary and excess liability insurance coverage from commercial insurers and the RRG. The primary coverage is written by the RRG, and a portion of the risk is reinsured with the captive insurance company. Commercial excess insurance and reinsurance is purchased under a claims-made policy by the participating institutions for claims in excess of primary coverage retained by the RRG and the captive. Primary retentions are \$5.0 million per incident. Primary coverage is insured under a retrospectively rated claims-made policy; premiums are accrued based upon an estimate of the ultimate cost of the experience to date of each participating member institution. The basis for loss accruals for unreported claims under the primary policy is an actuarial estimate of asserted and unasserted claims including reported and unreported incidents and includes costs associated with settling claims. Projected losses were discounted at .73% and 1.2% for June 30, 2012 and 2011, respectively.

Professional and general liability insurance expense incurred by JHH was \$16.0 million and \$23.7 million for the years ended June 30, 2012 and 2011, respectively, and are included in purchased services expense in JHH's Statements of Changes in Net Assets. Professional and general liability insurance reserves recorded in JHH's balance sheets at June 30, 2012 and 2011 were \$86.0 million and \$41.2 million, respectively.

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**13. Transactions with Related Parties**

During the years ended June 30, 2012 and 2011, JHH engaged in transactions with JHHS and its affiliates, all related parties: Johns Hopkins Bayview Medical Center, Inc. ("JHBMC"), Johns Hopkins Medical Services Corporation ("JHMSC"), Johns Hopkins Community Physicians ("JHCP"), Johns Hopkins Medical Management Corp. ("JHMMC"), Johns Hopkins Employer Health Programs, Inc. ("EHP"), Johns Hopkins HealthCare, LLC ("JHHC"), Johns Hopkins Home Care Group, Inc ("JHHCG"), Central Maryland Heart Center, Dome Corporation, Howard County General Hospital ("HCGH"), Priority Partners Managed Care Organization, Inc. ("Priority Partners"), JHMI Utilities, LLC, and Suburban Hospital Healthcare System ("SHHS"). The following is a summary of related party transactions and balances:

	<u>2012</u>	<u>2011</u>
<u>Revenue/(expense) transactions (in thousands):</u>		
Purchasing, legal, advertising and other services provided by JHHS	\$ (82,277)	\$ (83,124)
Cost recoveries for laboratory and various services provided to JHBMC	14,460	14,153
Cost recoveries for laboratory services provided to HCGH	7,382	7,449
Cost recoveries for laboratory and various support services provided to JHCP	253	275
Contribution to JHCP for services provided by JHCP to uninsured patients	(2,687)	(2,712)
Temporary staffing services provided by JHMMC	(14,153)	(14,746)
Premiums paid to EHP for administration of health care claims	(5,428)	(5,215)
Net patient services revenue from providing services to subscribers of JHHC	53,044	38,663
Cost recoveries for fringe benefit and various support services from JHHCG	16,658	13,807
Net patient service revenue from providing services to subscribers of Priority Partners	105,656	111,813
Utility and telecommunication services provided by JHMI Utilities, LLC	(26,754)	(25,204)

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	<u>2012</u>	<u>2011</u>
<u>Due (to)/from related party balances as of June 30 (in thousands):</u>		
Due from JHHS for services provided and funding for strategic initiatives and swap collateral	\$ 126,036	\$ 49,376
Due from JHBMC for laboratory and various support services	1,077	1,267
Due from JHMSC for notes receivable	307	614
Due to JHCP for support services	(255)	(99)
Due from JHHCG for fringe benefits and patient receivables from operation of discharge pharmacies	535	(1,167)
Due from JHHC for services to patients and financing costs	12,801	169
Due from JHMI Utilities LLC for utility and network service and capital costs	25,668	(407)
Due from HCGH for support services	111,161	267
Due from SHHS for support services	99	39
Other	<u>(1,926)</u>	<u>(1,324)</u>
Total	<u>\$ 275,503</u>	<u>\$ 48,735</u>

Included in the amounts due from affiliates in the accompanying Balance Sheets as of June 30, 2012 and 2011 are \$.3 and \$.6 million, respectively, in a note receivable from JHMSC. The note receivable bears no interest with annual payments from JHMSC of \$307 thousand.

Broadway Services, Inc. ("BSI"), a related organization, is a wholly-owned subsidiary of the Dome Corporation. The Dome Corporation is owned equally by JHHS and JHU. BSI provides JHH with various services including security, housekeeping, escort and transportation. During 2012 and 2011, JHH incurred costs of approximately \$12.1 and \$10.3 million, respectively, for these services.

In March 2012, JHH and HCGH entered into a short-term Promissory Note ("Affiliate Note") under which JHH loaned \$110.6 million to HCGH. The Affiliate Note carried an interest rate of 2.75% and principal and accrued interest was due on May 31, 2012, or upon an earlier long-term extension of the Affiliate Note. In May 2012, the Affiliate Note was extended, and has a final due date of July 1, 2033. The Affiliate Note carries an interest rate that resets annually and varies from 4.11% to 4.82%, and is payable semi-annually. Principal payments are due on July 1 of each year and range from \$700 thousand in 2013 to \$7.2 million in 2034.

**14. Contracts, Commitments and Contingencies**

JHH has agreements with JHU, under which JHU provides medical administration and educational services, patient care medical services, and certain other administrative and technical support services through the physicians and interns employed by JHUSOM. Compensation for providing medical administration, educational services and other support services is paid to JHU by JHH; compensation for patient care medical care services is derived from billings to patients (or third-party payors) by JHU. The aggregate amount of purchased services incurred by JHH under these agreements was \$194.7 million and \$197.4 million for the years ended June 30, 2012 and 2011, respectively.

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JHH had non-cancellable commitments under construction contracts of \$73.0 million and \$238.2 million at June 30, 2012 and 2011, respectively, relating primarily to its campus redevelopment project which includes the construction of a new Cardiovascular and Critical Care Adult Tower and a Children's Hospital.

Commitments for leases that do not meet the criteria for capitalization are classified as operating leases with rentals charged to operations as incurred.

The following is a schedule by year of future minimum lease payments under all operating leases as of June 30, 2012, that have initial or remaining lease terms in excess of one year (in thousands).

2013	\$4,756
2014	4,683
2015	2,389
2016	2,299
2017	2,042

Rental expense for all operating leases for the years ended June 30, 2012 and 2011 amounted to \$12.4 million and \$14.0 million, respectively.

In 2005, JHH and JHU created a Limited Liability Company (JHMI Utilities, LLC) to provide utility and telecommunication services for their East Baltimore Campus. Each member owns 50% of the LLC and shares equally in the governance of the LLC. The existing JHH utility assets have been transferred at cost to the LLC. The LLC has also assumed the liability for the JHH's 1985 Pooled Loan obligation of \$8.5 million. The cost of acquiring and upgrading the existing utility facilities, the construction of a new power plant and an upgrade of the telecommunication system have been financed through the issuance of tax exempt bonds by MHHEFA and the proceeds of the Pooled Loan program sponsored by MHHEFA. JHH and JHU have guaranteed the total debt issued by MHHEFA. At June 30, 2012 the amount of debt guarantees by JHH was \$44.6 million. JHH records its investment in JHMI Utility LLC under the equity method of accounting.

During the year ended June 30, 2006, JHH recorded asset retirement obligations associated with the abatement of asbestos in several buildings that were constructed prior to 1980. The fair value of the estimated asset retirement obligations as of June 30, 2012 and 2011 was \$18.2 million and \$17.7 million, respectively.

The change in the asset retirement obligation for the year ended June 30, 2012 consisted of the following (in thousands):

Retirement obligation at beginning of year	\$ 17,743
Liabilities settled	(79)
Accretion expense	564
Retirement obligation at end of year	<u>\$ 18,228</u>

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JHH has pledged investments having an aggregate market value of \$24.5 million and \$23.7 million as of June 30, 2012 for JHHS compliance with regulations of the Workers Compensation Commission and the Department of Economic and Employment Development's Unemployment Insurance Fund. These investments are included in assets whose use is limited by board of trustees in the Balance Sheet

**15. Functional Expenses**

The Hospital provides general health care services to residents within its geographic location as well as to national and international patients. Expenses related to providing these services for the years ended June 30 consisted of the following (in thousands):

	<u>2012</u>	<u>2011</u>
Health care services	\$ 1,475,868	\$ 1,412,985
General and administrative services	230,804	216,536
Total expenses	<u>\$ 1,706,672</u>	<u>\$ 1,629,521</u>

**16. The Johns Hopkins Hospital Endowment Fund, Incorporated**

The Endowment Corporation was organized for the purpose of holding and managing the endowment and certain other funds transferred from and for the benefit of JHHS and affiliates. The affairs of the Endowment Corporation are managed by a Board of Trustees, comprised of Trustees who are self-perpetuating. Neither JHHS nor any affiliate holds legal title to any Endowment Corporation funds. The Endowment Corporation's distributions from net assets to JHH were \$8.2 million and \$8.8 million in the years ended June 30, 2012 and 2011, respectively, and were recorded as other revenue. The Board of Trustees may, at its own discretion, award funds from the Endowment Corporation to organizations other than JHHS or its affiliates if the Board of Trustees determines that doing so is for support, benefit, or in furtherance of the mission of JHHS. Accordingly, these amounts are not presented in the financial statement of JHH until they are subsequently distributed to JHH from the Endowment Corporation. The Endowment Corporation's net assets were \$547.2 million and \$553.2 million as of June 30, 2012 and 2011, respectively.

**17. Subsequent Events**

In August 2012, JHH issued \$84.6 million and \$85.1 million of Revenue Bonds, Series 2012C and Series 2012D, respectively. These bonds were issued to refund the JHH Series 2008E and Series 2008F Commercial Paper, and are due in 2038. The 2012C Bonds are subject to mandatory sinking fund installments ranging from \$260 thousand to \$8.7 million. The 2012D Bonds are subject to mandatory sinking fund installments ranging from \$325 thousand to \$8.7 million. The 2012C Bonds and 2012D Bonds are variable rate bonds, and carry a mandatory purchase date of November 15, 2017. The 2012C Bonds and 2012D Bonds pay interest monthly based on 67% of LIBOR plus a spread of 0.83%. The interest rate is reset on the first business day of each month. Subsequent events have been evaluated by management through September 28, 2012, which is the date the financial statements were issued.